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Via email: LWUReview@treasury.nsw.gov.au

NSW Productivity Commission

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Orana Water Utility Alliance Technical Committee submission – March 2024 *Inquiry into Alternative Funding Models for Local Water Utilities in NSW*

Thank you to the for the **NSW Productivity Commission** for the opportunity to provide a submission.

The Orana Water Utility Alliance represents 13 local government owned water utilities (LWU's) in the Orana and Far Western Region of NSW. These utilities include the [Councils of Bogan, Bourke, Brewarrina, Central Darling, Cobar, Coonamble, Dubbo Regional, Gilgandra, Mid-Western Regional, Narromine, Walgett, Warren and Warrumbungle](#). These utilities provide safe drinking water and sewerage services to over 105,000 people, across 257,000 square kilometres via over 43,000 water and sewer connections. The Objectives of the Alliance and information on its activities can be found at: <https://owua.net/>

Amongst these LWU's are some of the most drought vulnerable and socially disadvantaged communities in NSW. Our member Councils have long held the view that water management in NSW is best facilitated by the Local Government ownership model. While saying this we acknowledge that there are always opportunities for improvement. The majority of the member Councils operate with a water and sewer team of less than 10 people. These people are usually made up of dedicated locals, especially the operational field staff.

In the last few years, regional NSW has experienced unprecedented impacts on water security and water quality arising from drought, bushfire, water quality challenges and the COVID-19 pandemic. By the end of 2019, the worst drought in 130 years of records saw numerous regional community water supplies at high risk of failure.

The OWUA believes that all state government water related agencies need to collaborate and invest in water utility resilience with regional water providers through capacity building, improved water utility risk management and non-asset solutions such as digital technology and improved access to water operator training in regional NSW.

Our submission

Forced amalgamations

While we acknowledge the current governments commitment to there being no forced amalgamations and that, this is a critical assumption in this inquiry we believe it is worth stating the position of the OWUA on this matter. The OWUA supports the long-held position of Local Government NSW opposing forced amalgamation. We support collaborative models at a regional level between councils to retain local community involvement and control over water and sewerage services.

This model can be enhanced by regional water alliances between LWU's, which can be facilitated through the local government Joint Organisations and Alliances model.

The OWUA recommends that the NSW government consider delivering permanent ongoing funding for regional water alliances of councils to assist them with delivering efficient water and sewerage services.

Alliance replies to questions raised

Challenges from current funding models:

1. What are the key factors that affect local water utilities' ability to recover costs through user charges?

We believe the key factors that affect cost recovery through user charges are:

- The limitations placed on LWU's by the impacts of the ongoing inflation driven price spiral is affecting all business endeavours in remote and regional areas of NSW.
- The massive jump in energy charges and associated costs are one of the biggest reasons why LWU's are all struggling at the moment.
- The ever-increasing maintenance and operating costs of large and at times ageing and non-fit for purpose infrastructure is another reason most remote utilities struggle. This includes the use of large quantities of chemicals and the associated transport costs.
- Socio economic disadvantage and the lack of economies of scale are the key factors that have a large impact on the ability of many remote and rural centres to obtain full cost recovery. This is perverse in that these areas are often large contributors to the State economy via agricultural endeavours that require townships for support.
- The increase in health and environmental regulatory requirements and the consequential increase in minimum quality standards have also had a direct impact on costs over the last two decades.
- Climate impacts on water usage – both drought and extended wet weather has an impact. Years of sustained drought led to a lack of income due to constant water restrictions and decreases in income from usage charges. This is reversed in wet years again by a decrease in consumption.
- High fixed costs – creating higher depreciation and higher costs for the servicing of borrowings.
- Recovery from bushfire and flooding – water and sewerage infrastructure is not eligible under DRFA for any form of subsidy.

2. What might be reasons for some local water utilities with similar size and remoteness to perform differently in terms of level of cost recovery?

