Access to Water and Sewerage Infrastructure

Explanatory Memorandum

September 2013

Government of South Australia
Department of Treasury and Finance

Department of Treasury and Finance
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1 Introduction

1.1 Introduction

This Explanatory Memorandum accompanies the consultation draft of the *Water Industry (Third Party Access) Amendment Bill 2013 (SA)* (the Bill) that has been prepared by the Minister for Water and the River Murray in accordance with section 26(4) of the *Water Industry Act 2012* (Water Industry Act).

> *(4) The Minister must use his or her best endeavours to introduce into Parliament within 9 months after the commencement of this section a Bill for an Act to provide for a third party access regime to water infrastructure and sewerage infrastructure services operated by entities licensed under this Part (after taking into account the contents of the report prepared under subsection (1) and any other relevant factor).*

A report entitled *Access to Water and Sewerage Infrastructure Services* (Access Report) was published for public consultation by the Minister for Water and the River Murray in February 2013. The Access Report and public submissions are available from http://www.treasury.sa.gov.au.

The Bill has been prepared on the basis of the published Access Report, with appropriate consideration being given to the public submissions.

The Bill amends the Water Industry Act by inserting a new part 9A that would provide a light handed negotiate/arbitrate framework for businesses to seek access to services provided by natural monopoly water infrastructure (e.g. transport services via SA Water's bulk water pipelines). In the first instance it is proposed to focus on establishing access arrangements to SA Water's bulk water transport services. Given the current stage of development of the South Australian water industry, it is not proposed to establish full retail competition. The Bill does not relate to retail services or bulk water resources.

There is potential for some inconsistency to arise between application of the state based access regime in the Bill and the Commonwealth Water Charge Rules made under the *Water Act 2007 (Cth).* To avoid this potential inconsistency, the Bill includes a provision that would declare provisions in the Bill to be 'Commonwealth water legislation displacement provisions' for the purposes of section 250D of the *Water Act 2007 (Cth*). This provision would eliminate any operational inconsistencies between the Commonwealth and the State regimes should they arise in the future. Consultation with the Commonwealth Government regarding these arrangements is required.

In May 2013, the Productivity Commission published its *National Access Regime Draft Report*. The Draft Report stated that primacy should continue to be given to negotiation between service providers and access seekers (the negotiate/arbitrate framework). The Productivity Commission also recommended some changes to the principles in the Competition Principles Agreement (CPA) to promote greater consistency with Part IIIA of the *Competition and Consumer Act 2010 (Cth)* (CCA).

The Productivity Commission's Final Report is not due until 25 October 2013.

It is therefore proposed to table the Bill in Parliament for a further period of consultation, rather than to introduce the Bill. During this period of further consultation the South Australian Government will undertake the necessary consultation with the Commonwealth regarding the interaction and consistency of provisions in the Bill with the *Water Act 2007 (Cth).* The Government will also give consideration to the Productivity Commission's Final Report, as well as any further public submissions, as part of the preparation of the Bill for introduction to Parliament.

1.2 Background

The Access Report consulted publicly on options for access that are compliant with relevant national competition principles.

The national access regime, established under Part IIIA of the CCA, incorporates these national competition principles and establishes three pathways for a party to seek access to significant infrastructure services:

- By applying to the National Competition Council to have services provided by a facility declared, which provides the access seeker with a right to negotiate with the service provider.
- Under terms and conditions set out in a voluntary undertaking which has been assessed and accepted by the Australian Competition and Consumer Commission (ACCC).
- Under an existing effective access regime (i.e. a state based access regime) which has been determined as being effective under the CCA (based on a recommendation from the National Competition Council and a decision from the relevant Commonwealth Minister).

Parties may also reach commercial agreement on access to infrastructure services outside of these formal processes, as has occurred with SA Water in the past.

The options for access outlined in the Access Report included:

- Voluntary arrangements - involves the water industry entities voluntarily making available access to the services provided by its water and sewerage infrastructure to access seekers.
- Legislatively mandated arrangements – involves the South Australian Parliament enacting legislation that mandates certain arrangements for water industry entities to make available access to the services provided by its water and sewerage infrastructure to access seekers.

Submissions received were generally supportive of the establishment of legislatively mandated arrangements (or a state based access regime).

This Bill establishes an economic regulatory framework for a state based access regime that would apply to all South Australian water industry entities declared by proclamation to be subject to it. Under the 2006 *Competition and Infrastructure Reform Agreement*, a state based access regime must be submitted to the National Competition Council for certification by the relevant Commonwealth Minister that the regime is an 'effective access regime' for the purposes of Part IIIA of the CCA. Once certified, access seekers would not be able to apply to the National Competition Council for declaration, under Part IIIA of the CCA, of services to which the state based access regime applies.

Once the final Bill is passed by Parliament, the South Australian Government intends to apply to the National Competition Council for certification of the state based access regime established by it, as has occurred already for the South Australian ports and rail access regimes.

1.3 Next steps

Industry participants and interested citizens are invited to comment on the Bill.

The closing date for submissions on the Bill is Friday 29 November 2013.

Submissions received will be placed on the Department of Treasury and Finance website and may be quoted.

Following receipt and consideration of submissions, the Government will prepare a final Bill for introduction into Parliament.

If the final Bill is passed by Parliament, the state based access regime commencement date would be determined based on the time required for water industry entities and the regulator to prepare.

