

# **Industry Panel**

*Application made by Icon Water Limited under section 24S of  
the Independent Competition and Regulatory Commission  
Act 1997 in relation to the first biennial recalibration*

## **Declaration and Report**

18 February 2015

The Industry Panel is established under the *Independent Competition and Regulatory Commission Act 1997*, following an application by ACTEW for the review of the Independent Competition and Regulatory Commission's Price Direction for Regulated Water and Sewerage Services, 1 July 2013 to 30 June 2019.

The Industry Panel is constituted under the ICRC Act by one President and two members.

The Panel Members are President Ms Mary Anne Hartley QC, and Members Ms Sally Farrier and Ms Claire Thomas PSM.

Correspondence or other inquiries may be directed to the Industry Panel at the addresses below:

Industry Panel  
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Canberra ACT 2601

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Further details of the Industry Panel process can be found at:  
<http://apps.treasury.act.gov.au/industrypanel>.

# Table of contents

1. Purpose of this report .....	1
2. Background .....	1
3. The Panel's Declaration .....	2
4. The Panel's process .....	3
5. The Panel's assessment .....	4
6. Summary of reasons.....	8
Appendix: Icon Water's section 24S application .....	11



## 1. Purpose of this report

Having received and assessed an application from Icon Water Limited ('Icon Water') under section 24S of the *Independent Competition and Regulatory Commission Act 1997* ('the Act'), the Industry Panel ('the Panel') has made a declaration. This declaration is contained in this report (see section 3). The report also describes the process and assessment undertaken by the Panel in reaching its declaration.

## 2. Background

In accordance with Part 4C of the Act, the Panel<sup>1</sup> is currently reviewing the price direction released by the Independent Competition and Regulatory Commission ('ICRC') on 26 June 2013 for prices applying to regulated water and sewerage services in the ACT for the period 1 July 2013 to 30 June 2019 ('the 2013 Price Direction'). The Panel released its draft decision in respect of its review of the 2013 Price Direction on 3 December 2014.<sup>2</sup>

Under the Act, the 2013 Price Direction continues to have effect until the conclusion of the Panel's review process and release of its final report, unless the Panel makes a declaration under section 24S. That section empowers the Panel to make a declaration to suspend or alter the implementation of the 2013 Price Direction following an application by a party to its review. Section 24S is reproduced below.

<b>24S</b>	<b>Implementation of price direction under review</b>
(1)	A price direction has effect despite any application for its review, unless the industry panel, on an application by a party, declares in writing that the implementation of the price direction is suspended or altered until— <ol style="list-style-type: none"><li>(a) if the panel confirms the price direction under review—the day the report of the review is presented to the Legislative Assembly (under section 24U (Functions of the commission)); or</li><li>(b) if the panel substitutes a new direction for the price direction under review—the day (or days) the substituted direction comes into effect.</li></ol>
(2)	The declaration of suspension or alteration is taken to be a variation of the price direction while the direction remains in force.
(3)	The following sections apply to the declaration of suspension or alteration as if it were the final report of a price regulation investigation: <ul style="list-style-type: none"><li>• section 21 (Final reports)</li><li>• section 23 (Confidential material in reports)</li><li>• section 24 (Presenting of reports to Legislative Assembly)</li><li>• section 24B (Correction of errors in reports).</li></ul>

<sup>1</sup> The Industry Panel was appointed in April 2014 by the ACT Treasurer in accordance with Part 4C and Schedule 3 of the Act, and comprises Mary Anne Hartley QC (presiding member), Sally Farrier and Claire Thomas PSM.

<sup>2</sup> Industry Panel, *Review of the Independent Competition and Regulatory Commission's 2013 Price Direction for Regulated Water and Sewerage Services in the ACT*, Draft Report, December 2014.

The 2013 Price Direction made provision for the ICRC to undertake two biennial recalibrations, due to occur in 2015 and 2017. The ICRC’s first recalibration process, which is designed to review the maximum prices that may be charged for regulated water and sewerage services from 1 July 2015, commenced on 29 October 2014. The tasks involved in the first biennial recalibration process, and the indicative timeline provided by the ICRC, are summarised in Table 1 below.

