ICRC

independent competition and regulatory commission

ICRC response to Issues Paper

Grant Review of the ACT's Water and Sewerage Pricing Framework

15 December 2014

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We have responsibilities for a broad range of regulatory and utility administrative matters. We have responsibility under the Independent Competition and Regulatory Commission Act 1997 (ICRC Act) for regulating and advising government about pricing and other matters for monopoly, near-monopoly and ministerially declared regulated industries, providing advice on competitive neutrality complaints and government- regulated activities. We also have responsibility for arbitrating infrastructure access disputes under the ICRC Act. In discharging our objectives and functions, we provide independent robust analysis and advice. Our objectives are set out in section 7 of the ICRC Act and section 3 of the Utilities Act.

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1 Preamble

Under the Independent Competition and Regulatory Commission Act 1997, the Commission is constituted by its Commissioners. At the present time these are Malcolm Gray and Mike Buckley. To avoid excessive formality in this document, we make frequent use of the personal pronouns "we" and "us". Wherever this occurs, it should be understood as synonymous with Gray and Buckley or the Commission. At some points we need to distinguish between the Commission as constituted under the Act and the "Commission" taken to mean the organisation as a whole, including our staff. We use "Commission" exclusively to refer to the former and "ICRC" to refer to the latter.

Unless specifically requested to, for example in a terms of reference, the Commission does not generally give policy advice. Given the subject matter of the review to which this is a submission, it would be particularly inappropriate for us to offer such advice in this case. The reviewer has, however, requested that we make a submission to this review. The approach we have taken, therefore, is to draw on our experience and knowledge of related inquiries elsewhere to bring relevant matters to the attention of the review and, on occasion, to suggest that certain initiatives that may be worthy of attention in the review.

2 Approach of this submission

The issues raised by the terms of reference and in the issues paper vary from the very broad to the quite specific. In addition, some of the questions arising from the terms of reference and posed in the issues paper raise other wider issues. For example, the issues paper asks:

> Does it remain appropriate, on a cost effectiveness basis, for the ACT Government to maintain its own independent pricing authority?

In order to answer this question it is necessary to answer a range of consequential questions such as:

- What other function besides setting water and sewerage services prices does the independent pricing authority perform?
- Should these functions continue to be performed?
- If yes, who is to perform them?
- What would be the overall cost of performing the required functions, including the pricing of water and sewerage services, in the absence of the Territory's independent pricing authority?

Answering the first question is a straightforward matter; answering the rest is not.

In order to respond to the terms of reference and issues paper in a coherent fashion, we have ordered the issues in a hierarchical fashion through a series of questions. In doing this it becomes apparent that some lower level issues only become relevant if particular answers are given to higher level issues. For example, the questions in relation to the current or potential future operations of the ICRC only become relevant if a positive answer is given to the question in the box above.

Our hierarchical questions are:

Does the ACT wish to retain its policy of the price of water and sewerage services being determined by an entity independent of government?

- If no, what alternative method should be adopted?
- If yes, does the ACT wish to retain its own regulatory agency to make this determination?
    - If no, who should perform this function?
    - If yes, how can the functioning of the determination process be improved? In particular
        - How can the costs of undertaking the water and sewerage services determination be reduced?
        - Can the governance of the entities participating in the determination process be improved to increase the effectiveness and efficiency of the process?
        - Is there a role for protocols or principles in relation to the water and sewerage services pricing process?
            - If so, who should formulate them and how should they be enshrined?
        - Can the legislative framework within which the independent agency operates be improved? In particular in its statement of
            - the objectives of the review process;
            - the balance between and the priority to be given to the various objectives;
            - the requirements applying to a draft report;
            - the process to be employed in undertaking a review of a pricing determination.

This submission addresses each of these areas in turn, based on the Commission's experience over the last three and three quarter years. In doing so, we identify the options that are available to address them.

3 An independent entity?

Australia has a long history of establishing institutions which allow for decisions to be taken and functions exercised independent of executive government. The courts are the clearest examples of this but there are also many specialist tribunals. In the economic sphere the RBA has been given responsibility for the implementation of monetary

policy though its setting of the cash rate. The rationale for this encompasses the need for decisions to be taken on their technical merits given the circumstances prevailing and away from political considerations.

3.1 Alternatives

The question of whether the Territory should have the prices of water and sewerage services set by an entity that is independent of government is not one to be passed over lightly. Although this is the approach that has been taken in the ACT since the incorporation of ACTEW in 1995, it is by no means the only approach that can be taken. There may be circumstances in which the policy adopted is to subsidise the price of water and sewerage services, with the quantum of the subsidy being set on a year by year basis in the budget process. Alternatively, the government may take the view that the profits made from the supplying water and sewerage services is a legitimate source of revenue and the rate of profit should be determined along with other tax rates in setting taxation policy.

A third possibility is that the entity supplying the service sets the price, subject to some kind of price monitoring arrangement. The recent Productivity Commission report on urban water pricing advocated that governments move towards such an arrangement.[1] Queensland has system where the QCA assesses prices proposed by water utilities against benchmark prices set by QCA. In Victoria, the government, through the Governor in Council, makes a Water Industry Regulatory Order.[2] The Victorian Essential Services Commission must then approve plans submitted by the various water authorities where it is satisfied that the plan meets the Order.

The principal weakness in these sorts of approaches is in specifying what should happen if the monitoring authority detects some problem with the prices being charged, for example, that they exceed a benchmark. In Queensland, for example, no action is specified so it is difficult to see how the scheme could be effective in restraining the use of any market power that may exist. Another example is provided by the arrangement under which the ACCC monitors the performance Australia's major airports, including in regard to the fees charged. In its 2011 review of the economic regulation of airport services, the Productivity Commission noted that:

> Fundamental to the effectiveness of the light-handed approach is the credible threat of sanction for airports that abuse their market power.

[1] Productivity Commission Inquiry Report, No.55, Australia's Urban Water Sector (2011) see http://www.pc.gov.au/inquiries/completed/urban-water/report.

[2] Review of Victoria's Framework for Economic Regulation of the Water Sector Gilbert + Tobin (2014).

and concluded that such a credible threat did not exist at that time in the airport monitoring regime[3].

It is beyond the scope of this submission to survey the advantages and disadvantages of the various alternative price setting frameworks. The most influential single document in the Australian policy debate is the Hilmer report. [4] More recently, the issues have been examined in the previously mentioned Productivity Commission report. Victoria is currently conducting a Water Review to address what the Victorian Government perceives as an overly complex and outmoded regulatory framework in order to increase efficiency both in terms of the governance of water businesses as well as the regulatory framework.[5] The Water Services Association of Australia recently released a position paper and report commissioned from Frontier Economics on improving economic regulation of urban water.[6] The balance of this submission will only address the issues that may arise once a policy decision to have prices set by an independent agency is taken.

3.2 Requirements for independence

Since the Hilmer review in 1993, there has been a general tendency in the water sector to avoid the above alternatives and to have prices set by an entity that is independent of government. It needs to be recognised, however, that adopting this option entails obligations to the independent entity that may not always be attractive to government.

- If an entity is to be truly independent, it needs:
- Its independence enshrined in an appropriate statute
- Adequate and unconditional funding
- Protection for undue influence
- Any mechanism for the review of its decision to be structured to maintain the integrity of the decision making process overall.

The work of the OECD Best Practice Principles for Regulatory Policy program has provided guidance on how this should be done.[7] In Australia, the Productivity Commission has provided guidance on the auditing of independent agencies.[8]

[3] Economic Regulation of Airport Services, Productivity Commission Inquiry Report No. 57, 14 December 2011.

[4] National Competition Review, Commonwealth of Australia 1993.

[5] Living Victoria, Strategy Plan, 2013, p 79.

[6] See www.wsaa.asn.au/WSAAPublications/Documents/Position Statement on Improving Economic Regulation.pdf and www.wsaa.asn.au/WSAAPublications/Documents/Report - Improving Economic Regulation of Urban Water.pdf. There is also a large technical literature addressing this and related issues.

[7] For a relevant, recent piece of work to emerge from this program, see www.oecd-ilibrary.org/governance/the-governance-of-regulators_9789264209015-en.

We look at each of these requirements in turn. The adequacy of the arrangements for ICRC against these criteria is discussed below.

Legislation

Independence needs to have a legislative basis. The entity should be autonomous, in Australia the usual form would be a statutory corporation. Executive government should be explicitly denied the power to direct the entity. Whether the entity can instigate investigations of its own volition will depend on the functions it is given. The important principle is that once the entity has a matter under consideration, including through reference by government, it should be unfettered, within the limits of applicable legislation, to make its own determination on the matter.

Funding

An institution can have statutory independence but to be effectively independent it also needs to have the financial resources necessary to be able to carry out its functions. Where an institution depends on funding from central government the budget appropriation process can influence the activities an institution can undertake and the way it can perform those functions even where they have statutory independence.

A partial answer may be to allow the entity to recover the costs of its regulatory activity from the regulated entities. Such a mechanism needs to include safeguards to endure that only relevant costs are recovered and that the independent entity only recovers the efficient costs of its regulatory activity. There will, however, be tasks that it is desirable or required for the independent entity to undertake that cannot be cost recovered. Examples might include research into regulatory approaches, interaction with other regulations, preparation of an annual report and appearance before the legislature or its committees. This suggests that a mixture of budget funding and cost recovery may be desirable.

Protection from undue influence

Pressure can be brought to bear on an independent entity in a variety of ways. It needs to be protected from all sources of undue influence that do or threaten to interfere with the independent exercise of its statutory functions. Funding is a source of such influence has been discussed above. It is likely that the independent entity will be much smaller than many of the entities it is charged with regulating. Safeguards need to ensure that such resource asymmetries cannot provide a means of exerting undue influence.