Submissions on the Bill should be sent to:

e-mail	regulatorypolicy@sa.gov.au
or	
post	Regulatory Policy Department of Treasury and Finance GPO Box 1045 Adelaide SA 5001

Additional copies of the Bill can be downloaded from http://www.treasury.sa.gov.au

2 Implementation of a state based access regime

The following sections will address the implementation of the state based access regime to be established by clause 6 of the Bill (proposed new Part 9A of the Water Industry Act) and compliance with the clause 6 principles of the CPA (set out in Appendix 1) to facilitate the regime's certification under the national access regime.

These sections are:

- Regulatory model
- Negotiation framework
- Dispute resolution
- Terms and conditions of access, including pricing principles
- Public health, environmental and safety standards
- Interstate issues.

2.1 Regulatory model

This section sets out the basis and level of government intervention in commercial negotiations for access. Key topics covered are:

- Appointment of economic regulator
- Scope of access regime
- Application of the access regime
- Periodic review of the access regime.

2.1.1 Appointment of economic regulator

The South Australian approach to economic regulation has been to establish the Essential Services Commission of South Australia (ESCOSA) to regulate across a range of industries, including energy, rail and ports. ESCOSA's responsibilities have been extended recently to include the water industry.

The Access Report sought comment on whether ESCOSA's role should be extended to include a state based access regime and whether a light handed or heavy handed regulatory regime would be required.

Submissions were generally supportive of ESCOSA being appointed as regulator, but SA Water considered that:

> *There may be a monitoring role for the economic regulator within the scope of a light handed regime that facilitates commercial negotiation and arbitration.*

Other submissions also supported the adoption of a light handed regime of monitoring to ensure that commercial negotiation and arbitration occurs in a manner consistent with prescribed principles, similar to the *Railways (Operations and Access) Act 1997*.

Nevertheless, ESCOSA submitted that:

> *…the regulator should be given the discretion to: choose whether to set any access prices directly or rely on negotiations as a first step…*

Section 86C of the Water Industry Act would appoint ESCOSA as the regulator of a state based access regime for water. ESCOSA would be required to adopt a light handed regime of monitoring and enforcing compliance with the access regime. ESCOSA would be required to report to the Minister each year about the work carried out by the regulator under the access regime (section 86D).

The adoption of a light handed regime that facilitates commercial negotiation and arbitration in a low cost manner is considered to be suited in an environment where access negotiations are likely to be infrequent and specific to the needs of the access seeker. This approach has been adopted in South Australia's certified legislative access regimes for railways (set out in the *Railways (Operations and Access) Act 1997)* and port services (set out in the *Maritime Services Act 2000).*

In an environment where access negotiations are likely to be frequent (i.e. there are potentially many access seekers and many reasons for access) and the needs of the access seekers are common, then an access regime that involves prior determination and approval of access terms and conditions and associated prices is likely to be more cost effective for facility owner and the access seekers. This approach has been adopted for industries that have been vertically separated and subject to substantial economic reform, including the gas and electricity industries, where there is full retail contestability.

Important economic reforms to the water industry have been made in South Australia through the Water Industry Act. The water industry, however, is not at the same stage of reform as the energy sector which has adopted vertical separation and full retail contestability.

2.1.2 Scope of access regime

Guidance as to the scope of a state-based access regime is provided by Clause 6(3)(a) of the CPA. Clause 6(3)(a) states that access regimes should:

> *Apply to services provided by means of significant infrastructure facilities where:*
>
> - *it would not be economically feasible to duplicate the facility.*
> - *access to the service is necessary in order to permit effective competition in a downstream or upstream market.*
> - *the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist.*

The Access Report sought comment on the potential scope of a state based access regime. Submissions were generally supportive of the access regime adopting a broad scope, including ancillary services, where appropriate. ESCOSA proposed to also:

> *Require any incumbent that harvests/produces resources (e.g., bulk water and sewage) to negotiate with any water industry entity that seeks access to bulk water (on acceptable terms) – either through the access regime or through separate bulk supply requirements – and require binding arbitration if negotiations fail.*

This proposal was not adopted in the Bill, which focusses on a negotiate/arbitrate framework for access to services provided by significant natural monopoly infrastructure (e.g. water transport services). It is envisaged that persons seeking access to transport water via SA Water's water pipelines would either produce their own water resources by desalination or recycling, or purchase bulk water entitlements to River Murray Water and/or other South Australian water resources under the *Natural Resources Management Act 2004*. Existing public health, environmental and safety standards would continue to apply and recycled water would be prevented from being injected into drinking water infrastructure.

The scope of the state based access regime would be established by section 86B(1) of the amended Water Industry Act and includes all water infrastructure services that comply with clause 6(3)(a)(1) and (2) of the CPA and are significant to the South Australian economy. This would include services provided by the following infrastructure:

- Bulk water transport
- Water distribution transport
- Local sewage transport
- Bulk sewage transport.

The state based access regime may apply to other services, such as water storages and treatment plants, to the extent that they are integral to the operation of the infrastructure services for which access is being sought (e.g. the transport services cannot be provided without passing through the water treatment plant).

The national competition principles aim to ensure that a state based access regime provides a balance between the incentive for commercial negotiations and regulatory intervention to facilitate access negotiations where an agreement is unable to be reached.

Clause 6(4)(a) of the CPA requires that a state based access regime should incorporate the principle that: *wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.* That is, to the extent possible, Government should avoid intervening in commercial negotiations between providers and access seekers.

Section 86ZO of the amended Water Industry Act would establish that nothing in the proposed legislation prevents a regulated operator from entering into an access contract with another person on terms and conditions agreed between the parties.