**Table 1: Indicative timeline for the ICRC’s 2015 biennial recalibration**

Task		Date
1	Information request provided to Icon Water	29 October 2014
2	Information return provided to the ICRC	1 December 2014
3	Information return published	8 December 2014
4	Demand modelling paper published	20 January 2015
5	Submissions on demand paper close	23 February 2015
6	Release of draft report	1 April 2015
7	Submissions on draft report close	5 May 2015
8	Release of final report and prices	11 June 2015

Source: Independent Competition and Regulatory Commission, *Technical paper: Water demand forecasting, Biennial Recalibration 2015*, Report 1 of 2015, January 2015.

## 2.1 The application

On 23 January 2015, the Panel received an application from Icon Water Limited ('Icon Water') under section 24S of the Act to alter the 2013 Price Direction to defer or remove the need for the first biennial recalibration, pending the release of the Panel’s final report. A copy of Icon Water’s letter of application is included as an Appendix to this report.

## 3. The Panel’s Declaration

In accordance with section 24S of the Act, the Industry Panel makes the following declaration with respect to the price direction released by the Independent Competition and Regulatory Commission ('ICRC') on 26 June 2013 for prices applying to regulated water and sewerage services in the ACT for the period 1 July 2013 to 30 June 2019 ('the 2013 Price Direction'):

- (a) with effect from the date of this declaration, the implementation of the provisions of clause 10 of the 2013 Price Direction in relation to the first biennial recalibration process will cease to apply, and neither the ICRC nor Icon Water Limited (ABN 86 069 381 960) will be required to carry out those processes; and
- (b) if a final decision has not been made by the Panel and become effective in accordance with the Act before Friday 5 June 2015, the maximum prices for water and sewerage services for 2015-16 will remain at the values applicable for 2014-15 until such prices are determined in accordance with the final decision of the Panel.

This declaration does not affect the implementation of the 2013 Price Direction with respect to the regulation of prices for miscellaneous services.

## **4. The Panel's process**

### **4.1 Decision-making framework**

There is no process outlined in the Act that requires the Panel to take particular steps in considering an application made under section 24S, nor is there any specified decision-making framework to be adopted by the Panel in assessing an application made pursuant to that section.

In the absence of any specific legislative directive concerning the Panel's consideration of Icon Water's application, the Panel has endeavoured to adhere to the general legislative purpose of the Act, and taken into account principles of general administrative law, best practice in administrative decision-making, and its own Charter.<sup>3</sup>

The Panel considered Icon Water's application expeditiously because:

- it was mindful that the costs associated with considering a section 24S application are recouped from Icon Water and ultimately borne by the ACT community; and
- in light of the advanced stage of the Panel's process in reviewing the 2013 Price Direction, it was appropriate to address the application expeditiously.

### **4.2 Consultation**

There is no formal consultation process required under the Act for deciding a section 24S application. However, in the interests of procedural fairness, the Panel ensured that persons whose interests may be affected by the Panel's decision were given a reasonable opportunity to comment on Icon Water's application.

The Panel provided Icon Water's application to the ACT Treasurer, and those persons who notified their interest in the Panel's ongoing review of the 2013 Price Direction.<sup>4</sup> The Panel indicated it would accept written submissions from these persons until 4 February 2015. A copy of Icon Water's application was also uploaded to the Panel's public website.

The Panel received one submission in response to Icon Water's application from Dr Terence Dwyer. Dr Dwyer called for the Panel to dismiss the application, claiming Icon Water was being "disingenuous" in seeking to avoid costs associated with the biennial recalibration process. The submission asked:

"why should we care about [Icon Water's] convenience? Or take any notice of any professed concerns about the costs it even now wants to ramp up in perpetuity[?]"<sup>5</sup>

<sup>3</sup> The Panel's Charter is available at the Panel's website (<http://apps.treasury.act.gov.au/industrypanel>).