If the independent entity is a government agency, the requirements placed on it and the administrative arrangements under which it operates as a result of this status must not be such as to interfere with the independent exercise of its powers. It must, for

[8] See http://www.pc.gov.au/__data/assets/pdf_file/0005/134780/regulator-audit-framework.pdf.

example, have administrative control of its staff. To the extent that its senior staff have reporting obligations outside the entity, these must be carefully managed.

The independent entity must, of course, manage itself and its affairs in such a way as to avoid creating channels through which undue influence may be exercised.

Review process

While it is generally desirable for there to be a process by which an aggrieved party can seek a review of a determination of the independent-entity, the grounds for and process of review must be carefully designed to protect the integrity of the decision making processes of the independent-entity. The grounds for review should essentially be that there has been an error on the part of the independent-entity. The review body should be required to establish that such an error has been made before it moves to consider action to amend the determination of the independent-entity.

The review body should be manifestly competent to consider matters likely to be referred to it. It should be entirely independent of the independent-entity and all those with an interest in the outcome of the review process. The review body's processes should be transparent and possess a high degree of integrity. In a small jurisdiction it may only be possible to secure these attributes by using a review body outside the jurisdiction.

3.3 Conclusion

The decision about whether to use an independent entity to set prices is a threshold decision that needs to be taken in full knowledge of the consequences of the choice made. If prices are to be set by an independent-entity, the government must be prepared to fulfil all the requirements necessary to ensure that the entity is able to be truly independent.

4 An ACT regulatory agency?

The decision as to whether the ACT should have its own regulatory agency to handle the determination of water and sewerage services prices should be made on the grounds of the cost effectiveness of the alternatives. Since the ACT currently has its own regulatory agency responsible for determining the price of water and sewerage services, the decision becomes one of deciding whether that function should continue to be discharged by that agency or whether alternative arrangements should be put in place.

To make the necessary comparison two cost estimates are required: the cost of the current arrangements and the cost of the most cost effective alternative arrangement that can be devised. Formulating these estimates is clearly beyond the scope of this submission. We can, however, offer some observations about factors that should be taken into account in devising them.

4.1 Current arrangements

One of the major purposes of this review is to identify ways to improve the cost effectiveness of the current arrangements. It is clearly the cost of the current arrangements after any of these identified improvements have been made that ought to be considered. Suggestions for reducing the costs of the current arrangements can be found at pages 31-33. Suggestions for addressing the problems of scale, overhead and cyclical workload in the current arrangements can be found at pages 26-29.

4.2 Alternative arrangements

In devising alternative arrangements there are two basic options: remove the responsibility for determining water and sewerage services prices form the ICRC, but otherwise leave its functions and responsibilities unchanged, or disestablish the ICRC and reallocate or discontinue all its functions and responsibilities.

The first option is unattractive because removing a major function for the ICRC would exacerbate many of the problems that increase the costs of operating the agency. Even if a suitable candidate could be found to take on the task of making the water and sewerage services determination, it is unlikely that the savings made would be sufficient to compensate for the loss in cost effectiveness of the residual ICRC.

Developing a proposal based on the second option requires a number of questions to be answered, including:

- Which functions should be discontinued and which reallocated to others to discharge?
- Which entities should take on the functions to be reallocated ?

The central question in pursuing either option is: Which entity should take on the responsibility of determining the prices of water and sewerage services? There is no other entity in the ACT with the required expertise and structure. The courts have the right structure, but lack the required expertise and are not well suited to discharging such a responsibility. None of the agencies in which relevant expertise resides, such as the Treasury, have the right structure, that is, they are not independent of government. This means the Territory would have to make some kind of inter-governmental agreement or contracting out arrangement to secure the services of an entity outside the Territory to perform the function.

Any such arrangement would need to be structured very carefully to ensure that, in discharging the function, the entity was and was seen to be operating independently of the ACT government. For example, if IPART in NSW were contracted to perform the function, the fact that IPART might be considered to operate independently of the NSW government in performing its functions in NSW would offer no guarantees that it would operate independently of the ACT government when discharging a function under a contract with the ACT government. Such an arrangement may result in

unintentional jurisdictional and territorial power issues, with the ACT government in effect ceding power to a state. It might well prove challenging to construct a contracting out arrangement that offered the same assurance of independence as a properly constructed, independent statutory authority in the ACT.

In addition to making determinations of water and sewerage services prices, the Commission also makes periodic determinations and annual resets of the regulated retail prices for electricity. The ICRC also performs a number of other tasks on a regular basis, this includes monitoring and reporting annually on the performance of the licensed water and the electricity and gas energy networks. This task has recently been streamlined and forms part of the ICRC's annual report. It also approves, on an annual basis, the standard customer contract for ACTEW and ActewAGL Retail (Electricity) to ensure that tariff offerings are consistent with the current price direction.

In recent years the ICRC has also been producing a number of monitoring reports for the Environment and Planning Directorate in relations to greenhouse gas emissions and the use of renewable energy in the ACT. This work is complementary to the quarterly reports on the installation of photo voltaic generators, the output of electricity from these micro-generators and the payments made for the electricity produced from them under the ACT's Feed-in tariff scheme.

In addition the ICRC has to be able to respond to inquiries relating to competitive neutrality complaints where an ACT business is concerned that a government business has an unfair advantage stemming from its government ownership. The competitive advantage generally relates to the fact that the government business does not have to set its prices so as to be profitable whereas a private business cannot operate if it is not profitable. The ICRC does not get a large number of these inquiries and our experience is that once the applicant learns that that they must fund the cost of the ICRC's investigation the inquiry does not proceed. Nonetheless, the ICRC has to be in a position to receive the complaint, conduct an initial review to see if an investigation is warranted, and to advise the applicant of the ACT's policy in relation to competitive neutrality.

Clearly these functions discharged by the ICRC have been grouped together for a reason. There are synergies between the licensing work the ICRC undertakes under the *Utilities Act 2000* and its price determinations for retail electricity and water and sewerage services. This allows the ICRC to assist government with advice on the regulation of utilities and their performance. There are also synergies between regulating retail electricity prices and reporting on the feed in tariff schemes, described above. If the ICRC is disestablished, either these functions will need to discontinued or a new agency identified to undertake them. If this leads to these functions being dispersed, these synergies will be lost.

4.3 Conclusion

Any identified improvements in the current arrangements should be implemented or their likely impact allowed for in making any comparison with the costs of an alternative arrangement.

Before moving to change the current arrangements a complete, a viable alternative should be developed. Any comparison of cost effectiveness should include consideration of all the ramifications and associated costs of the alternative.

5 Improving the functioning of the water and sewerage services price determination process

Before moving to consider how the water and sewerage services price determination process can be improved, it is important to note that we are not dealing with a dysfunctional system that is incapable of discharging its functions.

As part of the Victorian Review, mentioned earlier, Deloitte prepared a report, which provides an overview of the framework and approaches taken by Australian Economic Regulators in the water sector[9]. With some important caveats, which will be considered later, the report indicates that the approach taken by the Commission to determine ACT water and sewerage service prices is broadly comparable to that taken in other jurisdictions. The comparative study prepared by Deloitte highlights the similarities and differences between the approaches taken by regulators. This study showed that for regulatory decisions made in 2012-13, the Commission's procedural arrangements are consultative and comprehensive but that the decision also took the longest time period to complete.

Separately and in preparation for the 2015-16 biennial recalibration, we have reviewed ACTEW's 2013-14 statutory accounts[10]. This indicates that the current price direction is performing as anticipated. That is ACTEW's water and sewerage services business remains financially viable, in fact, is in a stronger financial position than it was in 2012-13. ACTEW's total revenues were higher than forecast. This is also consistent with the intent of the Price Direction, which anticipated that water sales and, consequently, ACTEW's revenues would be higher should the summer prove warmer and dryer than we had forecast. Our forecast was intentionally conservative to ensure that should the weather have proved wetter and cooler than anticipated, ACTEW's

[9] Comparison of Water Regulatory Approaches Final Report April, Deloitte (2014).

[10] On 28 October 2014, ACTEW Corporation Ltd changed its name to Icon Water Limited. For the period covered by the events of this review and in all the documents relevant to it, the corporation was known by its former name. This submission will follow the issues paper and use the name "ACTEW" to refer to the legal entity now called Icon Water Limited.

revenues would still have been sufficient to allow it to discharge its financial obligations.

The outcome of the 2013 price direction will be assessed more thoroughly in the biennial recalibration, but current indications are that the objective of delivering a stable medium-term price path for water and sewerage services while delivering an appropriate target return on equity underpinning is being achieved.

Nevertheless, there is evidence that there is scope for improvement in the cost effectiveness of the process. Following the hierarchy of questions posed at the beginning of this submission, we review four areas for potential improvements:

- costs;
- governance and administration;
- protocols and principles; and
- legislation.

6 Cost of the water and sewerage services price determination process

This section looks first at the total costs incurred by ACTEW and the ICRC. Second, it looks at the reasons why those costs might have been higher than they need have been.

6.1 Total costs

The Issues Paper notes that cost is a central focus of the review, quoting the figures provided by the performance audit of costs of $3.9m for ACTEW and $2.4m for the ICRC. While concluding, without any evidence or analysis to support the conclusion, that this was expensive, the performance audit does not inquire into why the costs were, apparently, above its expectations. This is unfortunate because, without establishing the causes of the unexpectedly high costs, it is difficult to identify effective ways in which they might be reduced.

Questions related to the costs incurred by ACTEW in the review process are largely a matter for the board and shareholders, but we make the following observations. It is difficult to see why the costs of the regulated entity should exceed the costs of the regulator by 62.5 per cent. It is difficult to see how the regulated entity in a review of this kind, in which it had previously participated on a number of occasions, should have incurred $400,000 in legal costs. It is difficult to see why the regulated entity should have found it necessary to engage consultants at a cost of $1.26 million to supply information about its own operations that a well run business would have been providing to its board and senior management anyway.