Clause 6(4)(b) of the CPA requires that a state based access regime should incorporate the principle that: *where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service provided by means of a facility.*

To achieve compliance with national competition principles, section 86B(2) of the amended Water Industry Act would establish a right for persons to negotiate access to services provided

by means of a facility in those segments of the water industry that exhibit natural monopoly characteristics. These services will be declared by the Governor by proclamation.

The next section discusses the application of the access regime under section 86B(2) of the amended Water Industry Act.

2.1.3 Application of the access regime

Water and sewerage infrastructure owned by water industry entities regulated under the Water Industry Act range from critical pipelines serving hundreds of thousands of people to local distribution networks serving less than one hundred. While the scope of the access regime would be broad in order to have consistent regulation across the South Australian water industry, it is not considered appropriate for the regime to be fully applied to all water infrastructure services.

The Access Report sought comment on the application of the access regime to specific infrastructure services. The Access Report proposed that a state based access regime should be fully applied to the services provided by SA Water's bulk water transport pipelines across South Australia. These bulk water transport pipelines are clearly significant. Further, the connection of the pipelines to the River Murray means that access to these services could stimulate competition in the market for River Murray water entitlements. For larger commercial, industrial and agricultural users, access to SA Water's bulk water transport infrastructure could also facilitate competition between alternative water sources.

Similarly, the Access Report proposed that the state based access regime should not be applied to community facilities, such as community waste management schemes and small water distribution systems. The common characteristic of these infrastructure networks is that they are relatively small in scale and are unlikely to facilitate competition in dependent markets. Thus, it is considered that they do not meet the requirement under clause 6(3)(a) of the CPA that the water and sewerage infrastructure be significant.

There is a range of water and sewerage infrastructure that does not easily fit in into either of the categories described above (full application and not applied). Only some sections of Part 9A of the amended Water Industry Act would apply to this infrastructure, relating to basic information requirements and reporting. Over time, the significance of this infrastructure may increase and may warrant full application of a state based access regime. But, at this stage the cost to the infrastructure service provider of complying with a state based access regime may not be justifiable.

Business SA supported the access regime applying to:

> *Bulk water transport, water distribution transport, local sewage transport and bulk sewage transport.*

A number of submissions also supported the regime not being applied to smaller water and sewerage infrastructure facilities.

Sections 86B(2) and (3) of the amended Water Industry Act would enable the Governor to proclaim specific water infrastructure that the access regime under Part 9A of the amended Water Industry Act would be applied to, and the extent of that application.

It is expected that the Governor would proclaim that Part 9A of the amended Water Industry Act would be fully applied to the bulk water transport infrastructure provided by SA Water set

out in Table 1. SA Water would be required to comply with all the provisions (e.g. information requirements and negotiate/arbitrate framework) under this new Part 9A.

Table 1: Water Infrastructure – Full application of state based access regime

Bulk Water Transport	Product
Murray Bridge to Onkaparinga Systems	Untreated Water
Mannum to Adelaide Pipeline	Untreated Water
Swan Reach to Paskeville Pipeline	Drinking Water
Myponga to Adelaide Pipeline	Drinking Water
Morgan to Whyalla Pipeline	Drinking Water
Tailem Bend to Keith Pipeline	Drinking Water
Eyre Peninsula Pipelines	Drinking Water
Glenelg to Adelaide Pipeline	Recycled Water

Under the amended Water Industry Act, the Governor would also be expected to proclaim that the regime would be partially applied to the other water and sewerage infrastructure set out in Table 2, including SA Water's water distribution, and bulk and local sewage transport network.

Table 2: Water Infrastructure – Partial application of state based access regime

Bulk Water Transport	Product
Other water industry entities	
Virginia Pipeline	Recycled Water
Willunga Basin Pipeline	Recycled Water
Water Distribution Transport	
SA Water	
Most South Australian Settled Areas	Drinking Water
Other water industry entities	
Barossa Infrastructure Limited Network	Untreated Water
Bulk Sewage and Local Sewage Transport	
SA Water	
Adelaide	Sewage
20 Regional Service Areas	Sewage

Where the access regime would be partially applied, the Governor would proclaim that only specific provisions in Part 9A of the amended Water Industry Act, relating to basic information requirements and reporting to ESCOSA, would apply to that infrastructure. In this case, the relevant infrastructure operator would be required to comply with the following information requirements:

- Provide the terms and conditions on which it would be prepared to make the regulated infrastructure available for use by others (section 86F(1)(a)).

- Provide the procedures that it would apply in determining a proposal for access to any regulated infrastructure (section 86F(1)(b)).
- Provide contact details of its representative and information about how to lodge an access proposal (section 86F(1)(e)).
- Provide any other information required by regulation (section 86F(1)(f)).
- The information would be required within 30 days after the application for access is received (section 86F(2)).
- The information would be required under section 86H to be provided on a non-discriminatory basis.

The infrastructure operator could then establish commercial agreements with the access seeker.

The infrastructure operator would also be required to provide information about access seekers to the regulator under section 86F(3). As part of its report to the Minister under section 86D, ESCOSA would report on whether the access regime in relation to a specific piece of water or sewerage infrastructure should be extended. ESCOSA's report would be required to be tabled in Parliament.

Some providers, such as small scale water facilities which are provided as a community service, would not be proclaimed under section 86B(2) of the amended Water Industry Act. It is expected that the small scale water infrastructure facilities set out in Table 3 would not be proclaimed, and therefore the new Part 9A of the Water Industry Act would not be applied to this infrastructure.

