



ACT
Government

2015

**THE LEGISLATIVE ASSEMBLY
FOR THE AUSTRALIAN CAPITAL TERRITORY**

**Government Response to the Final Report – Pricing of Regulated Water
and Sewerage Services: Review of the Regulatory Framework
(The Grant Review)**

Background

The review of the water and sewerage pricing framework was instigated by Government in late 2014, to action its commitment to review the overall framework, made as part of its formal response to the *Auditor-General's Report: The Water and Sewerage Pricing Process Report No.2/2014* (the Auditor-General's Report).

The Government commissioned Mr Peter Grant PSM to undertake this review (the Grant Review), and his final report was submitted to the Government in February 2015. The Government has now considered the findings of the Grant Review, and the following response outlines the position of the Government in regards to each recommendation made by Mr Grant.

Overarching Government Comment

The Government recognises that the current regulatory model and framework has served the Territory well since its introduction in 1997. The implementation of the improvements proposed in the Grant Review will be expected to improve the operation of the regulatory model in advance of the next major pricing investigation related to regulated water and sewerage services.

The recommendations made in regards to governance and accountability arrangements are aligned with the Government's intention to improve the regulatory framework for water and sewerage pricing.

The Government recognises that the legislative framework has provided a strong foundation for the operation of the regulatory system. However, the Government notes that there are a number of issues created by the current drafting of the *Independent Competition and Regulatory Commission Act 1997* (the ICRC Act) that should be rectified. The Government will also utilise this opportunity, in consultation with key stakeholders, to refine and improve as appropriate other parts of the legislative framework for the provision of regulated pricing services in the ACT.

The Government recognises that resourcing matters are a significant issue for the Independent Competition and Regulatory Commission (ICRC), and that variability within workloads and swings in the resourcing base of the Commission have contributed to the issues highlighted in the Grant Review. As part of the 2016-17 Budget process, the Government intends to reconsider the overall resourcing arrangements for the ICRC.

However, the Government is not convinced that the current regulatory model represents the best approach to the provision of regulated pricing services in the Territory in the medium to longer term, especially in relation to ensuring cost effectiveness of regulatory processes.

Therefore, the Government will undertake further work to consider potential options for reforming the regulatory model in the medium term. This will include comprehensive consideration of whether an alternative model, more tailored to the circumstances and needs of the Territory could improve the efficiency and value for money associated with the regulatory pricing process.

Recommendation 1: The regulatory framework

Recommendation 1a

*The review **recommends** that the ACT Government:*

(a) retain the current regulatory framework at least for the time being, while pursuing the various changes and improvements recommended elsewhere in this report.

Government Response

Agreed.

The Government will in the short term seek to strengthen the current regulatory system, in order to resolve identified flaws in the administrative and legislative framework, and to improve accountability arrangements for both the Independent Competition and Regulatory Commission (ICRC) and Icon Water Limited.

This will include implementing many of the changes and improvements contained within Recommendations 2, 3 and 4 of this review. These changes will strengthen the current regulatory system and help to ensure its effectiveness during the upcoming regulatory pricing investigation for regulated water and sewerage services.

The Government will also undertake further work to consider potential options for alternative regulatory models that could be implemented in the Territory in the medium term. This consideration will seek to determine whether an alternative regulatory model, tailored to the particular circumstances of the Territory, could deliver improved outcomes in regards to the efficiency and value for money associated with regulated pricing processes.

Recommendation 1b

*The review **recommends** that the ACT Government:*

(b) keep open the option of a 'contracting out' arrangement, to be activated in the event that it is not satisfied with the adequacy or speed of progress made in implementing any agreed changes arising from this review.

Government Response

Agreed.

As outlined in the Government's response to Recommendation 1a, the current regulatory model will be maintained for the time being.

The Government will, within its consideration of potential options for reform to the regulatory model in the medium term, consider in depth the potential for a 'contracting out' arrangement to be incorporated into an alternative model for the provision of regulated pricing services in the Territory.

Recommendation 1c

*The review **recommends** that the ACT Government:*

(c) reserve the options of a price monitoring regime and the transfer of price-setting powers to a new national regulator for more detailed evaluation in the longer term, when conditions require or are appropriate.

Government Response

Agreed.

The Government considers that in the short to medium term, the emergence of a new national regulator for regulated water and sewerage services is unlikely. Such an approach to regulation will be considered if it becomes part of a future national reform agenda.

The Government does not consider it would be appropriate at this time to seek to proactively move to a price monitoring regime. However, the Government considers that as the regulatory system continues to develop, a key focus for all stakeholders should be on a gradual move, as judged appropriate, towards lighter handed regulation. Such an approach could help improve regulatory outcomes and in time reduce regulatory burden and costs.