<sup>4</sup> These persons are those who made a submission to the ICRC's original price investigation and who provided written notification, under section 24K(3)(a) of the Act, of their intention to appear as a party to the Panel's review.

<sup>5</sup> The submission is available on the Panel's website (<http://apps.treasury.act.gov.au/industrypanel>).

The Panel also requested and received the assistance of the ICRC in relation to identifying any issues associated with the implementation of its declaration.<sup>6</sup>

## **5. The Panel's assessment**

### **5.1 Analysis**

As the Act does not specify criteria under which a section 24S application should be assessed, the Panel established its own decision-making framework to consider Icon Water's request.

The Panel decided to assess the merits of the arguments presented by Icon Water in its application, having regard to the following overarching principles:

- the importance of maintaining the integrity of the regulatory system, particularly in relation to maintaining public confidence in regulatory processes and outcomes;
- minimising the burden of regulation, being mindful that the costs associated with the water and sewerage pricing framework (incurred by both Icon Water and the ICRC) are ultimately recouped from the ACT community; and
- best practice regulatory principles (discussed in further detail at Table 2).

In assessing the costs and benefits of Icon Water's application in the context of these principles, the Panel also had regard to the status of its review of the 2013 Price Direction. In particular, the Panel kept in mind the following considerations.

- The current timeline for the Panel's review of the 2013 Price Direction anticipates a final decision being made and becoming effective in time for implementation from 1 July 2015. Nevertheless, it is prudent for any declaration to provide for default prices to apply from 5 June 2015 in order to deal with the possibility of unforeseen circumstances resulting in a delay to the Panel's final decision becoming effective, and to allow sufficient time for processes necessary for adjustments to customer contracts.
- While it cannot be ruled out until the Panel's final decision is made, the likelihood of the final decision requiring the first biennial recalibration process to be completed for the purpose of setting 2015-16 prices is low, having regard to the Panel's preliminary findings in its draft decision and to submissions received in response to the draft decision. The draft decision currently substitutes a new price direction that fixes prices until 30 June 2018, without the need for any recalibration process. No submissions have been received by the Panel, nor new evidence presented, that contend against this proposed approach.

Table 2 below summarises the Panel's assessment of issues raised in Icon Water's section 24S application in support of its request for the Panel to defer or remove the need for the first recalibration process, and the issues raised in the submission of Dr Dwyer.

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<sup>6</sup> Section 24U(1) of the Act provides that the ICRC must give the Panel any assistance the Panel requires.

**Table 2: Detailed explanation of the Panel's assessment**

Issue raised by Icon Water's section 24S application	The Panel's assessment
<p><b>Confusion regarding multiple review processes</b></p> <p>Icon Water's application asserts that the continuation of dual price-setting processes over the next few months (ie, the finalisation of the Panel's review of the 2013 Price Direction, and the ICRC's first biennial recalibration) may "negatively impact on public confidence in the regulatory system".</p> <p>Icon Water notes "the large number of reviews and enquiries with respect to water and sewerage prices in recent years together with their associated public engagement". Given that the Panel's review of the 2013 Price Direction and the ICRC's first recalibration are now taking place concurrently, Icon Water's view is that "the continuation of two parallel processes at this time would cause unnecessary confusion and uncertainty." Icon Water contends that this confusion would be further exacerbated if different approaches are taken by each of the Panel and the ICRC or if different outcomes were to be reached.</p>	<p>The Panel recognises that the price regulation of water and sewerage services is a complex area. The continuation of two different price-setting processes in parallel runs the risk of reducing the clarity of price-setting arrangements, and increasing uncertainty among businesses and the public, particularly if the two processes yield inconsistent outcomes.</p> <p>The timeframes for the ICRC's biennial recalibration (as specified in Table 1 above), overlap with the Panel's ongoing review of the 2013 Price Direction. The Panel released its draft decision on 4 December 2014; invited written submissions on this draft decision by 23 January 2015; and held a public hearing on 6 February 2015. The Panel is now undertaking further analysis and consideration of public submissions with a view to reaching its final decision and releasing a final report.</p> <p>The Panel is aware that the ACT community has been asked to engage in multiple review processes about water and sewerage prices in recent times. In addition to the problem of consultation 'fatigue' (which may result in a lack of engagement in future processes), the Panel recognises the costs stakeholders incur by participating in such reviews (eg, the time taken to prepare submissions and/or attend public hearings).</p> <p>The Panel also considers that two separate price-setting processes being undertaken concurrently is not consistent with best practice regulatory principles. Generally speaking, these principles are that:</p> <ul style="list-style-type: none"> <li>• regulation should be cost-effective – the benefits to customers should exceed the costs</li> <li>• regulation should be proportionate – regulators should only intervene when necessary</li> <li>• regulation can adapt, but it should be predictable – while regulation should have the capacity to respond to changing circumstances, it should provide a stable and predictable environment and avoid adding undue uncertainty, and</li> <li>• regulation should be practical, pragmatic and feasible.<sup>7</sup></li> </ul> <p>Taking into account these principles, the Panel concludes there is a strong case to suspend the operation of the ICRC's first biennial recalibration process, on the basis that parallel price-setting processes undermine confidence in the regulatory system.</p>