Table 3: Water infrastructure – no application of state based access regime

Bulk Water Transport	Product
SA Water	
Southern Urban Reuse Scheme	Recycled Water
Mawson Lakes	Recycled Water
Adelaide Airport	Recycled Water
Barker Inlet	Recycled Water
Lochiel Park	Recycled Water
Water Distribution Transport	
Other water industry entities	
Skye	Non-Drinking Water
Roxby Downs	Drinking Water
Wallaroo	Drinking Water
Bulk Sewage and Local Sewage Transport	
Other water industry entities	
172 Community Sewerage Management Schemes	Effluent
Wallaroo	Sewage

2.1.4 Periodic review

Clause 6(4)(d) of the CPA requires periodic review of the need for access regulation to apply to any infrastructure service.

Under section 86ZS of the amended Water Industry Act, ESCOSA would be required to review the access regime established under Part 9A to ascertain whether the access regime should continue to apply to water and sewerage infrastructure services in South Australia. ESCOSA would be required to conduct the review by 30 June 2019 and every five years thereafter. The report would be provided to the Minister and tabled in Parliament.

2.2 Negotiation framework

In order to comply with the CPA, a state based access regime should require an infrastructure operator subject to the regime to *use all reasonable endeavours to accommodate the requirements of persons seeking access* (see clause 6(4)(e) of the CPA, which would include a requirement to engage in good faith negotiations).

The Access Report proposed rights and obligations that could apply to water and sewerage infrastructure service providers for receiving, responding to and negotiating access proposals and access seekers.

SA Water proposed that:

> *The inclusion of provisions similar to those in the IPART Negotiation Protocol to allow for clear negotiation protocols and stepped negotiation and dispute resolution processes.*

Business SA stated that all access arrangements should have:

- *A transparent and common set of minimum terms and conditions*
- *A negotiation framework established to determine other terms and conditions, such as in the Railways (Operations and Access) Act 1997.*
- *Clear information requirements*

Alano Water considered that:

> *30 days as a time period for an access seeker to receive a brochure on the subject matter is too long. Could this not be accomplished in say 14 days?*

Further Alano Water requested that the infrastructure service provider should:

> *Receive, consider and formally respond to an access proposal within a specified timeframe.*

The Bill provides rights to and obligations on providers of water and sewerage infrastructure services to which the state based access regime applies. These rights and obligations provide for clear information requirements and negotiation protocols, including minimum terms and conditions and a negotiation framework based on the *Railways (Operations and Access) Act 1997.*

It was considered that 30 days, rather than 14 days as suggested by Alano Water, was an appropriate maximum timeframe for an access seeker to receive an information brochure from a service provider. This is consistent with the *Railways Operations and Access Act 1997*.

Section 86K of the amended Water Industry Act provides clear timelines by establishing that a dispute exists if, within 2 months after an access proposal has been made, the regulated operator, the proponent and any interested third parties have not agreed on terms of the provision of access.

As discussed in the Access Report, the rights and obligations that would be included in the amended Water Industry Act are:

- Not unfairly discriminate or prevent or hinder access to infrastructure services (section 86ZR).
- Negotiate in good faith (section 86J).
- Prepare an information brochure with information about terms and conditions of access and other information required by regulations (section 86F).
- Provide an information brochure to an access seeker on request within 30 days (section 86F(2)).
- Provide information about current utilisation of the infrastructure (section 86G(1)(a)).
- Provide information about the extent to which it would be necessary to add to or extend the designated facility to meet the requirements of an access seeker (section 86G(1)(b)).
- Advise whether or not they are, as the infrastructure owner, willing to provide access. If not, the reasons why the service cannot be provided (section 86G(1)(c)).
- Receive and consider an access proposal within a specified timeframe (section 86K).
- Notify the regulator and other parties that may be affected by an access proposal (section 86I(6)).
- An access contract would be subject to limitations on the basis of consideration of interests or objections of other affected parties (sections 86J and 86K).

The provider of services to which a state based access regime applies would incur costs negotiating with access seekers. Section 86G(2) of the amended Water Industry Act would allow facility owners to recover reasonable costs from the access seeker.

2.3 Dispute resolution

In an effective access regime, the right to negotiate will be supported by provisions to enforce that right. Clause 6(4)(c) of the CPA states that: *any right to negotiate access should provide for an enforcement process*. Clause 6(4)(g) of the CPA states that: *where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.*

The Access Report proposed dispute resolution arrangements based on the South Australian railways access regime that has been certified by the National Competition Council.

Key aspects of dispute resolution included in the Bill are discussed under the following headings:

- Triggering arbitration
- Binding decisions
- Guidance to the arbitrator
- Extension of facility
- Variation and revocation
- Powers and procedures.

2.3.1 Triggering arbitration

The Access Report outlined criteria that would trigger an access dispute and the process for the regulator to appoint an arbitrator should conciliation be unsuccessful.

ESCOSA submitted that:

> *The regulator should have the discretion to choose (based on objective assessments of relevant considerations) whether to set access prices, arbitrate or appoint an arbitrator, so that the best approach is chosen for each relevant situation.*
>
> *The Minister should not be involved in the access dispute resolution process, other than in cases where SA Water is involved and then only on behalf of SA Water.*

SA Water submitted that:

> *The selection of arbitrator should be agreed between the access seeker and the access provider, and must be based on technical knowledge (including health, safety and the environment where relevant), commercial expertise and industry knowledge.*

It is considered that the provisions of the *Railways (Operations and Access) Act 1997,* as a certified effective access regime for the purposes of Part IIIA of the CCA, provide an appropriate model with regard to the access seeker's rights to trigger an access dispute and the process for appointment of an arbitrator. This regime allows for the relevant Minister to participate in arbitration proceedings.