Recommendation 2: Governance and accountability arrangements

Recommendation 2a

*The review **recommends** that, if the current regulatory framework is to continue, the ACT Government should play a more direct and proactive role in supporting the operation of the regulatory system by:*

- (a) strengthening the current accountability arrangements applying to both the ICRC and Icon Water Limited.*

Government Response

Agreed.

A strong governance and accountability framework is central to the ongoing successful operation of the regulatory framework. Therefore, the Government will undertake consideration in consultation with both the ICRC and Icon Water of what steps should be taken to strengthen the accountability framework.

Recommendation 2b

*The review **recommends** that, if the current regulatory framework is to continue, the ACT Government should play a more direct and proactive role in supporting the operation of the regulatory system by:*

- (b) providing an annual 'statement of expectations' to the ICRC, designed to make clear its requirements and expectations of the Commission without impinging on its statutory independence. After consultation with the responsible Minister, the ICRC should respond by preparing a 'statement of intent', which would then be the basis of a formal agreement between the Government and the Commission. The objective should be a clear set of expectations and common understandings as to what the regulator is to be held accountable for, and how it should conduct its business.*

Government Response

Agree in principle.

In September 2015, the Financial Management Amendment Bill 2015 was passed by the Legislative Assembly, which amongst significant amendments to the *Financial Management Act 1996* included changes to the overall operation of the statement of intent process for government agencies and statutory authorities.

The Government agrees that there is a need for it to have a more proactive role in setting the higher level expectations and objectives for the ICRC. The Government will undertake further consideration of potential options for achieving this outcome, including the proposed statement of expectations outlined within this recommendation.

Recommendation 2c

*The review **recommends** that, if the current regulatory framework is to continue, the ACT Government should play a more direct and proactive role in supporting the operation of the regulatory system by:*

(c) taking a more active role in setting the high-level framework for a pricing investigation.

Government Response

Agreed.

The Government agrees that a more active role for it within setting the high-level framework for regulated pricing investigations would be beneficial.

The Government will work with the ICRC to determine the optimal approach to achieving this objective, in order to balance the need for greater Government involvement with the need for appropriate recognition of the statutory independence of the ICRC, including in regards to the approach utilised in regards to major pricing investigations.

Recommendation 2d

*The review **recommends** that, if the current regulatory framework is to continue, the ACT Government should play a more direct and proactive role in supporting the operation of the regulatory system by:*

(d) ensuring that the ICRC is well prepared and equipped for the conduct of its future pricing investigations.

Government Response

Agree in principle.

Both the Auditor-General's Report and this review have identified that a key contributing factor to the issues that impacted on the effectiveness of the previous pricing determination process for regulated water and sewerage services was that the ICRC was not adequately prepared and equipped for the investigation.

The Government, as part of the 2016-17 Budget process, will reconsider the current resourcing arrangements for the ICRC.

Recommendation 3: The legislative framework

Recommendation 3a

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

- (a) to insert an overarching objects clause into the Act which makes it clear that the primary objective of the regulatory framework is to promote the goal of economic efficiency, while safeguarding the financial viability of the regulated entity.*

Government Response

Agreed.

The Government considers that significant benefit would be derived from the insertion of an overarching objectives clause into the ICRC Act, which identifies and clarifies the key objective underlying economic regulation.

The Government will undertake further consideration of the exact form of the objectives clause, including whether it should be reflective of an existing objectives clause, for example the National Electricity Objective.

Recommendation 3b

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

- (b) to confer on the Minister the power to determine the period over which a price direction is to apply, but with an option to delegate this decision to the ICRC.*

Government Response

Agreed.

The Government will seek to rectify the inconsistency within the ICRC Act identified in regards to the determination of the regulatory period for a price direction, by introducing legislative amendments that would explicitly confer on the Minister the power to set the regulatory period, or alternatively to defer this power to the ICRC, if deemed appropriate.

Recommendation 3c

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

- (c) to clarify that the requirement imposed under subsection 20(4) applies equally to a proposed price direction as to a final price direction; in both cases, the Commission must indicate the extent to which it has had regard to the matters listed in section 20(2).*

Government Response

Agreed.

The Government will seek to amend the ICRC Act to ensure that the requirements imposed on a final report of a pricing investigation and the final price direction, as outlined in section 20(4), are equally applicable to a draft report and draft price direction. This will help ensure clarity around the expectations of the contents of a draft report, while also simplifying the operation of the ICRC Act.

Recommendation 3d

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(d) to require that the terms of reference for a pricing investigation be issued by the Minister a specified number of months before the expiry of a current price direction.

Government Response

Agreed.

The Government considers there is merit in setting a minimum period before the expiry of a current price direction that the Terms of Reference for the next pricing investigation must be issued by the Minister.

