



Infrastructure
New Zealand

Crombie Lockwood Tower
Level 16, 191 Queen Street
PO Box 7244
Wellesley Street
Auckland 1141
New Zealand

Phone: +64 9 377 5570
Email: info@infrastructure.org.nz

Sunday 12 February 2023

Infrastructure New Zealand Submission to the Finance and Expenditure Committee – Water Services Economic Efficiency and Consumer Protection Bill

1. Introduction

- 1.1 Infrastructure New Zealand (INZ) welcomes this opportunity to submit to the Finance and Expenditure Committee on the Water Services Economic Efficiency and Consumer Protection Bill.
- 1.2 INZ is New Zealand's membership organisation for the infrastructure sector. We promote best practice in national infrastructure development through research, advocacy and public and private sector collaboration. Our members come from diverse sectors across New Zealand and include infrastructure service providers, investors and operators.

2. General Remarks

- 2.1 As we have outlined previously, INZ is a key proponent for reform to New Zealand's three waters sector. We consider that the status quo is failing well short of meeting community expectations and that the case for reform has been made.
- 2.2 In 2021 INZ submitted on the discussion paper titled Economic Regulation and Consumer Protection for Three Waters Services in New Zealand. We noted then, and continue to note now, that effective economic regulation and consumer protection is a key catalyst to the success of the Three Waters Reform Programme.
- 2.3 INZ considers there is a strong case for the economic regulation of water services. This includes drinking water, wastewater, and stormwater. We continue to not be persuaded that water services can remain exempt from economic regulation, especially as our three waters sector has strong monopoly characteristics, and with economic regulation regimes existing for the electricity and telecommunications sectors.
- 2.4 INZ is also concerned about the transition period and the inevitable lack of oversight as the new institutional arrangements are put in place. What happens in the period from 1 July 2024 until the Commerce Commission is in a position to fully undertake its oversight functions?
- 2.5 INZ notes that NZ's water services industry currently has significant inefficiencies when compared internationally with similar organisations like those in the United Kingdom. Even the most efficient service providers have increased operational costs without a corresponding improvement in efficiency of services or in the capital projects delivered. There is a distinct lack of customer and network performance measures in the current industry, and these should be required to be set under the legislation with consequences for not achieving these.
- 2.6 It is critical that there is oversight of the new Water Entities from the commencement of their operations. Any large gap in monitoring and oversight of the new Entities would be undesirable. The current unregulated status of some of these utilities whereby substantial price increases without any stated improvements in outcomes whilst they didn't even achieve their capital plan (that the price increases were funding)

3. Preliminary provisions (Part 1)

- 3.1 As we have previously stated, we are supportive of the Commerce Commission being set out as the regulator. The Commerce Commission has relevant expertise in the economic regulation of utilities which it can readily draw on.
- 3.2 However, unlike price and economic efficiency regulation in other sectors that the Commerce Commission is the watchdog over, the outcomes being sought from the Water Services entities are more complicated.

3.3 INZ expects to see the following outcomes achieved by the regulatory regime:

- i. Ensuring that the necessary capital investments are made in a timely manner to improve outcomes for customers and the environment whilst increasing efficiency. This includes meeting improved outcomes for drinking water, wastewater discharges, renewals, storm system resilience and increased capacity etc.
- ii. Ensuring that there are clear measures that each Water Entity must achieve in respect to their capital programme. Key outcomes and project milestones are part of the framework in the United Kingdom, along with consequences for non-achievement including the publication of results.
- iii. Limiting the price increases to the CPI (or other suitable index) increase *minus* the annual expected operational efficiency gains.
- iv. Empowering the Commerce Commission to ensure the investment programmes are achieved with regular site inspections and audits. Agreement of the Entities' baseline programme to meet objectives set by Government, including those set by Taumata Arowai and environmental regulators in respect to wastewater discharges etc. This will require the Commerce Commission to have specific industry knowledge or contract someone that does (which occurs in the UK) otherwise without this, there is a significant risk that the new regime will fail.

4. Price and quality regulation (Part 2)

Purpose (clause 12)

- 4.1 We note the purpose of the regulations (as per clause 3 and 12) has been modelled on the Telecommunications Act 2001.
- 4.2 However, we consider that there could be two main improvements.
- 4.3 Firstly, long-term sustainability is a fundamental consideration for water infrastructure that is not recognised. For too long a short-term perspective has been taken, leading to the magnitude of issues we are now faced with. INZ considers that the clause needs to be provide for this more clearly.
- 4.4 Secondly, clause 12(d) refers to economic regulation limiting the ability of the entities to extract excessive profits. However, we note that Water Service Entities cannot distribute profits to their owners. This means that there is little incentive for these entities to price in a manner that would generate excess profits. We are not convinced that there is any need for 12(d).

- 4.5 This new regime is to be set up to **not** seek a normal return on equity as that will simply impose more costs on the consumer. The return on equity should reflect financing and capital risk only, not a normal return on equity like Chorus etc

Recommendation 1 and 2

- 4.6 Infrastructure New Zealand recommends that clause 12 be amended to include recognition of the long-term sustainability of service.
- 4.7 Infrastructure New Zealand recommends that clause 12(d) be removed.

Commission review of funding and pricing plans certainty (Clauses 51-53)

- 4.8 These clauses outline that the Commission has the power to review funding and pricing plans and issue what is effectively a direction to amend the plan.
- 4.9 It is unclear at what stage this will occur. On first reading it does appear that the Commission's review would come after a final plan has been adopted and made publicly available as there is no reference to any consultation or engagement process.
- 4.10 However, we would assume that the Commission would be involved in reviewing during the drafting process and provide final checks before the plan is made publicly available. The legislation needs to be clearer on this review process, both in terms of how and when a review can occur but also the form in which direction needs to be provided.

Recommendation 3

- 4.11 Infrastructure New Zealand recommends that clause 51 is amended so that is clear that the Commission will review drafts of funding and pricing plans during the engagement on these documents and before the final plans are adopted by the Water Services Entity, and that the form of direction is specified.

5. Conclusion

- 5.1 We thank the Finance and Expenditure Committee for the opportunity to submit on Water Services Economic Efficiency and Consumer Protection Bill and wish to appear before the Committee to present our submission.

Michelle McCormick
Policy Director
Infrastructure New Zealand

Annex 1: Full summary of recommendations

#	Reference	Recommendation
1	Clause 12	That clause 12 be amended to include recognition of the long-term sustainability of service.
2	Clause 12	That clause 12(d) be removed.
3	Clause 51	Clause 51 is amended so that is clear that the Commission will review drafts of funding and pricing plans during the engagement on these documents and before the final plans are adopted by the Water Services Entity, and that the form of direction is specified.