In regard to the Commission's costs we note that these do not appear to be out of line with costs incurred in similar processes elsewhere in Australia. The Deloitte study, mentioned earlier, also included the results of a survey of the costs incurred by Regulators in conducting a price determination. The survey indicated that regulators incur costs in the order of $1 million to $2.8 million when making a price determination. Deloitte, however, notes that the methodology for estimating costs may not be the same for all submitters and that the result should be considered indicative only.

The Commission advised Deloitte of its costs for undertaking the 2013 ACTEW price determination as at 31 January 2013. At that time the Commission's recorded costs were $1.3m. The actual cost of conducting the price review were, as stated in the Auditor-General's 2014 report, $2.36 m. The Commission's cost included its direct costs, the cost of consultants and a contribution to the Commission's overheads. The Commission is not aware of whether the costs reported by other regulators shown in the table on page 19 of the Deloitte study have been prepared on the same basis or whether they represent the total cost of conducting the review. If the contribution to overheads is removed, the total direct cost of the Commission's water and sewerage services investigation and price determination is $1.3 million.

The Deloitte report makes clear that comparable data on the cost of conducting water pricing determinations made by different regulators is not available. The study suggests, however, that, at a minimum, a price determination by an independent regulator is likely to cost around $1 million to $1.5 million and that this cost will increase depending upon the complexity of the matters which need to be addressed and the length of time the process takes. By way of comparison, in the recent Public Accounts Committee hearings, ACTEW reported that it had made progress payments of $1 million for the Industry Panel review, which has just produced its draft report, and that "the budget that the panel has advised is circa $1.4 million"[11].

6.2 Cost drivers

Regardless of the merits of particular estimates or comparisons, if these costs can be reduced without reducing the effectiveness of the regulatory process it is clearly worth doing so. To this end we offer the following observations. In reviewing our experience of the review process we identify the following factors as increasing the ICRC's costs in ways that might have been avoided[12]:

[11] Legislative Assembly for the ACT Standing Committee on Public Accounts Annual and financial reports 2013 -2014 pages 67-68.

[12] There were other reasons why this review might have been more costly than some others, including the scope of the terms of reference and the complexity and sensitivity of the issues inherited from the previous regulatory period.

- the Commission was poorly prepared to receive the terms of reference for the review of water and sewerage services prices;
- the initial submission from ACTEW did not follow the precedent of its initial submission to earlier reviews of providing a complete business case, including the prices implied by its proposals;
- the second submission from ACTEW differed markedly from the first, causing the Commission to have to repeat much of the analysis it had completed on the initial submission;
- at the stage, in May 2013, when Commissioners were engaged most intensively in resolving the issues necessary to be settled to produce the final report and price direction, they were distracted by the necessity of dealing with the efforts of the Audit Office to commence a performance audit on a process which had not then been completed;
- the length of time taken to complete the review.

6.3 Poorly prepared

The efficiency and effectiveness of the price determination process will in part depend on the nature of the issues the Commission has to address, the institutional memory and analytical capacity the Commission has retained since the last price determination, the ability of the Commission to recruit and manage external experts, the Commission's relationship with the regulated entity, and its overal workload relative to its capacity at the time the reference is received.

The Commission received the terms of reference for the review of water and sewerage services on 13 October 2011. We received terms of reference for a review secondary water on 21 September 2011 and for electricity also on 21 September 2011. Both the latter references were due for completion by mid-2012. Commissioners Gray and Buckley were appointed on 1 March 2011 and took effective control of the Commission when then Senior Commissioner Paul Baxter took extended leave commencing on April 2011 prior to formally retiring in June 2011. It was apparent to the incoming Commissioners that the ICRC did not have the resources, not even the space required to house the staff necessary, to deal with the work required to undertake these three reviews. The delay in publishing the issues paper for the water and sewerage services review commented on in the performance audit report was the result of the prioritised sequencing of tasks that we were forced to adopt in late 2011 and early 2012, while we recruited staff, obtained new office premises and hired a new CEO.

The significance of these observations goes beyond the particular circumstances of 2011-12. This kind of resource crisis in the Commission is a regular occurrence because of the cyclical nature of the Commission's workload combined with its being funded principally through the recovery of its costs. As a consequence, when its workload troughs, the Commission is unable to fund a viable level of staffing. This

means than when its workload picks up the Commission has difficulty in finding the resources to respond. The distinguishing features of 2011-12 were that the preceding trough had been unusually pronounced and the subsequent pickup in activity unusually sharp. These ups and downs in activity and, therefore, funding mitigate strongly against the Commission operating efficiently.

In addition, the prominence given to the Commission has varied markedly over time. The Commission was initially operated on a contract basis out of the offices of PwC with a single Commissioner. The Commission then grew to three Commissioners with its own staff headed up by a senior executive CEO. Subsequent to the Costello review, the Commission was shrunk to a single Commissioner and its CEO downgraded to a SoG A. With the appointments of Gray and Buckley the Commission now has two Commissioners and its CEO has been upgraded to senior executive level.

Although these issues may be seen as beyond the scope of the present review, they are, nevertheless, an essential element in delivering an efficient and effective water and sewerage services pricing process. Their relevance is discussed further below.

6.4 Initial submission from ACTEW

In a water and sewerage services review, ACTEW will typically make two major submissions, one in response to the issues paper and one in response to the draft report. In previous reviews, including that in 2008, ACTEW's initial submission has presented a complete business case for its proposed operations over the coming regulatory period. This complete business case has included projected demands for its services, customer and fixture numbers for sewerage services and the volume of water sales, its proposed operating and capital expenditures over the regulatory period, the revenues it requires to recoup the costs of operating as proposed, and the prices necessary to raise those revenues.[13] In 2012, ACTEW's initial submission did not provide projections of water sales or proposed prices for water. This omission had two consequences.

First, the Commission sought to obtain ACTEW's projected water sales and proposed forecasts. This experience demonstrated that the Commission's power under section 41 of the ICRC Act to obtain information of this kind is, essentially, ineffective, and that the processes involved can be lengthy, contentious and legalistic.

Second, in order to consider the propositions put by ACTEW in its initial submission and to give the ACT community the opportunity to comment on them, the Commission was forced to construct water sales forecasts that seemed broadly consistent with the pattern of operations that ACTEW was foreshadowing and use these to infer the level of water prices that would be required to fund the business plan that ACTEW was putting forward in its initial submission. This was work we had not expected to have to

[13] ACTEW's submission may also include discussion of the form of regulation and other issues falling within the scope of the review.

do and had not allowed for in our planning. In our view, it would have been far more efficient if ACTEW had provided this information in its initial submission, as it had done in previous reviews.

6.5 Differences between ACTEW's first and second submissions

After careful analysis, assisted by a consultant engineer, the Commission concluded that the basis of the operating and capital expenditure proposals in ACTEW's initial submission was not sufficiently robust to allow the us to conclude that they were prudent and efficient. We, therefore, based our draft report and price direction on projected operating and capital expenditures that we constructed based on the historical levels of these expenditures. Our costs through this stage of the review process would clearly have been lower had we been able to have greater confidence in the expenditure proposals put forward by ACTEW.

In response to the criticisms made by the Commission and its consultant, ACTEW provided more rigorously justified operating and capital expenditure proposals in its second submission. While we welcomed this development and largely accepted ACTEW's proposals, it meant that we had, in effect, done two complete evaluation exercises rather than one followed by a fine tuning as would have been the case had the propositions in the initial submission been of the same standard as those in the second submission. As a consequence, our costs again were higher than they otherwise would have been.

6.6 Commencement of the performance audit

On 24 April 2013, the Auditor-General announced that the Audit Office would undertake a performance audit into the water and sewerage services pricing review. The audit was scheduled to commence on 29 April 2013. On the date the audit was scheduled to commence, the Commission was intensively engaged in reviewing submissions received in response to our draft report, including the lengthy one from ACTEW containing much new material, and finalising our position on key issues so that our final report and price direction could be completed. At this point, we were under considerable time pressure to complete the report because of the complexity of the issues to be resolved and the delays and duplications of work that had occurred earlier in the process as described above.

When we received notice of the Audit Office's intention and the implications for the Commission of the proposed start date for the proposed audit, we became concerned. Apart from the apparent impossibility for us and our staff working at the level required to complete the price review on time while meeting the demands of the Audit Office, we were concerned about the implications of the proposed scope and timing of the audit. The degree of disruption caused to the Commissioners' engagement in these crucial final months of the review may be gauged from a letter written by Senior

Commissioner Gray to the Auditor-General, which illustrates the seriousness with which we regarded these developments and the attention that they demanded. This letter is provided as a confidential addition to this submission. For the record, the Commission never received a reply to this letter nor responses to the issues it raised. In consultation on the draft performance audit report in December 2013 , the Auditor-General revealed that her response to our concerns had been to cease attempting to engage with us and instead engage with the "other auditees".

6.7 Length of the process

The Commission issued its final report and price direction on 28 June 2013 so the process of the review had taken 20 months. All of the factors listed above contributed to this. Clearly, the shorter the process, the lower the cost is likely to be. Part of the elapsed time in a review is taken up by allowing stakeholders time to respond to consultative documents produced by the Commission, including the issues paper and draft report. Nevertheless, by adopting some of the suggestions for process improvement identified in section 8, it may be possible to bring the time required for a water and sewerage services back closer to 12 than 20 months.

6.8 Conclusions

Our conclusions from this review of the experience of the 2012-13 investigation are:

- Adequate and stable resourcing are essential to maintaining the independence and effectiveness of the Commission.
- The processes by which the Commission gathered information for the investigation were inefficient. Possible ways of avoiding these inefficiencies are canvassed below.
- While the large cost incurred by ACTEW in participating in the investigation is largely a matter for its board and shareholders, there may be process improvements that could assist in reducing this cost.
- The Commission's costs for a pricing review can clearly be reduced by allowing the Commission to finish its review before attempting to audit its performance in conducting the review.
- Streamlining investigation processes to shorten the elapsed time taken for a review would reduce cost.
- Increased quality of information provided by the regulated entities.