The Government notes the need for a distinction to be made in regards to the minimum period for the two major pricing investigations currently undertaken by the ICRC - being price determinations for retail electricity prices for small customers and regulated water and sewerage prices in the ACT.

Recommendation 3e

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(e) to provide that the terms of reference for a pricing investigation may specify a date by which a draft report and proposed price direction are to be made available for public inspection.

Government Response

Agreed.

The Government considers it reasonable to introduce the ability for the Terms of Reference for a pricing investigation, if considered appropriate by the responsible Minister, to specify the date by which a draft report and draft price direction must be released by the ICRC during a pricing investigation.

Recommendation 3f

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(f) to require the ICRC to publish a statement of its information requirements within one month of receiving the terms of reference for a pricing investigation, and the regulated entity (and any other relevant parties) to provide the required information within the time period specified in the ICRC's statement.

Government Response

Agreed.

The significant issues that occurred during the last pricing investigation for regulated water and sewerage services in relation to the information requirements of the ICRC clearly highlighted the need to introduce greater clarity where possible in relation to the information required by the regulator early in the process.

The Government considers the recommended amendment represents a reasonable approach to ensuring that a clear statement of information needs is made at an early stage of a pricing investigation, which outlines clearly to Icon Water the information needs of the ICRC.

Recommendation 3g

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(g) to give the Minister a power to establish a dispute resolution process on a procedural matter if, after receiving a written request by either party, the Minister judges this to be the most effective and efficient way of resolving the dispute.

Government Response

Noted.

The significant disagreement about information provision that occurred between the ICRC and Icon Water Limited during the last pricing determination process was not conducive to the effective operation of the regulatory framework, or to ensuring that regulatory costs are minimised. The Government considers there would be merit, in circumstances of significant disputes over procedural matters, for there to be the possibility of the use of an independent arbitrator.

The Government however will not seek at this time to implement a formal dispute resolution process, but will retain it as an option in reserve, should future events indicate the need for such an inclusion within the legislative framework.

Recommendation 3h

The review recommends that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:

(h) to give the Minister the power to establish or appoint a review body, once an application for a review has been submitted, but without limiting the form of that review body to the industry panel model prescribed in the current legislation.

Government Response

Agree in principle.

The Government considers that the recently completed Industry Panel process, which reviewed the ICRC's price determination for regulated water and sewerage services from 1 July 2013, demonstrated that the current review provisions within the ICRC Act represent a viable mechanism for undertaking reviews of ICRC price determinations. However the Government will review these provisions, in light of the potential improvements that were identified throughout the Industry Panel process and in the Grant Review.

The Government will also take this opportunity to investigate the merits and possibility of appointing the Australian Competition Tribunal as the review body for hearing applications for review under the ICRC Act. Such an approach may help to reduce costs and increase the timeliness of a review process.

Recommendation 3i

The review recommends that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:

(i) to provide that the appointment of members to an industry panel, or other review body, should be subject to scrutiny by the Legislative Assembly.

Government Response

Agree in principle.

Should the current Industry Panel review model continue (pending the outcome of investigations into the possibility of utilising the Australian Competition Tribunal for this purpose), the Government agrees that any appointment to a future Industry Panel should be subject to scrutiny by the Legislative Assembly.

Recommendation 3j

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(j) to provide that an application for a review of a price direction must be accompanied by evidence that one or more of the following failings has occurred in the initial price determination process:

- a significant error in the application of law;*
- a material error of fact;*
- a material error in calculation or methodology; or*
- a significant failure in due process, procedural fairness or natural justice.*

Government Response

Agree in principle.

The Government will review the current drafting of the ICRC Act in regards to applications for review, including the basis on which such an application can be lodged. This will include a consideration of whether the approach proposed in this recommendation is viable and represents an improvement in comparison with the current review provisions of the ICRC Act.

The Government will also consider whether there may be another well established merit based review framework (such as the review provisions in the National Electricity Law) that could be adapted as a basis for the review provisions of the ICRC Act.

Recommendation 3k

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(k) to require an industry panel, or other review body, to provide the ICRC with an opportunity to respond to the issues and arguments raised in an application for review before any decision is taken on whether a review is to proceed.

Government Response

Agree in principle.

The Grant Review identifies that the omission of an explicit provision for the ICRC, as the original decision maker, to formally respond to the issues and arguments raised within an application for review represents a potential limitation within the current legislative framework. The Government will seek to integrate such a requirement into the overall review framework within the ICRC Act.

Recommendation 3l

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(l) to provide that an application for a review should be dismissed if the evidence presented in the application is found not to be sustained, or not to be sufficiently strong for a review to proceed.

Government Response

Agree in principle.

The Government considers that there is merit in providing the review body with greater ability early within the review process to dismiss an application if it considers that the evidence presented in support of the application can not be sustained or is not sufficiently strong.