<sup>7</sup> These best practice principles are discussed in more detail in the Panel's *Review of the Independent Competition and Regulatory Commission's 2013 Price Direction for Regulated Water and Sewerage Services in the ACT*, Draft Report, December 2014, Section 4.3.

**Cost of the biennial recalibration process**

Icon Water submits that “further costs to be incurred by Icon Water and the ICRC in relation to continuation of the biennial review process would be up to \$1 million”.

Icon Water suggests that, given the Panel’s draft decision, it is “most likely” that the Panel’s final decision will substitute a price direction that fixes prices for 2015-16 and 2016-17, without the need for a recalibration process. This would mean that “the current biennial review would not be required and the further time and resources spent on the process by both Icon Water and the ICRC would provide no real value to customers”.

The Panel is aware there is some uncertainty as to the costs payable by Icon Water for its continued participation in the first biennial recalibration process. In a media release dated 3 February 2015, the ICRC disputed Icon Water's estimate, stating that the estimate is "wildly at odds with the Commission's own estimates of the costs of completing the process." The ICRC estimated that Icon Water's costs in completing the first biennial recalibration process would be in the order of less than \$250,000.

While the Panel is not in a position to verify, in an expeditious way, the total amount of the regulatory costs likely to be incurred as a result of the continuation of the first biennial recalibration process, it accepts that they will be material. Irrespective of any conjecture as to the total amount that may be incurred, any funds directed towards the continued recalibration process may prove redundant, and therefore inexpedient for Icon Water and ultimately, its customers, to bear.

The Panel understands that if the current recalibration process continues, at least the following future costs will arise in undertaking the remaining steps to complete the process (as set out in Table 1 above):

- Icon Water will incur costs in responding to the ICRC’s technical paper on water demand forecasting<sup>8</sup>, and in making a submission to the ICRC's draft report, and
- the ICRC will incur costs in analysing submissions, and in preparing its draft and final reports.

Given the fact that regulatory costs associated with the regulation of water and sewerage services (ie, incurred by both the regulated water entity and the regulator) are ultimately recouped from the ACT community, the Panel considers it important that these costs be reasonable and necessary to the achievement of the regulatory objective.

The costs of the first biennial recalibration will be unnecessary if the Panel’s final decision resulting from its review of the 2013 Price Direction:

- becomes effective in time for implementation by the start of the 2015-16 regulatory year (ie, 1 July 2015), and
- substitutes a new price direction that does not include a recalibration process to set 2015-16 prices.

As per the Panel's draft report, the Panel anticipates both of these conditions will be met. This being the case, the Panel concludes there is a strong case to suspend the operation of the first biennial recalibration process on the basis that it will mitigate the burden of regulatory costs imposed on the ACT community. This will be the case irrespective of the accuracy of the estimate provided by Icon Water in its section 24S application.