7 Governance and administrative arrangements

By way of background, the Commission notes that the current governance framework broadly accords with framework which developed out of the Commonwealth-State and Territory National Competition Policy reforms of the mid-1990s[14]. Subsequently, the policies and procedures for regulating urban water were made subject to National Water Initiative Principles. As noted above, the Productivity Commission undertook a Review of Australia's Urban Water Sector in 2011.

The ICRC Act provides the generic framework in which the investigation and price determination process is conducted. This accords with the industry-wide approach to competition policy regulation which was advocated in the Hilmer report. The alternative model was an industry specific regulator such as the UK's Office of Water. While Australia has subsequently created the Australian Energy Regulator it is located within the Australian Competition and Consumer Commission.

While the intent of the Hilmer reforms was to establish an economy-wide regulatory framework for the regulation of monopoly service providers, developments since that time have produced industry specific regulatory regimes for both the telecommunications and the energy sectors. Nonetheless, the intent has been to try and maintain consistency in terms of the objective of the regulation e.g. to promote competition in related markets and to intervene in markets only where the benefit exceeds the cost.

The development of industry specific regimes has also been associated with the development of more comprehensive rules based regulatory regimes. In the energy sector a new institution the Australian Energy Market Commission (AEMC) was established with the function of producing the rules under which the AER determined network charges. Associated with the development of more prescriptive rules based regimes regulators such as the AER have been required to produce guidelines setting out the basis on which it conducts its processes and make its determinations.

The principal features of the current governance arrangement are:

- Water and Sewerage Services are delivered by a public company which is owned by the Territory and operated on a day to day basis by management who are accountable to a board appointed by the shareholder.
- The obligation to provide a specific level of water and sewerage services is specified in ACTEW's operating licence which was issued by the ICRC in accordance with the terms of the Utilities Act.

[14] These arose from the Hilmer review mentioned earlier.

- ACTEW is the only entity in the Territory licensed to provide water and sewerage services.
- The price of water and sewerage service prices are determined by an independent regulatory body – the Independent Competition and Consumer Commission in accordance with its legislation. The legislation governing a pricing investigation limits any direction the Minister can require the Commission to take account of in making a price direction.
- The policy framework relating to water security and availability is managed by a responsible minister and their directorate.

Against this background, we look first at the entities involved in the process and their roles, before looking at the governance of each. We then examine the administrative arrangements for conducting an investigation of water and sewerage services prices before offering some concluding remarks.

7.1 Entities and roles

There are four key entities involved in a water and sewerage services price determination process. These are:

- the community;
- the government;
- ACTEW; and
- the ICRC.

The definition and role of each entity is considered below.

Community

The ACT community is the user of ACTEW's water and sewerage services, it is also the beneficiary of any financial surplus returned to the ACT Treasury from ACTEW.

The role of the community is often forgotten in situations where it is not able to express its willingness to pay for a particular level of service as you would in a competitive market. Instead, government mandates service levels through specified service standards. Also, there is not a transparent mechanism for expressing any trade-offs between increased investment in ACTEW's infrastructure and investment in public transport, schools or hospitals. It maybe that ACTEW's ability to raise its own revenue outside of the budget appropriation process means it is better able to compete for investment funds than the providers of these other public goods.

In the ACT, consumers of ACTEW's services are able to participate in the investigation process through submissions to the ICRC, but there is no formal process like the consumer reference group which participates in the Australian Energy Regulator's determination of network charges; nor is there a consumer advocate, as in

the United States, which is funded by government to represent consumers at a rates hearing before a public utility commission.

The ICRC is sometimes viewed as representing the interests of consumers as opposed to ACTEW in a price determination. That view is wrong. While the Commission's ultimate concern is the welfare of the ACT community, it has to address the interests of all the sections of the community and all the interests they might have, not just the narrow and particular interests of consumers of ACTEW's services.

Government

The government has three distinct roles or potential roles relevant to a determination process.

As the shareholder, in trust for the community, it, in consultation with the ACTEW Board which it appoints, is primarily responsible for establishing ACTEW's performance and accountability framework and the oversight of that framework. The performance indicators need to be measurable and relevant to the efficient operation of the business. This means that the Chief Minister and Treasury Directorate need to have the capacity to critically assess ACTEW's performance.

The Commission discussed these roles in chapter 2 of its *Final Report on Regulated Water and Sewerage Services* as part of its consideration of the form of regulation to be applied in its Price Direction. This discussion concluded that the shareholder must take responsibility for the performance of ACTEW while it is the Commission's role to limit ACTEW's and, implicitly, its shareholders' market power.

In addition the government, through the Treasurer who is the minister responsible for the ICRC under the current administrative arrangements orders, provides the reference to the Commission that initiates the process of investigation and reporting which leads to the development and issuing of a price direction for water and sewerage services.

In the event that one of the parties eligible to do so under the ICRC Act lodges an application for review of the Commission's price direction by an industry panel, the Treasurer is also responsible for appointing the members of that panel.

ACTEW

In this context ACTEW's role is to deliver water and sewerage services on an efficient basis. ACTEW manages the operation of the business independent of government. As a corporatised entity ACTEW is responsible for the sustainable delivery of its services, engagement with its customers as to their needs in the context of its licence conditions and the ACT's water policies, as well it needs to be innovative in terms of its service delivery. It is not the role of the Commission to second guess ACTEW in the management of its business.

ACTEW clearly also has the important role in the determination of water and sewerage services prices of providing the ICRC with information based about its current and

prospective future costs and the likely demand for its services now and in the future. For without this information the ICRC would lack a sound basis on which to make its determination and is, therefore, likely to set prices that are too high or too low to the detriment of the community. As we have seen, however, the present system allows for considerable debate about the nature and extent of these responsibilities. Options for remedying this situation are discussed below.

ICRC

The ICRC has a range of roles only one of which, the determination of prices for water and sewerage services is relevant to this review. It is important to note that this role is quasi-judicial in nature. That is, Commissioners are appointed on the basis of specific qualifications and experience and they have a fixed period of tenure. Commissioners are expected to exercise independent thought and judgement in fulfilling their statutory obligations. The Act also provides scope for a Commissioner to make a dissenting opinion if they do not accept the majority position of the Commission.

The Commission makes a determination following a reference and request to make a determination from the Treasurer. The terms of reference provided can request the Commission to examine any matter the Treasurer might deem relevant to the making of the determination, request that specific matters receive explicit consideration and request that supplementary information be provided in the investigation report.[15] The Commission may, therefore, confront a potentially wide variation in matters to consider and report on as well as a wide variety of circumstances in which the investigation needs to be conducted. For these reason, we consider that the Commission should have a wide discretion to determine the information its needs to conduct its investigation and the capacity to adapt the regulatory processes, while having regard to the requirements of the ICRC Act, to meet the requirements of the investigations. Restricting that discretion may, in some circumstances, lead to matters that should be considered not being considered and, in other circumstances, to the Commission being forced to consider matters that it judges are not relevant.

In the case of a determination of the prices of water and sewerage services, the Commission's principal focus will be on establishing ACTEW's forecast efficient costs and establishing indicative revenues which are sufficient to maintain ACTEW's financial viability over the regulatory period (and beyond), allowing for uncertainty in water sales.

[15] For example, in the most reference for a determination of regulated retail electricity prices, the Treasurer requested that the Commission provide information of the contribution of the feed in tariff to retail electricity prices.

7.2 Governance

We now turn to the governance of each of these entities. It might be said that the community exercises its governance responsibilities once every four years and no more need be said about that. Each of the other entities are discussed below.

Government

Were the government to have a direct role in determining the prices of water and sewerage services, there would be a conflict of interest between its roles as custodians of community welfare and its role as ACTEW's shareholder and recipient of any profits made by ACTEW. In the former it ought to be restricting the exercise of any market power that ACTEW possesses. In the latter it would be interested in maximising the profit that ACTEW makes. This conflict is avoided by giving the ICRC the responsibility for determining the prices of water and sewerage services. As noted earlier, however, the Treasurer retains the role of providing the reference under which the Commission make s the determination. The Commission has argued elsewhere that the capacity to use this role to influence the Commission's determination is severely limited, particularly since the reference itself is a disallowable instrument.[16]

As noted above, the Treasurer also appoints the Industry Panel members should an application for review of a price direction be received. This creates a potentially more serious problem because the Treasurer, as a shareholder of ACTEW, would clearly prefer a price direction which yields a greater profit for ACTEW over one that yielded a smaller profit. Unfortunately, this potential conflict is not mitigated by any mechanism of scrutiny by the legislature. We return to this issue in the section of legislation, below.

ACTEW

The Commission addressed ACTEW's governance arrangement in some detail in chapter 1 of its Draft Report Regulated Water and Sewerage Services February 2013. In this analysis the Commission identified the respective roles of shareholder, the board management and their accountabilities in terms of the performance of the business. This analysis was undertaken as an input to the Commission's assessment of the form of regulation to be used for making the price direction.

ICRC

The Commission's own governance arrangements are specified in the Independent Competition and Regulatory Commission Act 1997. The Act establishes the objectives for the Commission, the functions and the procedures the Commission is to follow when conducting an industry investigation and making a price direction.

[16] See the Commission's response to the Auditor General's Performance Audit.