The reasons why some LWU'S of comparable size and remoteness perform differently in relation to cost recovery are:

- Differences in socio economic circumstances vary greatly especially in the very remote areas with local incomes often tied to the presence of industries such as mining, power generation etc.

- The performance of agricultural enterprises from season to season can also have a massive impact on the community's income and ability to pay.
- The setting of user pays charges from one LWU to another can often vary dependent on the financial circumstances of the community itself and an assessment by the utility of what its consumers can afford. This is a problem that is not well recognised within the parameters of current long-term financial planning principals. This was never more obvious than the impacts seen on LWU's during the COVID Pandemic. Inflexibility is one of the major failings of the current system of financial management which has been imposed on the industry via the current best practice model.
- The current FINMOD system is over two decades old and has not been reviewed to align with current financial approaches and circumstances. A review has been promised for some time now and it is the belief of the OWUA that this should occur as part of or in conjunction with the outcomes of this investigation.
- The success of an LWU in cost recovery is all too often influenced by the condition of its infrastructure. Therefore, some centres with older and more expensive to operate infrastructure struggle to maintain financial equilibrium.

3. What are key challenges with obtaining funding for water and sewerage infrastructure upgrades and investment?

Key challenges in obtaining funding for water and sewer upgrades and investment are:

- The Current grant system (safe and secure) excludes many smaller communities due to its rules relating to the Eligible Risks and Issues List (ERIL) score which derates risk for towns with population less than 2000. This means that the Productivity Commission does not have an accurate picture of risk and **underinvestment in essential infrastructure for small populations in remote and regional NSW.**
- The fixed co-funding scale of safe and secure funding bands can strongly disadvantage some utilities with some small utilities of between 2000 and 4000 connections falling over an arbitrary cut offline between 90% and 75% funding (**see Table 1**). This can be created by as little as an additional \$10,000 of revenue. Another difficulty with this system is that the revenue assessed for this determination is the average of the total combined income of both Water and Sewer funds over a three-year period. The impact of this model is that utilities that could or should attract 90% funding for either a water or a sewer project in fact may only receive 75% funding due to the **combined revenue of both funds being the deciding factor.**
- Funding so far has only been sufficient to address Level 5 risks under the (ERIL) systems appropriately to communities with the greatest socio-economic disadvantage. The remainder of Risk Level 5 projects were funded to achieve 'shovel-ready' status without any commitment to construction funding. It is important to mention that LWU's are often overlooked as funding partners. Investment in pre-construction investigation and design to achieve shovel-ready status can result in a small LWU having its pre-construction investment stranded for many years, with construction cost escalation inevitable.
- The other difficulty for small rural and remote utilities is that they have limited avenues for water and sewer funding. Unlike Roads that have multiple funding grants and opportunities from state and federal government, opportunities for water and sewer are not as common. Also, funding almost always required a contribution – this isn't the case for most road and other infrastructure grants

There can also be unintended consequences with the above approach where a Local Water Utility increases revenue to improve cost recovery but reduces its eligibility for capital funding by improving its position with the result of better management moving it into a lesser funding band.

Table 1. Program subsidy levels for local councils and local water utilities.

3-year average combined* revenue of proponent (from water and sewerage) 2016/17 to 2018/19	Safe and Secure Water Program funding band
> \$20,000,000	Up to 25%
> \$10,00,000 to \$20,000,000	Up to 50%
> \$5,000,000 to \$10,000,000	Up to 60%
> \$2,500,000 to \$5,000,000	Up to 75%
<=\$2,500,000	Up to 90%

* The three-year average combined revenue shown in Table 1 is for combined water and sewerage for 2016/17 to 2018/19 financial years. Where an organisation provides either water or sewerage services only, the actual revenue is doubled before applying the funding bands.

The three-year average revenue received for the provision of water and sewerage services is used for subsidy calculation purposes and the current eligible subsidy per eligible organisation is available by [emailing the program](#). The department may review subsidy bands periodically.