<sup>8</sup> Independent Competition and Regulatory Commission, *Technical paper: Water demand forecasting, Biennial recalibration 2015*, Report 1 of 2015, January 2015.

<b>Issues raised in Dr Dwyer’s submission</b>	<b>The Panel’s assessment</b>
<p><b>Icon Water is not serious about saving regulatory expenses, and costs should not be passed on to consumers</b></p> <p>Dr Dwyer submits that Icon Water should “pay the costs and not be reimbursed at [customers’] expense”, and that the Panel should not be concerned about Icon Water's "convenience".</p>	<p>The Panel had difficulty in interpreting this submission, although its main point appears to be concern about costs being passed on to consumers. The Panel notes that it is inevitable that the costs of the biennial recalibration process will ultimately be borne by the ACT community, either by:</p> <ul style="list-style-type: none"> <li>• customers of water and sewerage services, since the costs of regulation represent a form of operating expenditure, which may be passed on through prices, or</li> <li>• ACT taxpayers, given that any regulatory costs not recouped through prices would be reflected in lower dividends and tax-equivalent payments being paid to the ACT government by Icon Water.</li> </ul> <p>The Panel’s view is that measures should be taken to minimise the burden of regulation on the ACT community. The suspension of the biennial recalibration process now, before further costs are incurred, will mitigate against unnecessary costs being incurred by the community.</p>

## **5.2 Interim measures**

The Panel has considered and recognises that there are theoretical benefits from allowing the first biennial recalibration to continue – specifically, it would facilitate a smooth pricing transition in the event that the Panel’s final decision in reviewing the 2013 Price Direction is to confirm the original price setting regime (including the recalibration process). However, the Panel does not consider it likely that this theoretical benefit will arise in practice. And, in any case, the Panel’s view is that the disadvantages of continuing with the recalibration (as summarised in Table 2) outweigh the benefits.

Despite the Panel’s expectation that it will complete its review of the 2013 Price Direction in time for its final decision to be implemented by the start of the 2015-16 regulatory year, the Panel nevertheless considers it prudent to provide for default prices to apply from 5 June 2015 to deal with the possibility of unforeseen circumstances resulting in a delay of its final decision being implemented, and to allow time for Icon Water to adjust its customer contracts.

The Panel has considered Icon Water’s proposal that current prices be changed in line with the consumer price index ('CPI'), but believes that this method could potentially result in price volatility and uncertainty if prices were to rise in line with the CPI, and then change again following the implementation of a substituted price direction to be made by the Panel. To avoid this situation, the Panel has decided that prices should remain unchanged at current levels, pending the release of the Panel’s final decision. While the Panel recognises that this could have adverse financial implications on Icon Water, it considers the risk of the default prices coming into effect as very low. Moreover, if there is a significant unforeseen delay to the completion of the Panel's final decision resulting in the unchanged default prices taking effect, the Panel could take into account the delay in revised prices coming into effect when making its final decision.

In the unlikely event that the Panel arrives at a final decision that requires the first biennial recalibration to be completed, the Panel's decision could specify revised timelines for the recalibration process and deal with the transition from the default prices set by this section 24S declaration to the new prices determined in accordance with the Panel's final decision.

## **6. Summary of reasons**

The primary reasons underpinning the Panel’s decision to suspend the first biennial recalibration process are summarised as follows:

- **Allowing two price-setting processes to continue to operate in parallel threatens to undermine confidence in the regulatory system for the pricing of water and sewerage services in the ACT.** The ICRC’s first biennial recalibration is currently proceeding concurrently with the finalisation of the Panel’s review of the 2013 Price Direction, potentially causing confusion and uncertainty about water and sewerage pricing among the ACT community. The Panel also recognises that consultation

‘fatigue’, and the costs incurred by participants in engaging in dual price-setting processes, could reduce future community engagement in such processes. In addition, the Panel’s view is that the current situation is inconsistent with best practice regulatory principles, such as cost-effectiveness, proportionality, predictability and pragmatism.