Generally, the officers who are responsible for the final decision making of the independent entity have charge of its governance. Examples include the commissions of the Australian Competition and Consumer Commission, the Australian Securities and Investments Commission, the Australian Energy Market Commission and the commissions or authorities of most of the state regulators. One issue that arises in most jurisdictions is the relationship between the officers of the commission or authority, who are usually statutory officers, and the CEO, the person responsible for the day to day management of the staff of the agencies, who is usually a public servant with statutory responsibility for matters such as human resource and financial management and who may or may not be a member of the commission or authority. IPART, the NSW Independent Pricing and Regulatory Tribunal previously had a structure which included the CEO as a member of the Tribunal. IPART now operates with a structure consistent with the ICRC's. [17]

This model is followed in the ACT, with the Commission of the ICRC being constituted by its commissioners, who appear to have overall responsibility for its operation.[18] The CEO of the ICRC is not a member of the Commission and the division of responsibility between the commissioners and the CEO is not entirely clear.[19] The ICRC has chosen to manage this by having all significant decisions made jointly by the Commission and the CEO, usually at one of the Commission's formal monthly meetings, which then effectively functions as executive for the management of the resources of the ICRC. Exercise of the regulatory powers of the ICRC is still solely the province of the Commission, with the CEO coordinating and participating in the processes by which the staff of the ICRC provide advice to the Commission.

Agencies of the ACT government, of which the ICRC is one, may be divided into those that have a governing board and those that do not.[20] Agencies with a governing board are broadly supposed to operate like a public company with the governing board playing the role of the board of directors. The requirement, noted above, that the CEO of the entity be a public servant and have statutory responsible for financial and staffing matters means that the model of a public company, in which all powers reside in the board and are delegated to the CEO, cannot be followed entirely. The ICRC does not have a governing board. Interestingly, the Gambling and Racing Commission (GRC) of the ACT, which has similar functions in its area of responsibility to the ICRC, including the exercise of quasi-judicial powers, has a governing board. Also unlike the ICRC, the CEO of the GRC, who is a public servant, is an *ex officio* member of the commission of the GRC. We are unable to shed any light on why these two

[17] http://www.ipart.nsw.gov.au/Home/About_Us/Corporate_governance_statement_-_November_2013 Prior to this statement the CEO formed part of the Tribunal.

[18] S.6 and Schedule 2.1E ICRC Act.

19 Specifically, there appear to be inconsistencies between the ICRC Act and the FMA.

[20] The importance of this distinction is illustrated by the fact that agencies with a governing board are treated differently under the FMA than agencies without.

agencies should have been set up in these different ways. In practice, either seems capable of operating satisfactorily.[21]

Whatever mechanisms of governance are chosen, it is vitally importance that they make the entity independent of government and allow it to operate independently of government and its agencies. As noted above, the CEO and staff of the organisation are, as in the case of the ICRC, typically public servants and will, therefore, be embedded in the hierarchical structure of that public service and be subject to its performance evaluation and performance processes. It is important that staff of the entity, particularly senior staff including the CEO, do not feel that those processes inhibit their provision of frank and fearless advice to the Commission or their impartial execution of the entities functions.

7.3 Administration

Since the Commission is not in a position to comment on the administration of other entities, this section is restricted to comments related to the administration of the ICRC. We begin by looking at the basic economics of the ICRC's administration before looking at how the ICRC is funded.

Improving cost effectiveness

As an agency of government, an independent price setting entity will be subject to the policies government has imposed on all its agencies, or some subset of them. Examples include ACT government requirements relating to financial management and audit, document management, property services, freedom of information, and web site management. While these policies are generally imposed with the object of ensuring that agencies operate effectively and efficiently and meet appropriate standards, for a small agency, the plethora of such policies can present a significant burden and inhibit efficient operation. For the ICRC, its small size is combined with a highly variable workload that makes achieving effective and efficient operation a significant challenge.[22]

The issues paper seems focussed on assessing whether the ACT can afford to maintain the Commission, operating in the relatively inefficient way described above, with or without the function of determining the prices of water and sewerage services. An alternative approach is to ask what can be done to improve the efficiency and effectiveness of the Commission by addressing the scale and cyclicality issues directly. Clearly, if the Commission were bigger and had a wider range of functions, the the

[21] This observation is based on part on Mr Gray's experience of serving as Chairperson of the GRC for almost nine years.

[22] Commissioners commented on the impact of variations in our workload in their foreword to the ICRC's 2014 Annual Report.

impact of these factors would be reduced. An obvious candidate to be combined with the ICRC is the Technical Regulator.

At present the functions of licensing and general regulation of utilities in regard to, amongst other things, consumer protection and public safety, are split between the ICRC and the technical regulator. Overall responsibility for licensing and general regulation lies with the ICRC. The technical regulator is responsible for standards of technical performance and issues of public safety in regard to matters like the construction standards of item of utility infrastructure. Currently, the functions of the technical regulator are carried out by a unit in the Environment and Planning Directorate, with the role of technical regulator being fulfilled by the Director General of that Directorate.

This arrangement has a number of disadvantages. It is poor governance practice to embed a regulatory function in a policy body responsible for providing advice to ministers. Licensed utilities have to deal with two bodies attached to different directorates. Coordination between the ICRC and the technical regulator creates inefficient bureaucratic process. For example, when the technical regulator wishes to change a technical code it must have its minister provide a draft of the code to the ICRC, which then liaises with the technical regulator to ensure that all requirements have been met. The Commission then writes back to the minister to tell him that we have no objections to the proposed changes. On a number of recent occasions this process has taken months to complete. Were the ICRC and the technical regulator to be combined independent of government most of this bureaucratic process would be internalised within the combined entity, with the minister only approached once when all legislative and any other necessary requirements have been met.

Besides assisting with the problems of scale and cyclicality, combining the two entities would also give the ICRC access to staff with a range of technical skills, which would reduce the ICRC's reliance on outside consultants when it needs to deal with technical issues, as it does, for example, in making a determination of water and sewerage services prices.

Another way to address the problem of cyclicality would be for other agencies of government to make use of the ICRC's analytical, report writing and consultative skills for specific projects, particularly ones that are difficult for a policy advising body, needing to give priority to the daily needs of its minister, to progress[23]. The cost to the agency of retaining the ICRC's services seems to have been a barrier to agencies making use of the ICRC's skills in this way. Some of the options canvassed in the next section might remove or lessen this obstacle. We believe, for example, that the ICRC could make a useful contribution to the government's red tape reduction program.

[23] See IPART Corporate Governance statement for an overview of the type of activities as agency such as the ICRC could perform.

Funding

Under current arrangements the Commission has four sources of funds:[24]

- cost recovery for work done on matters referred to the Commission, including for price directions;
- licence fees for non energy licensed utilities;
- a budget appropriation, at least partly in lieu of licence fees from licensed energy utilities; and
- through a service level agreement (SLA) with the Treasury directorate to fund functions that the ICRC is required to carry out but for which it cannot recover costs.

In addition to its complexity, this arrangement has a number of other drawbacks.

It is not apparent why licence fees for energy utilities should be treated differently from licence fees from non energy utilities, with the former, known as the energy levy, determined by and paid to the Revenue Office and the latter determined by and paid to the ICRC. Although the budget appropriation and the energy levy were introduced at the same time and the levy is determined on the basis of information about the costs of maintaining the licensing system, there is no connection between the quantum of the levy and the quantum of the budget appropriations received by the entities responsible for providing licence related services. [25]

The SLA is negotiated with Treasury, but in practice the amount paid under the SLA is determined through the budget process with no input from the ICRC. Because payments of the SLA are under the control of Treasury, these could be used to restrict the Commission's ability to determine what activities it needs to undertake to discharge it s functions. As the SLA represents a cost to the directorate, Treasury are naturally keen to exercise some control over it. As discussed in section 3.2, this can interfere with the independence of the Commission.

In line with discussion in section 3.2, consideration could be given to:

- maintaining cost recovery for work done on matters referred to the Commission, including for price directions;
- returning to a situation where licence fees are paid by all licensed utilities and doing away with the energy levy;

[24] Subject to satisfying certain legislative requirements, the Commission may enter into agreements to provide services for a fee. Up until the end of September it was conducting the greenhouse gas emissions inventory for the ACT on this basis through an agreement with the Environment & Development Directorate.

[25] In addition to the Commission, these are the Technical Regulator and ACT Civil and Administrative Tribunal.

- providing a budget appropriation, to fund functions that the ICRC is required to carry out but for which it cannot recover costs and to ensure that reliance on cost recovery does not act to limit the independence of the Commission; and
- doing away with the SLA with the Treasury directorate.

This funding structure would retain a large element of cost recovery in the ICRC's funding. We believe this is helpful in maintaining a cost conscious culture in the ICRC. For example, we believe that we are the only agency of the ACT government in which staff and Commissioners keep timesheets which interact directly with the invoices we issue. These are a vital component of our system of assessing costs to be recovered, but they are also an invaluable aid to managing our most important and expensive resource, the time of our staff. Supplementary funding from a single budget line would provide essential supplementary resources to the ICRC while providing simple accountability, including to the Budget Estimates Committee of the Legislative Assembly.

The Commission is not aware of any concern amongst the utilities about the level of its cost recovery charges, but accountability for the use of public resources could, perhaps, be increased by the actual regulatory costs of any review process being reported on customers' bills.

7.4 Conclusions

Overall, the ACT water and sewerage services governance framework accords with recognised best practice, both in Australia and internationally.[26] That is, ACTEW's day to day operations are managed independently of executive government, while the determination of water and sewerage services prices is undertaken by an independent regulator. Both ACTEW and the Commission are accountable to Legislative Assembly for their performance.

The Productivity Commission, in its report on Australia's Urban Water Sector (2011), addressed the roles and responsibilities of the entities in the water sector. Their characterisation is similar to that discussed in the relevant sections above[27]. The major difference was its recommendation that water utilities should be responsible for setting prices. They made this recommendation on the basis that governments' would establish stronger accountability mechanisms.