Table 1

Funding model principles:

4. What factors should be taken into account in calculating government subsidies for local water utilities?

There are many factors that should be considered in relation to ensuring the equitable distribution of financial assistance for everyday operation of Local Water Utilities if it were to become available.

- Socio-economic status of the community and its ability to provide services to a poorer community
- The relative cost of the service (economies of scale and remoteness)
- Local Water Utility capacity to deliver operational and capital work
- Risk of service level failure compared with the ability to self-fund solutions

The member utilities of the OWUA know from their years of operation that there are much higher costs of operation and capital delivery in remote parts of NSW by comparison to those of the utilities along the seaboard.

We acknowledge that a risk-based approach is important to prioritise funding toward the areas of highest need. There is however a different level of risk that emerges with the socio-economic impact on the whole state of NSW itself being high should a major service failure of any utility in the OWUA Region jeopardise sustainability of small communities especially those supporting mining and agricultural industries.

5. What might be the typical costs for delivering water and sewerage services for a well-run local water utility?

Typical residential bills can be constructed using numerous data points, the problem with this approach though is that there is no typical cost to deliver water and sewerage services due to the wide range of operating environments that are beyond the control of the LWU. This includes geographic distance between population centres served, climate, hydrology, management of shared water sources, infrastructure required per capita, and short-term servicing needs such as tourism.

Another issue in this space that is often overlooked when assessing and comparing typical costs is that not all water sources are the same and varying security and sources of supply play a big part in the costs associated with water production and supply. This means that there can huge variations from one utility to another in things such as

- Maintaining reservoirs and pipe networks
- Water quality testing
- Staff training
- Reporting and monitoring for regulatory requirements
- EPA licencing costs
- Water costs (Water NSW)
- Chemical and freight costs

Water utility costs are very dependent on climate impacts and can vary significantly from a wet year to a dry year especially in remote areas of the state. It also should be noted that many LWU's are delivering a lower level of service due to operational funding constraints.

6. What indicators could be linked to funding to drive ongoing performance improvements and deliver value for money for customers?

One of the consequences of the current operating environment are that the incentives to achieve constant improvement are minimal. An unfortunate side effect of this system being that poor performing utilities are often more eligible for state supported capital funding for major asset replacement and renewals. Real time data plays an especially important part in empowering engineers and operators to intervene. Prevention is better than the cure in service failures – reactive maintenance can cost up to 3 times as much as planned maintenance and asset renewal programs.

Performance data has become so important to our regulators (DCCEEW) that over 600 data points are now required in NSW to benchmark utilities. These points are geographically aggregated and annualised. Many of these data metrics are beyond the control of LWU's such as climate, geographic distance, catchment features and energy costs.

The position of the OWUA is that funding indicators should be based on the principals of assisting and enabling LWU's to achieve health and environmental standards and to practice quality asset management standards as a minimum.

Minimum service levels:

7. Should the minimum service levels be applied universally to all towns within the area serviced by a local water utility, irrespective of size, remoteness, or cost?

It is the position of the OWUA that everybody in NSW deserves safe, reliable, and affordable water and sewerage services. Small communities deserve equitable access to these critical and essential services. Local government is best positioned to deliver these services in regional NSW. The idea that there should be different service levels between different communities in Australia is morally challenging. Realistically however it is acknowledged that not all small communities have access to reticulated water and sewerage services, with a basic service level being a roof-connected rainwater tank for their water supply and an on-site sewage management system (such as a septic tank) for managing wastewater. Basic services such as these inherently have a higher risk of failure to meet drinking water health standards or environmental protection standards, respectively. The OWUA believe more attention could be paid to mitigating risk for un-serviced communities. An example of where this has been achieved is in the improvements made to discreet Aboriginal Communities in NSW in provision of these services.