- **The first biennial recalibration is imposing unnecessary regulatory costs on the ACT community.** No submissions have been received, nor new evidence presented, that will likely cause the Panel to alter its draft decision to set water and sewerage prices until 30 June 2018 without the need for a biennial recalibration process. Given the Panel expects it will finalise its review of the 2013 Price Direction in time for it to be implemented by the start of the 2015-16 regulatory year, the regulatory costs associated with the first biennial recalibration appear unnecessary and, in the Panel’s view, represent an unreasonable burden on the ACT community since these regulatory costs are ultimately recouped from water customers or taxpayers.



## **Appendix: Icon Water's section 24S application**

23 January 2015

Ms Mary Anne Hartley Q.C.  
President, Industry Panel  
GPO Box 158  
CANBERRA ACT 2601

Dear Ms Hartley

### **Application to alter the current Price Direction for regulated water and sewerage services**

Icon Water Limited (Icon Water) is writing to apply for alteration of the Price Direction of 26 June 2013 for regulated water and sewerage services for the period from 1 July 2013 to 30 June 2019 (Price Direction) in accordance with section 24S of the Independent Competition and Regulatory Commission Act 1997. Icon Water requests the Industry Panel (Panel) to defer or remove the need for the first biennial recalibration under the Price Direction pending the issue of the final report by the Panel.

As you would be aware, the Independent Competition and Regulatory Commission (ICRC) has commenced its first biennial recalibration process in accordance with the timetable set out in the Price Direction. On Monday 1 December 2014, Icon Water lodged its information return with the ICRC. The next step in the process set out under the Price Direction is for the ICRC to prepare its draft report in readiness for release on 1 April 2015.

Based on recent experience and Icon Water's internal resourcing requirements, we anticipate that the further costs to be incurred by Icon Water and the ICRC in relation to continuation of the biennial review process would be up to \$1 million.

We have noted from the Panel's draft report released on 3 December 2014 that *"the Panel's draft decision is to substitute a new price direction that sets prices until 30 June 2018, without the need for a recalibration process."*<sup>1</sup> Icon Water notes that *"the Panel is now consulting with the ACT community about its draft price direction"*<sup>2</sup> and that details of the substitute Price Direction will depend on this consultation. However, it appears most likely that the Panel's substitute Price Direction will set prices for 2015-16 and 2016-17.

If this occurs, the current biennial review would not be required and the further time and resources spent on the process by both Icon Water and the ICRC would provide no real value to customers. Icon Water is conscious of the amount of money spent in recent years on price determinations for water and sewerage, which is ultimately borne by the community.

Icon Water is also acutely aware of the large number of reviews and enquiries with respect to water and sewerage prices in recent years together with their associated public engagement. We recognise the value for the Canberra community of clarity regarding the review process. In our opinion, the continuation of two parallel processes at this time would cause unnecessary confusion and uncertainty. This would be further exacerbated if different approaches are taken by each of the Panel and the ICRC or if different outcomes were to be reached. Icon Water is concerned that the continuation of dual

<sup>1</sup> Industry Panel 2014, Review of the ICRC's 2013 Price Direction - Draft Report, December, p1.

<sup>2</sup> Industry Panel 2014, Review of the ICRC's 2013 Price Direction - Draft Report, December, p13.

processes over the next few months may negatively impact on public confidence in the regulatory system.

For these reasons, we feel that it is incumbent on us to request that the Panel defer the current biennial recalibration process until after the Panel's final report has confirmed whether the process is needed or remove the need for the process.

If it is necessary to specify a placeholder price that would apply from 1 July 2015, Icon Water proposes that it be based on a change to the current price, in line with the change in the consumer price index. Our presumption though is that a final Panel decision will be effective for implementation on 1 July 2015.

Icon Water is making this application with a view to the best interests of customers through minimising unnecessary costs and further public confusion in the determination of water and sewerage prices.

Icon Water would be willing to discuss with the Panel the specific alterations to the Price Direction that could be made to give effect to the deferral requested in this letter, if that would be helpful. If you would like to take up this offer, please contact Dr Ben McNair, Principal Economist, on 02 6248 3386.

Yours sincerely



John Knox  
Managing Director