Following the Commission's recommendations on governance, the ACT government commissioned a review of the issues by Bruce Cohen. The report of that review was

[26] Competition Principles Agreement (1996); OECD, Regulatory Reform, Privatisation and Competition Policy (1992); National Water Initiative (2004).

[27] Productivity Commission (2011) p. 249.

issues late last year.[28] The government is yet to respond to it. We believe that adoption of some of the recommendations in the Cohen report would contribute to the regulatory transparency of ACTEW and further the objectives of this review.

There are grounds for governance concerns about the Treasurer's role in an Industry Panel process. Potential remedies for these are discussed in section 9, below.

Some aspects of the legislative basis for the administration of the ICRC would benefit from clarification.

The cost effectiveness of the ICRC might be improved by extending its functions, perhaps by combining it with another agency unit.

Rationalisation of the ICRC's funding arrangements could improve resource management and enhance the independence of the Commission.

8 Protocols and procedures

The review is seeking comment on the recommendation of the performance audit report for the development of principles to guide the Commission's administrative processes relating to consultation documents, information gathering powers and dispute resolution.

The ICRC Act requires the Commission to undertake consultation as part of an inquiry process and it specifies the nature of notifications and timeframes for consultation. The Commission also reports on the consultation which it has undertaken in its reports.

In managing an inquiry process the Commission and Commission staff are guided by the ACT Public Sector Code of Conduct. These principles, among other things, establish a framework for professional conduct, accountability, project preparation and planning, communicating effectively and understanding legal obligations.[29]

The Commission seeks to implement these principles and values when performing its functions. There is a risk, however, in trying to codify these principles and values in the ICRC Act as the Commission may end up overtime with arrangements which are not consistent with those that apply more generally to the ACT Public Service. Moreover, any action in that regard could weaken the Commission's capacity to conduct its inquiries in the way it sees best while also impacting negatively on the Commission's capacity to be innovative when conducting an investigation or price determination.

[28] Cohen, B. Review of Institutional Arrangements for ACTEW Corporation Limited (2013) http://www.cwd.act.gov.au/__data/assets/pdf_file/0009/535572/ACTEW-Review-Report.pdf.

[29] ACT Public Service Code of Conduct December 2013.

8.1 Consultation documents

The ICRC Act specifies that the ICRC must, when undertaking an industry investigation, produce a draft and a final report. The Act does not specify the production of issues papers, technical papers or working conclusion documents. The ICRC, however, has in the past exercised its discretion and produced these types of documents when it considered that these made a cost effective contribution to an investigation.

It is questionable whether mandating that the ICRC produce of issues, technical papers and other guidelines will mean a better outcome for the ACT community. Every investigation is different and there is no guarantee that an approach that is effective for one investigation will be as effective in another. The Commission notes that the National Electricity Rules require the Australian Energy Regulatory (AER) to produce guidelines in relation to how it will apply the rules. The ICRC also notes that the AER is a national regulator and guidelines are intended to assist a large number of businesses each of whom may have a different view on how a rule should be applied given their particular circumstance. In the case of the ACT water utility, the ICRC is only dealing with one entity.

That does not mean that the ICRC does not see merit in producing these types of documents. In our view, there is likely to be value in the Commission producing guidelines and technical papers, but, in many cases, these documents will need to be produced before the price investigation commences. Moreover, their value comes from confirming practices and procedures and thereby allowing a future investigation to be undertaken on a more streamlined and cost effective basis. Consideration needs to be given to how the Commission might resource these activities outside of the formal investigation process.

8.2 Information gathering powers

The ICRC Act specifies the powers of the Commission to collect information and the conditions under which it can require the publication of confidential information. In this context, the performance audit report found fault with aspects of the ICRC's communication with ACTEW. The Commission addressed this criticism in its *Response to the ACT Auditor-General's Office Performance Report April 2014.* As the Commission noted that, in an overwhelming number of cases, the information exchange process between the ICRC and ACTEW worked well. The disagreement between the Commission and ACTEW to which the performance report devotes so many pages was not, however, a communications issue. Rather it was about whether ACTEW was required to provide the water sales forecasts that the Commission had requested to assist it in preparing its draft report.

Unless included as a reset principle in a previous price direction, a rather clumsy mechanism, ACTEW is not compelled to provide any kind of submission to the Commission in the course of an investigation. The Commission does have power under

section 41 of the ICRC Act to compel the production of information, but, our experience suggests, this is not likely to be effective in compelling ACTEW to create information, such water sales forecasts. This is a serious weakness in the Commission's information gathering powers because setting a price is a forward looking activity and much of the information that is required is in the form of forecasts or projections of the likely values of the relevant variables in the future.

The weakness of the section 41 power could be addressed by the inclusion of a new provision in the ICRC Act which would allow the Commission, when conducting an investigation prior to making a price direction, to issue a statement of its information requirements. The provision would compel the parties to whom the statement is issued to supply the information specified in the statement to the Commission within a time period specified in the statement. The introduction of such a provision is discussed further in the section 9 below.

8.3 Dispute Resolution

On the basis of its discussion of the dispute described above, the performance audit report also raised the possibility of introducing a third party dispute resolution process. This suggestion has two major drawbacks: it adds an unnecessary complexity to the process of making a determination of the prices of water and sewerage services and would therefore, likely increase the cost of the determination and it is incompatible with the quasi-judicial nature of the determination process.

Disputes of the kind that were the subject of the performance audit report would not occur if the new provision in the ICRC Act, described in the last section, were to be introduced. Had that provision been in place in 2012, the Commission would have issued a statement of its information requirements, including water sales forecasts, and there would have been no doubt that ACTEW was required to provide the information specified in the statement, including the water sales forecasts.

The Commission's experience in the early stages of the 2015-16 biennial recalibration process is that providing a statement of information requirements that ACTEW knows it must comply with not only causes the information to be provided in a comprehensive and timely fashion, but also fosters good relations and better understanding between the Commission and ACTEW. If the issuing of the statement of requirements is preceded by consultation as to its form and content, as was the case with the 2015-16 process, the efficiency, effectiveness and cordiality of the process can be markedly enhanced. Water sales forecasts were provided in this process, without any need for follow up action by the Commission, as a routine part of the process. Moreover, the information exchange process which has occurred as part of the biennial recalibration, which included the development of the information template was completed on a collaborative basis with ACTEW and that the required information was produced by ACTEW without any problems.

The lesson from this process is that where the Commission's information requirements are clearly specified and have been developed in consultation with ACTEW and they are supported by a legal instrument then information exchange conducted under the Act, as it currently operates, is likely to be effective and not unnecessarily resource intensive for either the Commission or ACTEW.

Since the issuing of a price direction is a quasi-judicial process, with the Commission in the role of decision maker, it would be difficult to introduce a third party into the process to resolve disputes without undermining the authority of the Commission as decision maker in the process. Disputes about procedure, like the one described in the performance audit report, are best handled by the Commission making sure, at the outset of the investigation, that there is no doubt about the procedure to be followed. Disputes about the content of a price direction or a conclusion reached in a report, which are the far more common kind, are precisely those matters that the Commission exists to determine. Introduction of a third party into a dispute of that kind would undermine the foundations of the regulatory price setting process.

8.4 Guidelines and principles

The Commission notes that there is a trend to specify matters regulators must address when making pricing or network charges determinations. It is a matter for judgement whether these are necessary or likely to be cost effective in the case of a determination of the prices of water and sewerage services, given that the Commission is already bound to have regard to the matters specified in section 20(2) of the ICRC Act. That said, if policy makers see merit in giving economic efficiency prominence and or specifying how economic efficiency is assessed, we suggest that economic efficiency might be assessed in terms of:

- The value of past investments in the water and sewerage business which were prudent and efficient;
- The need for future investment in the utility to meet licence obligations, regulatory requirements and ACT water policies;
- Accounting and economic depreciation;
- Efficient operating costs;
- Debt servicing obligations, interest costs and financing charges; and
- A return on equity appropriate for a government owned entity.

That is, economic efficiency would essentially be considered in terms of technical efficiency or achieving a least cost outcome. Specifying these considerations could address concerns about the predictability of the Commission's approach while also assisting to streamline the regulatory process by focussing the Commission's investigation to addressing:

- The efficiency of ACTEW's operating costs;

- The effectiveness of ACTEW capital planning and delivery practices;
- ACTEW's financial viability; and
- The territory's water security outlook and the supply side and demand side measures need to maintain water security and while addressing the community's expectations about water availability and environmental amenity.

While these are the basic building blocks used by Australian regulators (they are also included in the NWI Pricing Principles[30]) to assess the efficient costs of network utilities, specification of these principles would formalise the requirement to consider these matters when assessing ACTEW's efficient costs.

Were such guidelines or principles to be introduced, it would important to make clear how these relate to section 20(2) of the ICRC Act. The potential role of section 20(2) in the determination of the prices of water and sewerage services is further discussed in section 9 below.

8.5 Conclusions

Much guidance on the procedures that should be followed in making a determination of the prices of water and sewerage services is already provided, particularly in the ICRC Act and the ACT Public Sector Code of Conduct.

What consultation documents are produced to facilitate a particular investigation may be best left to the discretion of the Commission.

There may be merit in introducing a new provision in the ICRC Act to improve the cost effectiveness of information gathering by the Commission.

If the new provision is introduced into the Act, the case for a dispute settling procedure is considerably weaker. In addition there may be incompatibilities between a dispute settling procedure involving a third party and essential features of the role of the Commission.

Whether guide lines of principles are necessary is a matter for policy makers. Were they to be introduced, conflict with existing provisions of the Act would need to be avoided.