It is also the position of the OWUA that the costs of incident management especially as it relates to support in droughts, as in the trucking of water, need to be factored into decision making on funding and approving of capital works in remote communities. The maintenance of minimum health standards to these communities can be downgraded or compromised due to funding constraints as the cost to these communities can be significant if this happens. It is a known fact that a boiled water alert in a community of 800 people has cost over \$30,000 per day, this was because of a lack of operational funding to maintain simple risk management principals.

8. What metrics should be considered in minimum service levels?

There should be no reason that the metrics required to be met by NSW city-based utilities or those of rural, remote and some private utilities in other jurisdictions with regard to quality and reliability of service should not be considered for adoption. It is important though to account for matters beyond an LWU's control. For example, upstream catchment water quality needs a whole-of-catchment, multi-agency and community-oriented approach. For most regional LWU's, water crosses many boundaries. Water NSW has a significant part to play to assist LWU's with real-time water quality data and an awareness of water quality impacts from operations to mitigate drinking water quality risk in regional NSW towns.

The OWUA firmly believes that it isn't wise to simply impose a higher regulatory standard without a multi-agency technical and funding support approach. This support – especially access to specialist skills – will be required regardless of the funding model or institutional structure.

9. What is the existing evidence on current basic service levels, customers' needs for minimum service levels and willingness to pay in regional and remote communities?

There is little or no publicly available evidence to support any claim on either side of this argument. Customer service surveys are also well known to be unreliable in small populations where special interest groups can sway views simply by having the loudest voice. These factors must not detract from the need for basic water and sewerage services at an affordable price to be available in small and remote communities.

Rural communities generally pay higher charges whilst not achieving full cost recovery that includes the total cost of ownership of water and sewerage infrastructure. Often this problem is unfortunately, exacerbated in some communities through the Safe and Secure Water Program and / or its predecessor the Country Towns Water and Sewer Program. This is often due to over design and over engineering of expensive assets based upon traditional out of date public sector principals.

These high-cost assets are generally not fit for purpose and tend to incur higher costs for operation and maintenance with LWU's generally shouldering the costs and blame when these gifted assets don't perform or fail prematurely.

Capital construction costs of these assets are regularly blown out by the requirement for multiple reports, studies and the excessively prescriptive nature of the strategic planning and approvals process should a LWU wish to stray from the established norm.

This has been reviewed during the Town Water Risk Reduction Program (TWRRP1) but is yet to show any improvement. Most small communities are happy to pay for safe clean drinking water and sanitary services, they are often though left shouldering higher costs due to the issues outlined due to failed gifted infrastructure.

The requirements to meet the Australian Drinking Water Guidelines (ADWG) under the Public Health Act 2010 (NSW) and the Environmental Protection Act can be achieved by small LWU's. This can be done by the use of new lower cost high-tech solutions in both capital and operational settings. These types of solutions can and are regularly adapted for use in remote settings in other jurisdictions and in the private sector.

There is unfortunately a long-held view amongst regulators in NSW that solutions must be large, dumb, and built totally of concrete and steel to be considered a robust solution. The excuse for not adopting new tech given being that operators in remote and rural settings can't operate smart solutions. It is obvious no matter what solutions are decided upon, Typical residential bills can be constructed using numerous data points, the problem with this approach though is that there is no typical cost to deliver water and sewerage services due to the wide range of operating environments that are beyond the control of the LWU. This includes geographic distance between population centres served, climate, hydrology, management of shared water sources, infrastructure required per capita, and short-term servicing needs such as tourism.

10. What are the barriers to setting measurable service levels?

The infrastructure, and the financial and technical capacity of LWU's in NSW to meet the service levels are not known explicitly at a granular level required to set measurable KPI's. A State of the Assets report for LWU's, reporting on technical and financial performance would be an important first step in any attempt to do this. This should include the costs to provide water and sewerage infrastructure for unserved communities.

