Economic Regulation of Three Water Services

Submission of Taituarā to the Commerce Commission

March 2025

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Taituarā-Local Government Professionals Aotearoa ('Taituarā') thanks the Commerce Commission ('the Commission') for the opportunity to submit in respect of the discussion document Economic Regulation of Water Services – Information Disclosure ('ERWS').

Taituarā is New Zealand's leading network for local government professionals.

A few words about us. Taituarā is Aotearoa New Zealand's leading membership network for professionals working in, and for, local government. We have a membership base of 1,019 members drawn from local authority Chief Executives, managers, and staff across all 78 local authorities.

What unites Taituarā members is our commintment to be our own professional best, supporting local government excellence through connection, collaboration and care for the wellbeing of our communities.

Taituarā strengthens the local government sector as a whole by using our members' insight and experience to influence the public policy debate. We submit on legislation and regulationsto provide perspectives on what works and how to make policy work.

We offer the perspectives of a critical adviser.

Taituarā is a managerial organisation as opposed to a political one. Our role therefore is to advise on consequences, and to assist policymakers to design a policy that can be implemented effectively. We participated (and continue to participate) in the reform process to provide these perspectives.

Our submission takes the perspective of a 'critical adviser' in the reform process – supportive of the need for affordable, sustainable three waters services, while aiming to ensure the legislative end result works.

Our 2024 'conversation starter' A Practical Approach to the Economic Regulation of Water Services provides more information on the approach regulators should take, and some first thoughts on the basket of measures that the regulators should employ.

The views expressed in this current submission represent refinement and an expansion of those in the conversation starter and therefore prevail over the conversation starter.

Economic regulation must reflect the unique design features of the Local Water Done Well.

Economic regulation will play an important role in securing overall consumer confidence in any proposals to reform water services. Local Water Done Well (LWDW) is likely to founder if there is any suggestion that water users are being 'overcharged' for this service, or that the funds raised are not being spent 'appropriately' (for example spending on 'gold-plated' water services).

We submit that the policy settings that underpin these reforms are quite different from telecommunications, energy and groceries. They point to a regime that is more light-handed and based on disclosure, at least initially.

There are particular features of LWDW that bear on the design of economic regulation. Specifically:

- each of the delivery models are based on public ownership (whether it be by local authorities, community trusts or some combination of the two)
- the ringfencing provisions (most notably clause 16) make it very clear that water revenues **must** be spent on water services[1]
- the activities of water services providers are limited by statute to the provision of water services (drinking water supply, wastewater treatment and disposal and stormwater treatment and disposal)
- water services providers will be subject to a quite detailed regime of public accountability including the production of a water services strategy (which the Commission can request be audited). The accountability model is loosely based on the long-term planning provisions of the Local Government Act 2002 and will apply equally to all providers regardless of the ownership model.

[1] Our submission to the present legislation has noted an apparent inconsistency in the legislation in that the legislation states clearly that water revenues must be spent on water service and a major provider (Watercare) is expressly prohibited from distributing any surplus. Yet cabinet papers appear to suggest that dividends not only could be paid but would be taxable. Also, the legislation allows the Commission to regulate rates of return, a power that would be redundant if water services providers were spending all water revenues on water services.

The purpose of economic regulation in the LWDW environment will therefore be concerned about providing assurance to users of water services that services are being delivered efficiently and in their long-term interests. Associated with that the Commission will also have to administer the ring-fencing requirements. In the LWDW environment the control of monopolistic excess profits will be less of a concern.

The benefits that economic regulation bring to the LWDW come from transparency that requiring disclosure of information brings. The associated 'benchmarking' is a commonly-used tool to introduce some degree of competitive tension into monopoly services. This enables consumers to detect differences in performance between providers and hold them accountable for these (for example, enabling customers to ask questions such as "why is the price I'm paying for this service different from that elsewhere?"). The other benefits of information disclosure are accurately reflected in ERWS (at paragraph 1.25).

ERWS could have more clearly set out the Commission's intended approach to the incorporation of stormwater.

Taituarā supports the economic regulation of stormwater. Stormwater services share many of the same natural monopoly characteristics as other water services, additionally stormwater services do not generally lend themselves well to user charging.

The size and scale of the likely future investment in stormwater services is less well quantified which may lend itself to a greater user demand for transparency, pointing to a preference for the economic regulation of stormwater services.

Stormwater networks tend to be more complex than other water systems. Most consist of a piped stormwater network as well as above-ground, watercourses, secondary, and overland flow paths. Currently there are significant gaps in stormwater flood risk information and how it is developed, variations between councils' levels of service, design standards and policies related to flooding and protection.

Stormwater disposal is often provided alongside other non-water services. For example, the curbing and channelling that runs alongside streets in many urban areas. The regulator must take care than any regulation of stormwater disposal does not impose reporting (or other) obligations in respect of non-water services.