9 Legislative framework

As noted in the preamble to this submission, the Commission is established by its own Act, the *Independent Competition and Regulatory Commission Act 1997*. The Act provides the basis for the Commission to exercise its statutory powers independent of

[30] National Water Initiative Pricing Principles (2010) COAG Steering Group on Water Charges.

ministerial direction. In the context of this review of the determination of the prices of water and sewerage services, it is essential to remember that the Act gives the Commission a range of functions, extending beyond price determinations, and that other acts, most importantly the *Utilities Act 2000*, give the Commission other functions and powers. The procedural requirements in the ICRC Act are designed to accommodate this range of functions. Any proposed change related to a particular function, such as the determination of the prices of water and sewerage services, needs to be designed carefully so as not to compromise the Commission's capacity to carry out any of its wider range of functions.

Although the ICRC Act gives the Commission the power to make price directions in general and specifies how it should go about this task, it does not confer a power to make a price direction for any specific industry. Rather it provides the means by which certain industries may be identified as subject to the price determination powers of the Commission. The trigger for commencing a particular price determination process is provided by a reference from the responsible minister, currently the Treasurer. Such a reference will specify the industry or sector of industry to which the price direction is to apply and may specify, among other things, the period over which the price direction will run, referred to as the regulatory period, the date by which the price direction is to be published, the date of commencement of the regulatory period, and any matter the minister wishes the Commission to take account of during its investigation. It is also usual for the reference to include an instruction that the Commission should consider any other matter that it deems relevant.

In the course of an investigation leading to the formulation of a price direction, the Commission will typically be required to consider a diverse range of matters, including engineering, financial and economic issues as well as the impact the price direction may have on the community, government, the regulated entity, and the achievement of policy objectives of government. Consideration of these matters will inevitably involve the exercise of judgment in assessing the likelihood of various outcomes in the future, the reliability of evidence and expert opinion placed before the Commission, the applicability of various regulatory principles to questions arising in the course of the investigation, and the priority to be accorded to the frequently competing objectives to which the Commission must have regard. Making such judgements will inevitably entail making tradeoffs, including between the benefits available if a certain outcome can be secured against the risks involved in pursuing that outcome.

For example, in a water price determination, lower prices are generally more desirable than higher ones, but not if setting a lower price results in damage to the financial viability of ACTEW or the failure of ACTEW to provide a reasonable return to its shareholder. The volume of water sales determines whether a particular price will provide sufficient revenue to ACTEW to achieve these objectives. The volume of water sales in the future is obviously not known to the Commission at the time it must make its price determination. The Commission must, therefore, undertake a risk assessment of the benefits of lower water prices to the community generally against the

possibility that lower than anticipated water sales will result in insufficient revenues for ACTEW.

The judgements described above are too complex to be made other than by a small group of individuals and that is the reason the Commissioners was established. The appointment of a Commissioner is to entrust that individual with making these judgements on behalf of the community and within the framework of law that has been created for this purpose. Having entrusted Commissioners with this responsibility it is important that they be given the freedom to exercise their judgement about where the best interests of the community lie in any matter that they must consider. This is the reason that statutory independence is critical to the proper functioning of the Commission. Only if it is afforded this independence is it reasonable for the community to hold the Commission accountable for the consequences of the decisions it makes.

Generally, the ICRC Act in its current form has proved workable; many reports and price directions have been produced with the framework that it provides. The context in which that Act operates has, however, changed over time. In 2005 the AER assumed responsibility for determining network charges for the ACT's electricity and gas distribution networks. This means that the ICRC objectives of promoting effective competition and ensuring non-discriminatory access are now not as relevant. Instead, the Commission is primarily concerned with protecting consumers from ACTEW's monopoly power when it is making a water and sewerage services price determination. Unlike, energy regulation, responsibility for regulation for urban water authorities has stayed with the States and Territories and there does not appear to be an agenda to change this.

The Act has also been subject to various amendments, in amendments consequential to changes to other acts seemingly unrelated to the ICRC Act, some of these; at least, do not sit well with the pre-existing provisions and schema of the Act. A review of the Act is, therefore, timely. The following four areas have either been identified through the issues paper or other processes or have come to the attention of the Commission in the course of its work:

- objectives and principles;
- determination of the regulatory period;
- requirements of a draft report;
- review of a price direction.

Each of these is discussed in turn below. In addition to these comments, lawyers on the staff of the Commission participated in the legal workshop convened by the reviewer, which afforded the opportunity for more technical discussion of some of the legal issues arising from this review of the Act.

9.1 Objectives and principles

The overarching objectives for the ICRC are specified in section 7 of the ICRC Act. Given the comments above about the changing role of the Commission, consideration might be given to updating this section to reflect that the ICRC's principal objective is to improve the welfare of the ACT community by promoting the provision of efficient, reliable and safe infrastructure services.

Section 20(2) of the ICRC Act specifies the matters to which the Commission must have regard in making a price direction. These principles may appear to contain a disparate list of considerations, however, when viewed in the context of the Queensland Competition Authority's (QCA) 2013 Statement of Regulatory Pricing Principles referred to in the issues paper, the list could be seen as incorporating the efficiency and fairness considerations discussed in that statement.

The QCA statement in relation to economic efficiency identifies technical, allocative and dynamic efficiency. While all aspects of efficiency are important, in making a price direction for water and sewerage services, the Commission focuses on technical efficiency and ACTEW's ability to deliver the service at least cost on a sustainable basis.

As the QCA observed, pricing principles used by it and other Australian regulators are mainly concerned about the relationship between prices and costs. The fairness element goes beyond this to encompass considerations of the impact of the price or a change in the price on different parts of the community. The issues of fairness and efficiency are however intertwined. The QCA notes this when it observes that it may not be viewed as fair if someone imposes a cost and does not pay for it, or when someone is required to pay for a cost that they did not generate.

Similarly, the principles encompass ecologically sustainable development, demand management and least cost planning. In this context it is important for the Commission to understand how ACTEW is accounting for its costs including environmental externalities. Ultimately, it a matter for ACTEW's management to incorporate these considerations in their business plans and for the Commission to assess the cost effectiveness of this when it reviews their forecast operating and capital expenditures.

The Commission also needs to consider the time dimension of costs and benefits. If costs are incurred now to ensure future benefits then consideration needs to be given to assigning recovery of those costs to future users. This also requires the Commission to take account of ACTEW's cash flow requirements. The Section 20(2) principles allow the Commission to do this.

The breadth, complexity and interconnectedness of these principles do not, however, provide much of a guide to how the Commission is likely to approach the making of a price direction for water and sewerage services. It may be helpful to those looking for such guidance if the Act were amended to require the Commission, when making a price direction for water and sewerage services, to set prices such as to provide

reasonable assurance that the expected efficient costs of the utility will be recovered, provided that setting prices in this way does not put the financial viability of the regulated entity at risk.

The Commission might also be required to explain how it concluded that the prices set meet the required criterion and, if it concluded that prices meeting the criterion would put the financial viability of the regulated entity at risk, how it reached that conclusion and the variations it introduced in the price direction it would otherwise have brought to deal with that situation.

Since this principle has, broadly speaking, underpinned all the Commission's past price directions for water and sewerage services and it is difficult to imagine circumstances in which the Commission would not wish to take this approach, introduction of such a provision is unlikely to have much effect on the price directions the Commission makes. If, however, it enhances the transparency of the process, it may be worth considering.

9.2 Determination of the regulatory period

The performance audit report provides legal opinions to the effect that the ICRC Act does not permit the responsible minister to delegate to the Commission the power to determine the length of the regulatory period in a price direction and that any reference that attempts so to delegate this power and any price direction produced in response to such a reference are invalid. Notwithstanding that the ACT government and the Commission obtained independent legal opinions that came to the opposite conclusion, namely that the responsible minister does have such a power, there would clearly be merit in removing any doubt about the matter.

This could be done in one of two ways: the power could be given to the responsible minister explicitly or the responsible minister could be required to specify the regulatory period when making a price direction. There have been occasions when the responsible minister has neither delegated the power to the Commission nor specified the regulatory period. Since the regulatory period is an integral part of a price determination, on those occasions, the Commission has simply specified the regulatory period in the price direction.

The length of the regulatory period is often intimately connected to the form of regulation adopted. Since this latter matter is almost always left to the Commission, it would seem sensible to give the minister the ability to delegate the power to determine the regulatory period to the Commission. There may be occasions, however, such as occurred on the introduction of full retail competition into electricity retailing in the ACT, when the government wishes the Commission to make a price direction for a particular period. In this case, the Commission would design a form of regulation that was appropriate for the regulatory period the government had specified. Giving the minister the power to delegate, but leaving the exercise of the power to the minster's discretion would cover both cases.

9.3 Requirements of a draft report

The section on the requirements applying to a draft report is one of the more confused parts of the performance audit report. A detailed analysis is provided in the Commission's response to the performance audit report.[31] For present purposes the key points are these:

- that Part 3 of the ICRC Act applies to a draft report and Part 4A to a final report has never, to our knowledge, been disputed;
- the assertion that ACTEW "had expectations" that the draft report on the prices of water and sewerage services would, as a matter of law, meet the requirements Part 4A lacks credibility;
- since Part 3, section 18(5)(a), requires the production of a draft price direction, all the matters that must be settled to produce a price direction must be dealt in the draft report; and
- the draft report and draft price direction on the prices of water and sewerage services issued by the Commission in February 2013 met all the requirements of Parts 4 and 4A, except those that only a final report could meet, such as tabling requirements. [32]

The scheme of the Act in relation to these matters is quite clear. Division 3.1 of Part 3 of the Act deals with industry references, which are the kind of reference used to seek a price direction from the Commission. Part 4 of the Act deals with price directions and Part 4A deals with final reports and procedures to be followed. Although perhaps it could be argued that Section 20(2) of Part 4A of the Act does not apply to draft price directions, by virtue of its use of the phrase "In making a decision under subsection (1),...", the Commission has never, to our knowledge, taken this view and we certainly did not in formulating the draft price direction for water and sewerage services in February 2013. The approach taken by the Commission is supported by Section 20(4) which does not distinguish between a draft and final price direction, being stated thus:

> In a price direction, the commission must indicate to what extent it has had regard to the matters referred to in subsection (2).