Again, we cannot stress enough the importance of a consistent multi-agency regulatory approach being in place to compare the socio-economic costs against the benefits of increasing regulatory standards year-on-year. We believe that trade-offs would inevitably be required between social, financial and environmental requirements. Any assessment should avoid distantly conducted desktop scenarios and must use real-world examples and data to be in anyway representative.

It is too our firm belief that in a first world country such as Australia there should never be two significantly different levels of service anywhere based on equitable and affordable access to a service that is essential to human life. In the age of social media and connectivity communities are no longer willing to accept lesser services when it comes to basic human needs and rights.

11. What are challenges with monitoring and reporting against minimum service levels?

Most small and remote LWU's already point to significant burdens in the reporting requirements of the numerous regulators being a major challenge. This is often as not because the engineering staff in these utilities are limited to one person to cover all activities in the business unit. Other challenges can be due to the operating context and environment faced by and within which the utility operates.

Some utilities are known to provide lower levels of service due to attempting to stay within financial means this is usually done in the first instance by not maintaining infrastructure and then as equipment fails by the down rating of service levels.

Alternative funding options:

12. What are the desired outcomes for addressing the challenges currently faced by local water utilities?

The key outcomes should be for all communities to have access to safe and affordable water supply and sewerage services across NSW, with consumer costs comparable to metropolitan areas. In achieving this, there needs to be a clear understanding of what service level is to be provided to each community and how it is to be funded. In seeking this outcome, it must be understood that One Size does not fit all and that there are a large variety and diversity of operating environments in which LWU's operate and therefore many differing levels of service and therefore levels of funding required.

The most desired outcome the OWUA would like to see is an increase in state and federal funding, without co-contributions.

Increased assistance and support around founding and operating alliances, joint organisations and increased support for smaller regional and remote utilities again free of the need for co-contribution.

13.What are obstacles to greater use of loans from financial institutions to fund infrastructure investments in water and sewerage services?

Debt taken on by LWU's affects the financial position of the Council as a whole. In 2015/16 this affected Fit for the Future metrics that drove amalgamation of councils. Another obstacle is the size of an LWU relative to size of debt being taken on for a major project, most commonly to match the funding mix required by the Safe and Secure Water Program. As a result of the above, most small and rural Councils tend to not want to incur debt by taking loans.

14.What measures would drive investment planning that takes account of climate change risks and ongoing costs of infrastructure maintenance?

In replying to this question, we would refer to recent climatic events such as the Black Summer bushfires in 2019-2020, coinciding with the worst drought in 130 years of measurements and subsequent record flooding in 2021 and 2022. Infrastructure standards should be reviewed and updated to improve resilience against climate events based on lessons learned from the last 5 years, including drought management and contingency planning.

15.Who are most at risk from high water bills in regional, remote, and metropolitan New South Wales?

During the current cost of living crisis, in Australia it is inevitable that anyone can be at risk due to higher utility bills. Much is being made of this at all levels of government and industry. It is the belief of the OWUA that the NSW Government should fully fund the pensioner rebates schemes for all LWU's across NSW consistent with the assistance provided to the SOC's and their customers. Pensioners and other highly marginalised persons who are living at or below the poverty line should never be denied the benefits of safe clean drinking water and sanitation.

There is a significant inequity in pensioner rebates between the two SOC's of Sydney Water and Hunter Water, and the regional LWU's. The SOC's have \$650 and \$380 pensioner rebates respectively, which are both 100% covered by the NSW Government through a CSO payment, yet regional LWU's have a capped pensioner rebate of \$175 per customer (\$87.50 each for water and sewer) with the NSW Government only covering 55% of this.

There has been no increase in this rebate since 1993, and the Issues Paper notes that if this rebate had been increased with CPI it would be worth around \$390 per year in today's dollars.

