26 February 2013

Mr Marcus Crudden
Acting Director, Water
Water Price Review
Essential Services Commission
Level 37, 2 Lonsdale Street
MELBOURNE VIC 3000

Dear Mr Crudden

Water Price Review 2013

The Victorian Council of Social Service (VCOSS) welcomes the opportunity to comment on the Metropolitan and Regional Businesses Water Plans for 2013–2018.

VCOSS is the peak body of the social and community sector in Victoria. VCOSS members reflect the diversity of the sector and include large charities, peak organisations, small community services, advocacy groups, and individuals interested in social policy. In addition to supporting the sector, VCOSS represents the interests of vulnerable and disadvantaged Victorians in policy debates and advocates for the development of a sustainable, fair and equitable society.

VCOSS supports the submission lodged by the Consumer Utilities Advocacy Centre (CUAC) and the Consumer Action Law Centre (CALC). However our views on price paths and inclining block tariffs differ slightly, and are explained here along with some other matters.

Summary

1. *Water businesses proposing non-smoothed price increases should demonstrate their understanding of the impacts on vulnerable customers and their commitment to proactively helping customers in hardship by explaining how they will enhance their hardship programs and payment processes to mediate those impacts and help vulnerable customers adapt to higher prices.*

2. *Water businesses making significant changes to tariff structures should demonstrate their understanding of the impacts on different types of*

customers and their commitment to proactively helping vulnerable customers by explaining how they will mediate the impacts and, where necessary, help vulnerable customers adapt.

3. *Water businesses with few materially improved targets, or with targets consistently less rigorous than the 5-year average, should clearly demonstrate the rationale for the level of their service standards or revise them.*

4. *Water businesses with few or no voluntary GSLs should provide a clear rationale and demonstrate an alternative approach to identify and honour baseline critical service standards.*

5. *The Commission should consider requiring a minimum number of self-defined GSLs.*

6. *The Commission should limit cost offsets from previous periods as much as possible, ensure water businesses make prudent contingencies, and promote a regulatory environment whereby appropriate levels of revenue–expenditure divergence to support such prudence are allowable.*

7. *VCOSS supports the D-factor approach proposed by the metropolitan water businesses for possible use of water from the desalination plant. A similar approach could be taken by Coliban Water and Central Highlands Water with regard to the Goldfields Superpipe.*

Discussion

Price paths and hardship policies

One of the most controversial issues in the current Water Price Review is the way large price rises are being implemented. Of those with significant price increases:

- The metropolitan water businesses have proposed to collect the additional revenue evenly over the period by a one-off price increase at the beginning of the period;
- Western Water has proposed to increase it incrementally over the five-year period;
- Coliban Water has proposed a middle path with an initial price jump and smaller subsequent ones.

When assessing the 'one-off' versus 'smoothed' approach to tariff increases, it must be recognised that each has its distinct benefits and disadvantages. The 'one-off' approach gives customers a price shock that may cause temporary hardship or exacerbate existing hardship; but once the household has adjusted to the new price there are no further price shocks for the remainder of the period. The 'smoothed' approach gives a much softer price jump that is difficult for fewer households; but this smaller group then has a similar price shock every year and by the end of the period all customers are paying considerably higher prices than they would be if the 'one-off' approach had been taken.

After much consideration and conferral with other consumer advocates, VCOSS supports the 'one-off' approach, *providing additional steps are taken to assist vulnerable customers avoid hardship and adapt to higher prices*. Our rationale is simply that for the average household, the price shock will be noticeable but not onerous – so vulnerable and disadvantaged households should not be exposed to higher prices caused by unnecessarily protecting middle and upper income households from a modest price shock. The additional cost water businesses would bear in implementing a smoothed price path for their entire customer base is better spent giving vulnerable customers additional assistance to cope with the increase.

With this in mind, the Commission should assess the degree to which those water businesses proposing significant 'one-off' price rises have identified the likelihood of increased hardship among a segment of their customer base and proposed additional steps to address it – and specifically, to give vulnerable customers considerable time and flexibility to adapt to higher prices over several billing periods. Research VCOSS undertook in 2006 (unpublished) with households in financial crisis and discussions with frontline agencies all indicates that payment flexibility is critical in proactively assisting vulnerable customers – in fact, it's often all that's needed to keep a vulnerable customer from falling into serious financial hardship.

VCOSS notes that Yarra Valley Water, South East Water and Coliban Water have all made an explicit connection between their proposed steep price rises and hardship and have consequently enhanced their hardship programs. In particular:

- Yarra Valley Water and South East Water propose enhanced hardship programs with increased payment flexibility. This is an appropriate corollary to the significant price rise proposed for 2013.
- Coliban Water proposes payment-matching in instalment plans and selective debt write-off for customers in hardship. This is an effective approach to customers whose payment difficulties have led to unaffordable debt (though matching every ninth payment seems overly optimistic – other successful payment-matching schemes we have seen matched the third, fourth, or fifth). However though they mention the importance of payment flexibility for avoiding hardship, Coliban Water has not specified any enhancement to payment flexibility – necessary to mediate the impact of their proposed 2013 price increase on vulnerable customers.