The key point, which does not seem to have been recognised clearly in the performance audit report, is that the purpose of a draft report, as Section 18(6) of the Act makes clear, is to allow stakeholders to have a final opportunity to influence the

[31] Response to the ACT Auditor General's Office Performance Audit – The Water and Sewerage Pricing Process.

ICRC Report 3 of 2014 April 2014, pp31.

[32] It is worth noting that the terms of reference issued by the Treasurer for the wss investigation specifically required the investigation to consider the matters listed in Section 20 (2).

Commission's consideration of matters before it issues its final report.[33] Obviously, anything that limits the freedom of the Commission to respond to submissions it receives reduces the value of this consultative process. The performance audit report draws attention to the differences between the draft and final reports. All the significant differences between the two reports can be traced to reconsideration of relevant matters by the Commission stimulated by the receipt of submissions from stakeholders. In many cases the stakeholder making the submission was ACTEW, which provided a large volume of new information is response to the draft report, including some water sales forecasts.

The issues paper notes that the performance audit report highlighted concerns about the lack of clarity about the relationship between Parts 3 and Part 4 of the ICRC Act. Although this does not seem to have been a concern prior to the 2012-13 water and sewerage services prices investigation, consideration could be given to whether the relationship could be made clearer. The key points would seem to be that the matters listed in Section 20(2) must be taken into account by the Commission in formulating a draft price direction, but that a final price direction and associated report can differ from a draft price direction and associated report in the conclusions reached and the determinations made by the Commission having considered that list of matters.

9.4 Statement of information requirements

As discussed in section 8.2 above, there may be merit in introducing a provision to the Act that, for a reference seeking that the Commission make a price direction, the Commission be required to provide to the regulated entity a statement of information requirements within some period following receipt of the reference. The provision would require that the regulated entity provide the required information with the timeframes specified in the statement. The provision might contain safeguards, for example, restricting the Commission only to requesting information that is necessary for the purposes of making the price direction.

The provision would have to be designed not to conflict with the existing provisions through which the Commission can seek input from stakeholders, including the regulated entity.

9.5 Review of a price direction

The ICRC Act provides for the referring authority, currently the Treasurer, or the utility, currently ACTEW, to seek a review of a price direction for water and sewerage services made by the Commission. The Act prescribes that such a review must be

[33] Section 18(6) of the Act states that "In preparing its final report of an investigation, the commission must take into consideration any written comments submitted in accordance with the invitation in subsection (1) in relation to the draft report of the investigation."

conducted by an Industry Panel appointed by the referring authority. Prior to 2013, no application had ever been made under this provision. In September 2013 such an application was received by ACTEW in respect of the price direction for water and sewerage services made by the Commission in June 2013. The Industry Panel appointed to conduct that review issued its draft report in December 2014 and is expected to issue its final report in the first half of 2015.

Because this provision has never been used before, little attention has been paid to it. Recent events have, however, served to raise serious concerns about the operation of these provisions. These concerns fall into two groups: concerns about governance of the Industry Panel process, including the appointment of Panel members, and concerns about the nature and purposes of the review.

Governance

The members of the current Industry Panel were appointed by the Treasurer, who is a shareholder of ACTEW and has a direct interest in the revenues generated by ACTEW since its profits are paid to the government as tax equivalent payments and dividends. Unlike the reference requesting the Commission to make a price direction, this appointment process is not subject to scrutiny by the Legislative Assembly or, indeed, to any scrutiny at all. The secretariat support for the IP has been provided by staff from the Treasury, operating out of the Treasury and supported as necessary by outside consultants.

The role played by the Treasurer and his directorate in the processes of appointment and the ongoing operations of the Industry Panel would seem to constitute a clear conflict of interest: the Treasurer being a shareholder in the entity that is the subject of the price direction under review and having a direct interest in the outcome of the review.

The obvious way to deal with this conflict would be for the Act to specify an existing entity to conduct the review. This would have the added advantage of avoiding problems associated with the temporary nature of an Industry Panel and the property rights in materials produced by it or for it. It could also provide a mechanism for dealing with circumstances in which a relevant entity considers that the review body has acted contrary to its legislation and that any determination that it has made is, therefore, invalid. The difficulty with the current provisions is that the Commission may find itself in a position of being required to defend a price direction, brought down by an Industry Panel, that it has doubts about.

There does not seem to us to be any standing body in the ACT that could hear an application for review of a price direction. The courts have the independence and authority, but lack the technical expertise and normal court procedures are not well suited to dealing with a matter of this kind. Similar observations apply to the ACT Civil and Administrative Tribunal. It would clearly not be cost effective for the Territory to establish its own specialist standing body to hear such applications. There is, however, such a standing body at the Commonwealth level: the Australian

Competition Tribunal, which deals with appeals against the decisions of Commonwealth regulatory bodies such as the Australian Energy Regulator, it also reviews decisions made by the economic regulator in WA. It may be worth considering whether an agreement can be reached with the Commonwealth to make the Tribunal available to hear any applications for review of a price direction. The existing provisions of the Act in regard to the costs of the hearing could substitute the Tribunal for the Industry Panel.[34]

Nature and purposes

Section 24N of the Act covers the nature of the review. It states:

> (1) On an application for review of a price direction, an industry panel may—
>
> (a) substitute a new price direction for the original price direction; or
>
> (b) confirm the original direction.
>
> (2) An industry panel must make a decision on an application for review—
>
> (a) on the merits of the case, having regard to the criteria listed at section 20 (2) for price directions; and
>
> (c) as required by section 20A, section 20B and section 20C for price directions.
>
> (3) Despite subsection (2), the panel may not consider any matter on an application for review that was not raised on behalf of the applicant in submissions to the commission for the purposes of the investigation of the price direction that is the subject of the review.
>
> (4) An industry panel review is not a legal proceeding for the Criminal Code, chapter 7 (Administration of justice offences).

The Industry Panel in the current review seems to have interpreted (2)(a) to mean that the hearing is a merits review and, therefore that it is free simply to remake the price direction without having found fault with the Commission's price direction and that, notwithstanding (3), it is free not only to consider but to create, or have created for it, material that was not raised on behalf of the applicant in submissions to the Commission in during the investigation that led to its making its price direction.[35]

[34] Such an arrangement may require amendment of the Competition and Consumer Act 2010 (Cth) to allow the Tribunal to be bound by ACT legislation when it conducts a price direction hearing, although the general provisions under which the Tribunal usually operates are quite similar to those in the ICRC Act.

[35] The Commission notes that the application for a review from ACTEW did attempt to establish grounds for a review, indentifying two matters. The current Panel's review has ranged well beyond these matters.

Leaving aside the legal question as to whether the current Industry Panel has acted within its powers under the Act, the fact that a Panel can form the view that proceeding in this way is within the provisions of the Act is of deep concern.

The first deficiency of the Act is that it fails to specify the grounds on which an appeal may be made. To leave the grounds for appeal open ended in this way is contrary to the quasi-judicial nature of the Commission's decision making powers. In law, appeals are based on an error of law or fact, from this stem the various grounds for review, including jurisdiction, justifiability, and standing. The Act as it stands seems to have had no regard for well tested administrative law principles.

The lack of grounds for an application then seems to lead to the Industry Panel being allowed to remake the Commission's price direction without first making a finding of error and, therefore, without the Commission's views on the alleged error being considered. This remaking of the price direction simply on the grounds that had the Industry Panel had the responsibility of making the price direction it would have approached it differently invites forum shopping by the regulated entity. If no error is identified before the Industry Panel commences to remake the price direction, there can be no presumption that the Industry Panel's price direction is any way superior or to be preferred to the price direction made by the Commission.

The second deficiency in the Act is the limited class of persons that may make an application for a review. Consumers of the regulated entity's services are not permitted to make an application, for example, when they may be adversely affected by a price direction. On what grounds the referring authority might legitimately seek a review are unclear. The Treasurer as referring entity might wish to seek a review as a shareholder in ACTEW, providing another illustration of the conflict of interest mentioned above, but ACTEW itself already has the right to appeal.

We note that the Commissioners' Preface to our last Annual Report discussed one aspect of the matters raised here and suggested that, when the regulated entity and applicant for a review is a government owned entity, the only grounds for review should be that the Commission's price direction threatens the financial viability of the entity and that the application should be dismissed if the reviewing entity cannot make a finding that this threat is present in the price direction.

The shortcomings identified here have financial as well as legal ramifications. The remaking of a price direction when such a remaking may not be justified is likely to incur a significant unnecessary cost.[36]

[36] As mentioned earlier, the current estimate of the cost of the current Industry Panel process is $1.4 million.

9.6 Conclusion

It is beyond the scope of this submission to make detailed suggestions about how some of the more legally complex of these matters should be addressed. The Commission is, however, prepared to engage in further discussion, including with the involvement of the lawyers on its staff, to devise means to address these matters.

10 Conclusions

This submission has identified various ways of improving the cost effectiveness of the process of making a price direction for water and sewerage services. Some of these are also likely to improve the quality of the regulatory outcomes more generally.

In some cases, the basis and directions for reform are clear and progress could be made quickly. In others, more development work is needed before any reform initiatives will be ready for implementation. Some of the legislative issues identified in the previous section clearly fall into this category. In yet other cases, the basis for change has not been clearly established, for example, as to whether the Territory should retain its own independent regulatory agency. In these cases, the question of whether any change is required remains to be settled. This submission has tried to provide some pointers about how that question should be approached.

The Commission regards the review as providing an opportunity to make a worthwhile contribution to improving regulatory processes in the Territory and looks forward to reading the review report.

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