Consistent with the *Railways (Operations and Access) Act 1997*, sections of the amended Water Industry Act would provide that:

- The access seeker has a right to trigger an access dispute and commence binding arbitration after the regulator has first sought to resolve the dispute through conciliation (section 86L).
- The regulator would appoint the arbitrator (section 86N).

- The arbitrator must be a person who is properly qualified and the regulator must consult with all parties to the dispute and must attempt to make an appointment acceptable to all parties (section 86N).
- The Minister for Water and the River Murray and the regulator have a right to participate in arbitration proceedings (section 86S).

2.3.2 Binding decisions

Clause 6(4)(h) of the CPA states that: *decisions of the dispute resolution body should bind the parties; however rights of appeal under existing legislative provisions should be preserved.*

Section 86ZI of the amended Water Industry Act would make an award of the arbitrator enforceable as if it were a contract between the parties.

Further, under section 86ZJ, an appeal of a decision of the arbitrator to make an award, or not to make an award, could be made to the Supreme Court of South Australia on a question of law.

2.3.3 Guidance to the arbitrator

Clause 6(4)(i) of the CPA describes the matters that the arbitrator should take into account when deciding on the terms and conditions for access. The matters are:

- The owner's legitimate business interest and investment in the facility.
- The costs to the owner of providing access, including any costs of extending the facility but not associated with losses from increased competition in upstream or downstream markets.
- The economic value to the owner of any additional investment that the person seeking access agreed to undertake.
- The interest of all persons holding contracts for use of the infrastructure.
- Firm and binding contractual obligations of the owner or other persons (or both) already using the infrastructure.
- The operational and technical requirements necessary for the safe and reliable operation of the infrastructure.
- The economically efficient operation of the infrastructure.
- The benefit to the public from having competitive markets.

The Access Report proposed that the arbitrator would be explicitly required to take into account the matters outlined above, the objects of the Water Industry Act, and any pricing principles for reference tariffs set by ESCOSA, having had regard to clause 6(5)(b) of the CPA.

Alano Water indicated that:

> *ESCOSA may need to seek examples of access pricing in the water industry that have been struck in other states in order to gain an understanding of what a fair access charge would be.*

SA Water stated that:

> *SA Water supports the establishment of guiding principles that accord with the requirements set out in clause 6(5)(b) of the CPA.*
>
> *As SA Water's retail service prices are informed by an allowable (efficient revenue requirement as determined by ESCOSA, resulting retail charges have to be based on efficient levels of costs. As this eliminates the risk of 'monopoly rents' in retail pricing, retail prices are a sound and equitable basis for setting access prices.*

ESCOSA considered that the regulator should be given the discretion to:

> *choose whether to set any access prices directly or rely on negotiations as a first step*.

It is not considered necessary for the regulator to set access prices as explicitly as it does when regulating SA Water's retail services. Nevertheless, it is proposed that the Bill would include access pricing principles that would provide guidance for the arbitrator in the event of a dispute.

Clause 6(5) of the CPA requires specific pricing principles to be incorporated into all State and Commonwealth access regimes. These principles have been incorporated into certified state based access regimes such as the South Australian ports and rail access regime as matters that the arbitrator must take into account. They have also been included in the NSW water access regime under the *Water Industry Competition Act 2004 (NSW)* and the national access regime in Part IIIA of the *Competition and Consumer Act 2010 (Cth).*

Consistent with the *Railways (Operations and Access) Act 1997,* section 86P of the amended Water Industry Act would include the CPA pricing principles as matters that an arbitrator must take into account when determining terms and conditions of access. It is therefore unnecessary for ESCOSA to set pricing principles.

Clause 4 of the Bill would insert an additional objects clause into the Water Industry Act that is consistent with clause 6(5)(a) of the CPA.

Section 86P(3) of the amended Water Industry Act would provide explicit guidance to the arbitrator that a decision cannot prejudice the existing right a person has to use the infrastructure. It is not appropriate for an arbitrator to consider changes to existing arrangements for access to the infrastructure on the basis of a request for arbitration by a new access seeker.

Further, under section 86ZL, the Supreme Court would have the power to order compensation of persons who have suffered loss or damage as a result of a contravention against a state-based legislative regime.

2.3.4 Extension of infrastructure

The Water Industry Act provides all South Australian water and wastewater service providers, not just SA Water, with the necessary powers to develop infrastructure and offer retail water and sewerage services to South Australians. Developers are no longer limited to connecting to SA Water for developments in South Australia.

Developments that are not self-sufficient in terms of drinking water supplies or the treatment of sewerage, could benefit from the establishment of a state-based access regime. The interconnection of these developments may require the water or sewerage infrastructure provider to extend their existing infrastructure to meet the needs of the access seeker, in this case the water and sewerage services retailer for the new development.

Clause 6(4)(j) of the CPA states that: *the owner may be required to extend, or permit extension of, the facility that is used to provide a service if necessary.*

Clause 6(4)(j) of the CPA sets out some matters that the arbitrator must take into account in relation to an extension of infrastructure. The matters are:

- Such extension being technically and economically feasible and consistent with the safe and reliable operation of the infrastructure.
- The owner's legitimate business interests in the infrastructure being protected.
- The terms of access for the party taking into account the costs borne by the parties for extension and the economic benefits to the parties resulting from the extension.

These matters would be included in section 86P of the amended Water Industry Act as principles that the arbitrator must take into account when making an award.

Explicit guidance to the arbitrator that the decision of the arbitrator cannot have the effect of requiring the owner of the water or sewerage infrastructure to bear any of the capital cost of any addition or extension to the infrastructure unless the infrastructure owner agrees, would be included in section 86P of the amended Water Industry Act.