Conversely, City West Water (and Central Highlands Water, whose 8.5 per cent increase is not one of the highest but is delivered in full at the beginning of the period) has not made an explicit connection between price shock and increased hardship, and has not proposed any enhancements to their hardship program.

Water businesses proposing non-smoothed price increases should demonstrate their understanding of the impacts on vulnerable customers and their commitment to proactively helping customers in hardship by explaining how they will enhance their hardship programs and payment processes to mediate those impacts and help vulnerable customers adapt to higher prices.

Tariff structures

The continuing shift away from inclining block tariffs (IBTs) is evident in the 2013-18 water plans. Some water businesses have abandoned IBTs, others have reduced the number of blocks from three to two.

Much of the discussion about IBTs has focused on whether or not they give a price signal for conservation, and whether or not they increase or decrease equity. What is often overlooked is the potential for IBTs to offset the impact of a high fixed cost for low-volume households. VCOSS considers this a positive equity outcome, and maintains that so long as the block thresholds are carefully set, the higher blocks are not too expensive, and there is systemic or targeted assistance or offsets for large low-income households where necessary, IBTs need not deliver inequitable outcomes. They should be assessed on their merits.

The other tariff structure issue of interest in the current crop of water plans is the move by many businesses toward rebalancing the relationship of volumetric to fixed prices. Much of the customer consultation undertaken has found strong support for having the volumetric charge as a greater proportion of the bill in order to give a better reward for water conservation or simply to give households greater control over the size of the bill. Some of the tariff restructures to implement this, however, may have unintended consequences for some customers. For example, East Gippsland Water is adjusting its residential tariff so that for the average customer, 60 per cent of the bill will be variable while the total bill will remain essentially the same. However customers with above average consumption will be paying more in proportion to their additional consumption, and tenants will have an increase of around 50 per cent. Because tenants are much more likely to be low-income households (70 per cent of tenants are low-income or low-wealth households[1]), this is a considerable equity and affordability issue that needs to be addressed by any water business proposing to significantly shift the balance between fixed and volumetric charges.

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[1] ABS, 4102.0 - Australian Social Trends, March Quarter 2012, Canberra 2012.

Water businesses making significant changes to tariff structures should demonstrate their understanding of the impacts on different types of customers and their commitment to proactively helping vulnerable customers by explaining how they will mediate the impacts and, where necessary, help vulnerable customers adapt.

Service standards and Guaranteed Service Levels (GSLs)

There is considerable variance among the water businesses in the relationship between their proposed service standards and both the previous period and the five-year average. Without specific knowledge it is difficult to assess the appropriateness of service standards. However some businesses have made strong cases for not improving specific service standards (generally, assessments that marginal improvements would require significant additional costs), and some have provided evidence of customer consultation that guided the service standard – cost compromises. This is an appropriate approach.

Because water businesses generally would have stronger performance in some service areas than others, a typical business would be expected to have service standard targets similar to the previous period or the five-year average in some areas (for services that they are delivering well) and improved targets in others (for services they believe have room for improvement). Some businesses (for example Barwon Water, Central Highlands Water, Goulburn Valley Water, Western Water) have, however, set almost all their targets similar to the previous period, and in some cases appreciably below either (or both) the previous targets and/or the five-year average.

Water businesses with few materially improved targets, or with targets consistently less rigorous than the 5-year average, should clearly demonstrate the rationale for the level of their service standards or revise them.

Guaranteed Service Levels (GSLs) are an indication of a water business's commitment to meet critical baseline standards, and the non-prescriptive approach taken by the Commission is an opportunity for businesses to identify their service priorities and demonstrate their commitment to customer service. Businesses with few or no GSLs beyond the compulsory hardship GSL are failing to demonstrate this awareness and commitment.

Water businesses with few or no voluntary GSLs should provide a clear rationale and demonstrate an alternative approach to identify and honour baseline critical service standards.

The Commission should consider requiring a minimum number of self-defined GSLs.

Cost offsets from previous period

A number of water businesses are seeking to offset costs from under-recovery in the previous period. In one case (Central Highlands Water) this does not seem to have been indicated in the draft water plan. VCOSS understands that unforeseen circumstances (such as floods, bushfires, or the severity of a drought) can result in unanticipated expenditure; and that over-recovering for contingencies can foment social and political discontent (as demonstrated by media storm and impulsive policy-making over the Melbourne Water over-recovery in 2012). Nevertheless, the end result is a very poor outcome for customers, especially in situations where there is already upward pressure on prices. One of the roles of water businesses is to carry a degree of risk on behalf of their customers and absorb some revenue–expenditure variance in order to give customers predictable prices and moderate price paths.

The Commission should limit cost offsets from previous periods as much as possible, ensure water businesses make prudent contingencies, and promote a regulatory environment whereby appropriate levels of revenue–expenditure divergence to support such prudence are allowable.

D-factor

VCOSS supports the D-factor approach proposed by the metropolitan water businesses for possible use of water from the desalination plant. A similar approach could be taken by Coliban Water and Central Highlands Water with regard to the Goldfields Superpipe.

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If you have any questions about this submission or require more information on any of the matters raised, please contact Dean Lombard, Senior Policy Advisor, at Dean.Lombard@vcoss.org.au

Yours sincerely

Carolyn Atkins
Acting Chief Executive Officer