Current provisions within the ICRC Act, outside of frivolous or vexatious applications provide the review body with no opportunity to dismiss an application, even if it considers on balance the application is not sufficiently strong enough to warrant a full investigation. This proposed change would improve proportionality within the review system, especially if combined with the proposed change to a merits based review approach.

This approach would however increase significantly the evidence required to be presented in support of an application for review at the initial stage of the process. The Government therefore will seek to further consider the implications of this approach before making a final decision on whether to seek to implement it into the ICRC Act.

Recommendation 3m

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(m) to provide that an individual consumer, group of consumers or any other body with a relevant interest should be able to make an application for a review of a price direction by the regulator, with each party to a review required to bear its own costs.

Government Response

Agree in principle.

The Government will undertake further consideration of the possibility of amending the ICRC Act to broaden the definition of the parties that are eligible to make an application for review, in line with this recommendation.

Such a change would operate in tandem with the proposed change outlined within Recommendation 3l, which would increase the ability of the review body to dismiss an application early in the process, if the evidence presented is not found to be sustained or sufficiently strong enough for a review to proceed.

Within its consideration of this recommendation, the Government will seek to balance the rights of consumers with the costs and reasonableness of the appeals process.

Recommendation 3n

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(n) to provide an option for an industry panel, or other review body, to refer a matter raised in an application for a review back to the ICRC, as the original decision-maker, with directions for the making of a fresh decision.

Government Response

Agreed.

The inclusion of the ability for the review body to refer a matter raised in an application for review back to the original decision maker, with directions, represents a mechanism that can improve the current review provisions of the Act.

Such a mechanism would allow, where appropriate, for a simpler review approach to be utilised in regards to straightforward issues within an application for review, which may help reduce the overall costs associated with undertaking a review of a price direction.

Recommendation 3o

*The review **recommends** that, if the current regulatory framework is to be retained, the ICRC Act be amended as follows:*

(o) to require an industry panel, or other review body, to transfer to the ICRC, on completion of a review, all information it has collected or created in the course of conducting the review which may be relevant or necessary to the Commission's role in implementing and managing a substituted price direction.

Government Response

Agree in principle.

Under the current review provisions, the Government recognises that there is no legislative provision to ensure that there is transfer of information back to the regulator at the completion of an Industry Panel review. The Government, should it maintain the current review provisions, will seek to amend the ICRC Act to address this issue.

Should a more limited merits based approach to reviews be adopted (as proposed in Recommendation 3j) and/or the use of the Australian Competition Tribunal as the review body be introduced, the Government will further consider whether a legislative requirement for information transfer is necessary under that approach.

Recommendation 4: Resourcing arrangements

Recommendation 4a

The review **recommends** that, if the current regulatory framework is to continue, the ACT Government:

- (a) consider options designed to boost the viability of the ICRC so that it is not so exposed to the adverse effects of cyclicalities in its workload and marked swings in its resourcing base. The options to be explored should include the assignment of additional responsibilities to the Commission, a merger with one or more other bodies with related functions, and an increase in the level of budget funding.

Government Response

Noted.

The Government will consider this issue in the 2016-17 Budget process.

Recommendation 4b

The review **recommends** that, if the current regulatory framework is to continue, the ACT Government:

- (b) retain a significant element of cost-recovery in the resourcing of the ICRC, partly as a means of making transparent the costs of its regulatory activity but also as a means of maintaining a cost-conscious culture within the ICRC itself.

Government Response

Agreed.

The Government considers that cost recovery should remain a central part of the overall funding model for the ICRC, and that the provision of transparent information about the costs associated with major pricing investigations should be a key objective.

Recommendation 4c

The review **recommends** that, if the current regulatory framework is to continue, the ACT Government:

- (c) review and rationalise the structure of licence fees payable under the *Utilities Act 2000*, and the revenue derived by the ICRC from this source.

Government Response

Agreed.

The Government agrees that it would be appropriate to undertake a broad reconsideration of whether the current structure of licence fees payable under the *Utilities Act 2000* remains optimal.

The Government will undertake this review at a future time, once the significant changes that will be required under other recommendations of this review are implemented.

Recommendation 4d

*The review **recommends** that, if the current regulatory framework is to continue, the ACT Government:*

(d) provide a single budget appropriation (rather than the current service level agreement) to fund those functions that the ICRC is required to perform but for which it cannot recover costs: for example, research into regulatory approaches and methods, interaction with other regulators, the meeting of accountability requirements, and the developmental work required to ensure that the Commission is well prepared for the conduct of future pricing investigations.

Government Response

Noted.

As part of the consideration of resourcing arrangements for the ICRC during the 2016-17 Budget process, the Government will also consider the best mechanism for providing funding to the ICRC for the non-cost recoverable functions that it undertakes.