Sensibly the present legislation will allow for stormwater to be brought under economic regulation at a later date. The legislation doesn't specify any kind of procedure or criteria for the Commission to apply in making the decision to extend the regulation to stormwater. We had looked to the Commission's early engagement with the sector to clarify this important aspect – ERWS has not done so.

Information disclosure, and economic regulation in general should be based on a rigorous set of principles.

Taituarā considers that the following principles are a useful basis for developing the information disclosure regime:

- *customer-focus* – the purpose of economic regulation is to promote the interests of the customer/user of water services
- *sustainability of service* - the economic regulator must achieve the above purpose in a way that encourages and supports providers to manage their assets sustainably over the long-term and in accordance with their other legal obligations (for example, compliance with the Water Services (Drinking Water Services for New Zealand) Regulations 2022)
- *support for the role of water services in promoting urban growth and strategic planning objectives* - water services are not provided for their own sake, but to support the development of our communities, especially of our urban areas
- *efficiency* – economic regulation of water services should encourage and support providers to seek efficiency gains, innovate and look for productivity improvements
- *simplicity* – a regulatory regime should require collection and disclosure of only that information necessary to fulfil the purpose of the regulations
- *transparency* – the regulator should provide evidence that the regulatory regime is achieving the intended purpose, water service providers should therefore expect that their data will be publicly available *at provider level* as well as any analysis or compilation undertaken by the provider.
- *Consistency and certainty* – the regulator must clearly set out definitions and methodologies to be followed by providers in supplying the information (the repealed legislation referred to these as input methodologies).

Taituarā welcomes the intent that the information disclosure regulations be cost-effective.

As we have seen, one of our design principles was that the Commission should be looking to re-use and re-purpose information from existing information sources including existing reporting to government agencies.

Paragraph 3.13 suggests that the Commission will 'build on information in the service delivery plans. While the service delivery plans may be a good source for foundational disclosures, the Commission should note that these plans are a one-off requirement and will date quickly. In our view the service delivery plans will become irrelevant within no more than 3-5 years.

We note that the Commission intends to gather information relating to levels of seinice, complaints, satisfaction and the like. We observe that the Commission will need to develop input methodologies for these items to ensure that any public reporting produces comparable information. This points to, for example, a common methodology for measuring and reporting customer satisfaction; common means for capturing and reporting customer complaints.[2] If customer satisfaction is deemed important then the Commission will need to develop a standard customer satisfaction survey and metric and so on. The Commission might need to develop a series of 'acceptable' solutions for generating some information sets, such as the customer complaint issue signalled in the footnote below.

In short, the cost to water providers is not only the levy that the regulators pay to finance the Commission's activity. It is also the time and resources necessary to produce that information which is not required by any other provider and investments in any systems or processes necessary to meet the Commission's requirements.

Table 2.1 is a generally sound description of stakeholder information needs.

We consider that the list of 'possible questions that stakeholders may be interested in asking' contains the items that rightfully fall within the scope of an economic regulator. We have specific comments about some of the needs listed on pp16-18.

Article te Toru (Article Two) guarantees Māori the right to make decisions over the resources and taonga they wish to retain. Water providers are public entities that will make decisions that impact on our waters and taonga such as the placement of infrastructure and levels of service. The present legislation requires providers to give effect to treaty settlements. It seems to us that expenditures and activities undertaken to support treaty settlements could be a key driver of overall spend in some area, and worth a separate collection.

We agree that customer complaints is an important piece of information. It is both a proxy for, and early warning of underinvestment, and the disposal of complaints is a key level of service in itself. Our question about this item is the focus on efficiency as the yardstick? Is it important that a complaint is responded to quickly and cheaply or

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[2] To take an example, one of the shortcomings of the present non-financial performance reporting is that that there are two distinct methodologies for collecting information regarding customers complaints. Some call centre packages treat multiple contacts about the same issue as a single complaint, in others each contact is regarded as a separate complaint.

that it is responded to 'right' i.e. in a way that provides a satisfactory outcome for both the provider and the complainant.

Our submission on the Local Government (Water Services) Bill has identified an inconsistency in the Bill and the headline policy that goes directly to the regulatory regime. The financial ringfencing provisions of the Bill provide that revenue received from water services can only be spent on water services. A plain text reading of that clause would therefore suggest that, among other things, a water service organisation cannot distribute a surplus or pay a dividend to its shareholding local authorities.

Yet we read in the Cabinet Paper Local Government (Water Services) Bill: Approval for Introduction that
"the prohibition on Watercare paying dividends or any surplus to Auckland Council should continue. The prohibition is a key feature of the financial separation of Watercare from the Council and is already provided for in legislation. This prohibition is unique to Watercare. Other water organisations will be able to make distributions if agreed by their shareholders and provided for in the organisation's constitution, or the equivalent document(s)"[3]

In short, pending clarification from Parliament, it seems likely that water providers will be unable to make a dividend payment, distribute a surplus etc.

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[3] Minister of Local Government (2024), *Local Government (Water Services) Bill: Approval for Introduction*, paper to the Cabinet Legislation Committee, page 5.

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