2.3.5 Variation and revocation

Clause 6(4)(k) of the CPA states that: *if there has been a material change in circumstances, the parties should be able to apply for a revocation or modification of the access agreement which was made at the conclusion of the dispute resolution process.*

Section 86ZG of the amended Water Industry Bill would provide for an award to be terminated or varied if all parties agree or there has been a material change in circumstances.

2.3.6 Powers and procedures

The Bill provides the following powers and procedures in relation to the arbitrator:

- The arbitrator would be selected by the regulator after consultation with all parties and must be a person who is properly qualified. The arbitrator must be independent of the dispute (section 86N).
- A party to the dispute may be represented in arbitration proceedings by a lawyer or, by leave of the arbitrator, another representative (section 86R).
- The Minister for Water and the River Murray and the regulator would have the right to participate in arbitration proceedings (section 86S).
- The arbitrator must act expeditiously and conduct arbitration proceedings in private (sections 86T and 86U).

- The arbitrator is not bound by technicalities, legal forms or rules of evidence (section 86V).
- The arbitrator will have the power to give procedural directions and to obtain information and documents (sections 86V, 86W and 86X).
- The arbitrator may refer a matter to an expert for report (section 86W(1)(e)).
- A person may request that information given to the arbitrator be treated as confidential, and the arbitrator may impose conditions on the access to and disclosure of information (section 86Z).
- The arbitrator and the access seeker can terminate arbitration under certain circumstances (sections 86ZA and 86ZB).
- The standard period of arbitration is up to 6 months (section 86ZC).
- The arbitrator must give a draft decision to the parties and the Minister for Water and the River Murray, the Department of Health and Ageing, the Technical Regulator and the Environmental Protection Authority and give opportunities for representations to be received and considered (section 86ZD(1)).
- The arbitrator must, within seven days of making a decision, notify the regulator, the Minister for Water and the River Murray, the Department of Health and Ageing, the Technical Regulator and the Environmental Protection Authority and the parties (section 86ZD(4)).
- The access seeker may within seven days of the decision elect to withdraw. The decision is rescinded and the access seeker will, for a specified period of time, be prevented from making further access proposals (86ZF).
- Costs of arbitration are to be borne by the parties in proportions decided by the arbitrator. If the access seeker terminates arbitration or elects to withdraw, then the access seekers must bear the costs in their entirety (section 86ZH).

2.4 Terms and conditions

Clause 6(4)(f) of the CPA states that: *access to a service for persons seeking access need not be on exactly the same terms and conditions.*

Section 86ZO of the amended Water Industry Act would ensure that access seekers and the infrastructure owner are not limited from negotiating commercial agreements outside of the provisions of the access regime. The Bill, as a safety net, confers rights on the access seeker in relation to negotiating access and imposing obligations on the infrastructure owner when the access seeker exercises those rights.

While light handed models of access regulation generally do not impose on the infrastructure owners or an arbitrator binding guidance on terms and conditions of access, the Bill includes some measures to ensure that sufficient information is made available to the access seeker and arbitrator to assist in negotiation and arbitration.

These measures are:

- Consistent with clause 6(4)(n) of the CPA, a requirement on the infrastructure owner to have separate accounting arrangements for the elements of a business which are covered by the access regime (section 86E).

- Pricing principles that the arbitrator must take into account as set out in clause 6(5)(b) of the CPA, which states that*:*

Regulated access prices should be set so as to:

(i) generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services and include a return on investment commensurate with the regulatory and commercial risks involved;

(ii) allow multi-part pricing and price discrimination when it aids efficiency;

(iii) not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and

(iv) provide incentives to reduce costs or otherwise improve productivity.

The powers and procedures described above are sufficient to meet the requirements of clause 6(4)(o) of the CPA which states that: *the dispute resolution body or relevant authority, where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service*.

2.5 Public health, environmental and safety standards

It is appropriate for the Government to regulate public health, environmental and safety standards. Similarly, clause 6(3)(a)(iii) of the CPA states that: *access should be provided where the safe use of the facility by the person seeking access can be ensured at an economically feasible cost, and if there is a safety requirement, appropriate regulatory arrangements exist.*

South Australia is well placed in relation to its regulation of public health, environmental and safety standards. The state based access regime would not seek to alter the regulation of public health, environmental and safety frameworks. For example, existing public health measures that prevent the injection of recycled water into the drinking water infrastructure will be maintained.

Key topics are discussed under the following headings:

- Public health, environmental and safety standards
- Arrangements between regulators and the arbitrator.

2.5.1 Public health, environmental and safety standards

Public health in relation to drinking water is regulated through the *Safe Drinking Water Act 2011.* The Act is based on implementation of the Australian Drinking Water Guidelines (ADWG) with key components being consistent with interstate and international legislation. The main provisions of the Act are:

- Registration of drinking water providers.
- Implementation of risk management plans as described in the ADWG including:.
    - Approved monitoring programs and incident notification protocols.
    - Regular audits and inspections.

- Reporting of results to the Department of Health and Ageing.
- Provision of results to consumers.

Public Health aspects of non-potable water and treatment of sewage are regulated through the *South Australian Public Health Act 2011* and *South Australian Public Health (Wastewater) Regulations 2013*, which include:

- Provisions for shutting down or upgrading a recycled water supply system if it poses a health risk.
- Installation approval requirements for waste control systems (including community wastewater management systems).
- Requirements for the approval of recycled water systems.
- Requirements for the approval of sewage products.