There are hidden risks based on other factors:

- When LWU's take on large new assets there are increased costs of operation, depreciation and servicing of borrowings that need to be covered with higher bills
- The 'infrastructure cliff' when a town was provided with services via donated assets at a point in time some decades ago and the assets reach the end of their useful life at a similar point in time.
- Disaster recovery costs with water and sewer assets ineligible for DRFA funding if the service charges are more than 50% of the cost of delivering the service.
- The demand for increased service levels due to increased regulatory expectations and standards

16.What are examples of projects or operations associated with a funding model based on regional collaboration for local water utilities? What were the challenges?

There are many examples of successful regional collaboration across regional NSW the OWUA and its predecessor the Lower Macquarie Water Utility Alliance being among these. Other successful entities such as the Central NSW Joint Organisation Water Utilities Alliance and The Namoi JO Water Alliance have been highly successful within the Regional NSW settings.

The challenges are insufficient funding to fully resource these organisations. With better funding and full-time personnel to serve and promote regional Alliances many more joint capital projects and non-capital operational support services could be created. In some parts of NSW there is a lack of political will to drive and facilitate regional collaboration between Local Water Utilities.

17.What has worked well and what have been challenges for local water utilities in leveraging the scale and expertise of State-Owned Corporations?

As an Alliance the OWUA has had no direct interaction with (SOC's) in aiding our member Councils. What we do know is that they have provided some assistance to one of our member Councils at the instigation of DCCEEW to provide support in a Water Treatment Plant. The plant in question was built in the last decade and is an example of a piece of Infrastructure that was never fit for purpose.

Assisting LWU's is (in most cases) not clearly authorised for State Owned Corporations (SOC's) through instruments such as their Operating Licence as it isn't 'core businesses for a corporation. The SOC's need to have a clear role and mandate to assist LWU's and the mechanism in place for this support to be provided when needed. In addition, there is a lack of problem definition – clearly defined strategies and assistance programs that inform SOC's on LWU needs.

18. How could government and local water utilities better partner with Aboriginal communities to improve their water and sewerage services?

The Aboriginal Communities Water and Sewerage Program (ACWSP) is a \$200 million program⁹ operating since 2008 partnering between the NSW government, NSW Aboriginal Land Council and Local Water Utilities to improve water and sewerage infrastructure for 63 eligible Aboriginal communities. THE ACWSP provides a platform for further partnerships to deliver improved service levels and increase Aboriginal participation in the program. The general consensus of the members of the OWUA member Councils who are involved in servicing these communities see the program as a vehicle delivering outcomes.

Concluding comments

The OWUA believes that developing a new alternative funding model for regional Local Water Utilities would represent a transformational opportunity for regional communities in NSW. We would strongly support a needs-based, evidence-based approach to assist socio-economically disadvantaged communities that lack access to economies of scale. It is important to generate a better balance between capital and operational support in the new model. The existing bias toward capital support has led to many unusual and unintended consequences.

A sustained long-term state investment in budget support for water and sewerage services to complement capital project subsidies will not only assist regional communities but will ultimately flow back to the state through improved economic development. We believe the optimising of whole-of-life costs of water and sewerage infrastructure is critical.

A concentrated focus on risk reduction through funding support of non-capital solutions via the Water Utility Alliances would be a huge gain. Things such as providing regional digital solutions in systems such as satellite internet services, digital management of data, leak reduction systems, smart metering services would be nothing but positive for regional, rural, and remote utilities. A key and critical add on would be integration into the Bureau of Meteorology, Water NSW and State Emergency early warning systems for rural and remote utilities to assist in avoiding major Water Quality incidents and being able to deal with major incidents and disasters.

The other and most critical area of support key in setting up an alternate funding model is support and assistance to Alliances and others in setting up and maintaining regionally and On Country based Training Centres for the ongoing education and training of all levels of LWU staff especially treatment plant and network operators.

The OWUA would like to thank you for the opportunity to make this submission and for your efforts in visiting and meeting with people from our region. Should any further information be required, I can be contacted via our Alliance Project Officer Georgie Sheridan.

Yours sincerely



Technical Chairman

On behalf of Orana Water Utilities Alliance Technical Committee