

22 March 2024

Peter Achterstraat, AM
Commissioner for Productivity
NSW Productivity Commission NSW Treasury
52 Martin Place
Sydney NSW 2000

Sent via Email: LWUReview@treasury.nsw.gov.au

Dear Peter,

RE: NSW Productivity Commission's Review of funding models for local water utilities

Effective funding and delivery of water and wastewater services in regional and remote NSW has proven challenging. Existing paradigms for funding and delivering services have struggled to create outcomes that achieve expected levels of service quality balanced with efficient costs. Furthermore, servicing solutions of the future will be more complex and require increasing capability for delivery and operation.

No matter how remote, all NSW Communities deserve a funding system that fairly and efficiently enables Local Water Utilities (LWUs) to meet the needs of their community. To achieve the proposed policy outcomes of:

- Achieving minimum levels of service,
- Efficient costs for service delivery,
- Support targeted to those communities that cannot achieve longer-term cost recovery due to size or socio-economic characteristics,
- Transparency on the achievement of service level outcomes and efficient costs,

will most certainly require a combination of options, and limiting participation in funding and delivery activities strictly to public entities arbitrarily and unfairly confines the effective solution space to a potentially less-than-efficient frontier of cost outcomes.

We recommend an efficient funding and delivery solution spectrum that fairly and transparently meets required service levels and embraces cooperation across an ecosystem of public and private stakeholders. To be clear, we are not suggesting privatisation. We recognise that privatisation is outside the terms of reference of the PC's review, and we acknowledge the NSW Government's policy position that councils will continue as the owners of their water and sewerage assets. We are recommending opportunities for private participation and collaboration, not privatisation.

The Issues Paper recognises the Queensland Water Regional Alliance Program (QWRAP) as a proven model for collaboration. Research supporting the QWRAP program found that the application of models is contextual to locality and sensitive to influence from multiple internal and external factors. Supporting private-sector participation, research also found that "increased outsourcing to the private sector provide[s] long-term benefits" in water sector reform.

Moreover, the issues paper directly recognises the importance of procuring services from the private sector to support the operation of LWUs, referring to testimony from the NSW Water Directorate to the Joint Select Committee on Protecting Local Water Utilities from Privatisation. The Water Directorate serves as the peak body providing independent advice in assisting NSW Regional Councils with water and sewerage technical

support and advocacy to all levels of government. In his testimony, Mr. Brendan Guiney, the Water Directorate CEO, encourages a progressive understanding of ownership through the lens of LWUs retaining “ownership and decision-making.”

Mr Guiney recognises the practical consequences of Sydney Water and Hunter Water's approach of “outsourc[ing] their operations and supplies to a far greater degree than local councils” with the private operation of water treatment plants. He acknowledges that a long-term lease that allowed a Council or LWU to maintain certain decision-making controls and powers would meet the test of “ownership and decision-making”.

Indeed, the importance of not only outsourcing but also the centrality of funding mechanisms to the efficient operation of water utility activities is reflected in the recent NSW Constitution Amendment (Sydney Water and Hunter Water) Bill 2023. The Amendment limits the concept of ownership to the enablement of the “main undertaking” of a water corporation, affording the water corporations the ability to privately fund and transact on assets if it is “in the ordinary course of business of a water corporation and results in the main undertakings of the water corporation remaining in public ownership.” The substance of the Amendment ensures that water utilities can access efficiencies provided by and share risk with private partners for corporate and operational activities, including funding and outsourcing, as long as fundamental control of overall purpose and strategic intent vests in the water corporation.

To give LWUs equal funding options with their water corporation counterparts, we ask the Productivity Commission to consider genuinely private participation in funding as a viable complement to public funding, in the same way that current LWUs maintain outsourcing as necessary for delivery and operations for Councils.

Models that include private funding participation should be considered viable solutions in a portfolio of options that best suit a region or Council's local context. In these models, there is no reason why LWUs and the State cannot retain decision-making controls while sharing financial risk with private investment partners in the same way they access effective and efficient private support through outsourcing.

Strong oversight is a common feature of successful water sector reform. Public governance and independent oversight supported by performance monitoring and reporting for continuous improvement can enable complementary public and private contributions for better outcomes. Public leadership with private support across the infrastructure lifecycle, including investment, can energise innovation across key dimensions to create sustainable regional utilities:

- 1) **Technical Expertise, Training, and Knowledge Transfer:** Efficient costs are linked to the individual utility's capability. Collaboration with private partners can connect local utilities to global networks, increasing overall regional capability and leading to greater local efficiency.
- 2) **Broader Collaboration:** Diversity of thinking from multiple backgrounds across an ecosystem of public and private stakeholders supports more innovative decision-making and more effective implementation.
- 3) **Whole-of-lifecycle Funding Considerations:** For at least a generation, private operators, owners, and investors have been participating in creating greater efficiency through outsourcing. Private stakeholders know all the ingredients required for successful commercialisation and corporatisation. Including private investors and funders in the solution complements efficient operation with efficient deployment of funding models, truly balancing long-term and short-term considerations across the entire infrastructure lifecycle.
- 4) **Scale:** Unlock smart execution at scale by balancing what can be consistent across regions and what needs to be localised to be successful. Looking at regional models like QWRAP, why limit technical

expertise to public entities within a region? Access to private-sector networks can unlock economies of scale without the need for amalgamation. Equally, no business problem is unique. Private-sector networks can also support local uplift for capabilities needed to address local context, providing efficient pathways for ensuring consistent services despite variability in capabilities, size and structure of LWUs.

- 5) **Transparency:** Investors and operators in the NSW market are familiar with independent oversight by IPART through the WIC Act. IPART's participation ensures the transparency of the process for governments and the emphasis on promoting customer value.

We submit that funding arrangements that include private participation across the dimensions outlined above can efficiently and effectively assist local water utilities in achieving short- and long-term sustainable performance. This can be done through collaboration, knowledge transfer, whole-of-life cycle considerations, and transparent management practices.

We recommend implementing a pilot program for private participation in funding for LWUs. While the Issues Paper notes commercial debt funding represents an under-utilised option and debt-to-equity could likely increase for many LWUs, we recommend a broader approach that includes participation that

- maintains the principles of public decision-making and control,
- focuses on outcomes, encourages innovation and provides flexibility in meeting the needs of LWUs and
- helps build an evidence base of what actually gets the intended results most efficiently with the least risk in openly considering opportunities for long-term private investment through vehicles across capital market offerings.

We recommend the pilot considers a holistic, long-term approach to private investment participation across the infrastructure lifecycle aligned with the following principles:

- 1) Understanding ownership through the frame of public control and decision-making that balances local concerns and service levels with the efficient deployment of funding;
- 2) Funding participation focusing on alignment of incentives to deliver minimum service levels for regional communities in the most efficient manner;
- 3) Remaining open to a broad consideration of appropriate investment vehicles and structuring;
- 4) Allowing breadth and longevity of private participation, balancing short and long-term considerations;
- 5) Sharing of risk where it is most effectively managed to create more efficient delivery;
- 6) Balancing regionalisation to capture economies of scale with relevant capabilities "at the edge" to address variations in local context; and
- 7) Partnering for continuous learning to foster continuous improvement.

Please do not hesitate to make contact if you have any questions or require more information.

Yours sincerely,