The *Environment Protection Act 1993* regulates environmental impacts from the operation of water services. This includes licensing of sewage treatment works, community wastewater management schemes, aquifer storage and recovery in specified areas and discharge of sewage to marine or inland waters.

The *Environment Protection (Water Quality) Policy 2003* also specifies obligations on water entities, for example:

- The *Code of Practice for Aquifer Storage and Recovery 2004* applies to aquifer storage and recovery schemes.
- The *South Australian Reclaimed Water Guidelines 1999* prepared by the Department of Human Services and the Environment Protection Agency apply to a person that reuses, or supplies for reuse, sewage collected by a community wastewater management scheme or a sewage treatment system.

Under the Water Industry Act the technical regulation of plumbing has been transferred to the Office of the Technical Regulator in the Department for Manufacturing, Innovation, Trade, Resources and Energy. The occupational licensing of plumbers will continue to be performed by Consumer and Business Services Division of the Attorney-General's Department.

The legislation requires the Technical Regulator to develop, monitor and regulate technical standards in connection with the water industry.

Technical standards and guidelines that may apply to access seekers include:

- Plumbing Code (AS/NZS 3500).
- National codes for water infrastructure developed by the Water Services Association of Australia, many of which have been developed into Australian Standards.
- Dam design guidelines developed by the Australian National Committee on Large Dams Incorporated, which includes South Australian and interstate water corporations, and implements dam safety guidelines.

As discussed in the Access Report, the Bill does not seek to alter the existing frameworks, as described above, for public health, safety and the environment. The Bill includes an

explicit requirement that the no decision taken by the regulator or arbitrator in relation to access to water infrastructure can override requirements or directions under the *Safe Drinking Water Act 2011*, the *South Australian Public Health Act 2011*, the *Natural Resources Management Act 2004*, the *Environmental Protection Act 1993*, or other law or other legislative requirement relating to health, safety or the environment.

Specifically, section 86P(3) of the amended Water Industry Act would provide that the arbitrator cannot make an award that would be inconsistent with an existing law or legislative requirement relating to health, environment and safety. Further, the arbitrator must accept any advice provided by a department of the Public Service (for example the Department of Health and Ageing, which administers the legislative arrangements pertaining to health, environment and safety).

2.5.2 Arrangements between regulators and the arbitrator

A facility owner may need to establish specific terms and conditions in the access agreement that impose obligations on the access seeker in order for the facility owner to comply with public health, environmental and safety standards. A state based access regime should empower the regulator and arbitrator to consult with the relevant regulatory body and ascertain whether the proposed terms and conditions are appropriate to ensure compliance by the facility owner with the public health, environmental and safety regulatory frameworks.

This issue has already been addressed by section 90 of the Water Industry Act which requires relevant Government agencies to consult with each other in connection with the operation and administration of the Water Industry Act. Clause 7 of the Bill extends section 90 of the Water Industry Act to include an arbitrator appointed by the regulator.

2.6 Jurisdictional issues - interaction with the *Water Act 2007 (Cth)*

Charges made by water industry entities in South Australia, including SA Water and South Australian irrigation trusts, may be subject to Commonwealth water charge rules made under Part 4, Division 1 of the *Water Act 2007 (Cth).*

These Commonwealth water charge rules are designed to apply price regulation to irrigation infrastructure for rural activities, rather than a negotiate/arbitrate approach to infrastructure services. The Commonwealth water charge rules currently adopt a tiered approach to regulation which means that an infrastructure operator is only subject to price regulation if the operator's relevant activities are over a significant size.

The Commonwealth water charge rules appear intended to exclude urban water supply activities from their remit, however, the precise scope of the application of the Commonwealth regime is not easy to determine. There is potential for inconsistency between the state based access regime and the Commonwealth regime where both regimes apply to the same infrastructure operator.

The Access Report proposed to avoid this regulatory uncertainty by using the provisions of Part 11A of the *Water Act 2007 (Cth)* to exclude or displace the operation of the Commonwealth water charge rules in the event that any such inconsistency arises.

The Bill includes a proposed section 86ZM of the amended Water Industry Act, which would be the subject of consultation with the Commonwealth. The proposed section 86ZM would, to the extent that there is inconsistency between the state-based access regime and the Commonwealth water charge rules, provide that the latter would cease to apply in South Australia to the same extent. That is, to the extent that any legal inconsistency exists or

could arise, the laws will automatically operate to deem that only one law (the state-based access regime) actually applies, and therefore there can be no inconsistency.

However, the proposed section 86ZM would not remove the application of the Commonwealth water charge rules where both regimes can be applied concurrently with no inconsistency arising.

South Australian irrigation trusts are currently exempt from the South Australian Water Industry Act. Irrigation trusts are classified as *irrigation infrastructure operators* under the *Water Act 2007 (Cth)*, and all charges levied for the delivery of River Murray water to members outside of urban areas are potentially subject to the Commonwealth water charge rules. The Access Report proposed that it would be reasonable to exempt these from the state based access regime and to allow them to be regulated solely under the Commonwealth regime.

Section 86B of the amended Water Industry Act would exclude irrigation trusts from the state based access regime established under the Bill.

3 Next steps

3.1 Next steps

Industry participants and interested citizens are invited to comment on the Bill.

The closing date for submissions on this report is Friday 29 November 2013.

Submissions received will be placed on the Department of Treasury and Finance website and may be quoted.

Following receipt and consideration of submissions, the Government will prepare a Bill for introduction into Parliament which will be based on this Bill and give consideration of the submissions received.

If passed by Parliament, the state based access regime commencement date would be determined based on the time required for water industry entities and the regulator to prepare.

Submissions on the Bill should be sent to:

e-mail	regulatorypolicy@sa.gov.au
or	
post	Regulatory Policy Department of Treasury and Finance GPO Box 1045 Adelaide SA 5001

Additional copies of the Bill can be downloaded from http://www.treasury.sa.gov.au

Appendix 1

Competition Principles relating to access arrangements as updated by the Competition and Infrastructure Reform Agreement

Access to Services Provided by Means of Significant Infrastructure Facilities

6.(1) Subject to subclause (2), the Commonwealth will put forward legislation to establish a regime for third party access to services provided by means of significant infrastructure facilities where:

(a) it would not be economically feasible to duplicate the facility;

(b) access to the service is necessary in order to permit effective competition in a downstream or upstream market;

(c) the facility is of national significance having regard to the size of the facility, its importance to constitutional trade or commerce or its importance to the national economy; and

(d) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist.

(2) The regime to be established by Commonwealth legislation is not intended to cover a service provided by means of a facility where the State or Territory Party in whose jurisdiction the facility is situated has in place an access regime which covers the facility and conforms to the principles set out in this clause unless:

(a) the Council determines that the regime is ineffective having regard to the influence of the facility beyond the jurisdictional boundary of the State or Territory; or

(b) substantial difficulties arise from the facility being situated in more than one jurisdiction.

(3) For a State or Territory access regime to conform to the principles set out in this clause, it should:

(a) apply to services provided by means of significant infrastructure facilities where:

(i) it would not be economically feasible to duplicate the facility;

(ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and

(iii) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate
regulatory arrangements exist; and

(b) reasonably incorporate each of the principles referred to in subclause (4) and (except) for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) subclause (5). There may be a range of approaches available to a State or Territory Party to incorporate each principle. Provided the approach adopted in a State or Territory access regime represents a reasonable approach to the incorporation of a principle in subclause (4) or (5), the regime can be taken to have reasonably incorporated that principle for the purposes of paragraph (b).

(3A) In assessing whether a State or Territory access regime is an effective access regime under the *Trade Practices Act 1974*, the assessing body:

(a) should, as required by the *Trade Practices Act 1974*, and subject to section 44DA, not consider any matters other than the relevant principles in this Agreement. Matters which should not be considered include the outcome of any arbitration, or any
decision, made under the access regime; and

(b) should recognise that, as provided by subsection 44DA(2) of the *Trade Practices Act 1974*, an access regime may contain other matters that are not inconsistent with the relevant principles in this Agreement.

(4) A State or Territory access regime should incorporate the following principles:

(a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.

(b) Where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service provided by means of a facility.

(c) Any right to negotiate access should provide for an enforcement process.

(d) Any right to negotiate access should include a date after which the right would lapse unless reviewed and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.

(e) The owner of a facility that is used to provide a service should use all reasonable endeavours to accommodate the requirements of persons seeking access.

(f) Access to a service for persons seeking access need not be on exactly the same terms and conditions.

(g) Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.

(h) The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.

(i) In deciding on the terms and conditions for access, the dispute resolution body should take into account:

(i) the owner's legitimate business interests and investment in the facility;

(ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;

(iii) the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake;

(iv) the interests of all persons holding contracts for use of the facility;

(v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;

(vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;

(vii) the economically efficient operation of the facility; and

(viii) the benefit to the public from having competitive markets.

(j) The owner may be required to extend, or to permit extension of, the facility that is used to provide a service if necessary but this would be subject to:

(i) such extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;

(ii) the owner's legitimate business interests in the facility being protected; and

(iii) the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.

(k) If there has been a material change in circumstances, the parties should be able to apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.

(l) The dispute resolution body should only impede the existing right of a person to use a facility where the dispute resolution body has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation.

(m) The owner or user of a service shall not engage in conduct for the purpose of hindering access to that service by another person.

(n) Separate accounting arrangements should be required for the elements of a business which are covered by the access regime.

(o) The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting

information pertaining to a service.

(p) Where more than one State or Territory access regime applies to a service, those regimes should be consistent and, by means of vested jurisdiction or other cooperative legislative scheme, provide for a single process for persons to seek access to the service, a single body to resolve disputes about any aspect of access and a single forum for enforcement of access arrangements.

(5) A State, Territory or Commonwealth access regime (except for an access regime for: electricity or gas that is developed in accordance with the Australian Energy Market Agreement; or the Tarcoola to Darwin railway) should incorporate the following principles:

(a) Objects clauses that promote the economically efficient use of, operation and investment in, significant infrastructure thereby promoting effective competition in upstream or downstream markets.

(b) Regulated access prices should be set so as to:

(i) generate expected revenue for a regulated service or services that is at least sufficient to meet the efficient costs of providing access to the regulated service or services and include a return on investment commensurate with the regulatory and commercial risks involved;

(ii) allow multi-part pricing and price discrimination when it aids efficiency;

(iii) not allow a vertically integrated access provider to set terms and conditions that discriminate in favour of its downstream operations, except to the extent that the cost of providing access to other operators is higher; and

(iv) provide incentives to reduce costs or otherwise improve productivity.

(c) Where merits review of decisions is provided, the review will be limited to the information submitted to the original decision-maker except that the review body:

(i) may request new information where it considers that it would be assisted by the introduction of such information;

(ii) may allow new information where it considers that it could not have reasonably been made available to the original decision-maker; and

(iii) should have regard to the policies and guidelines of the original decision-maker (if any) that are relevant to the decision under review.