15 November 2024

Mr Gerard Brody
Chairperson, Essential Services Commission
Level 8, 570 Bourke Street
MELBOURNE VIC 3000

via email: water@esc.vic.gov.au

Re: Essential Services Commission New Customer Contributions Review

Dear Commissioners,

The Urban Development Institute of Australia, Victoria (UDIA Victoria) welcomes the opportunity to respond to the Essential Services Commission's (ESC) Review of New Customer Contributions (NCCs).

About UDIA Victoria

UDIA Victoria is the peak body representing the urban development industry. UDIA Victoria is a not-for-profit advocacy, research and educational organisation supported by a membership of land use and property development organisations, across the private sector and Victoria's public service. Our committees are comprised of developers, consultants, and contractors who collaborate directly with several local governments and water authorities.

UDIA Victoria members are not just customers of water authorities but are partners in creating infrastructure to required standards while providing valuable assets for ongoing management. UDIA consults with water authorities throughout Victoria and seeks to be an active partner in pricing consideration and submissions. UDIA Victoria actively participated in several water authorities' 2023 Pricing Submission processes and noted several areas of concern with the NCC process.

New Customer Contributions (NCCs)

It is noted that the ESC has proposed a change in terminology from New Customer Contributions to Developer Contributions. This modification would reflect industry expectations that these contributions should be calculated on a similar basis to a Development or Infrastructure Contribution Plan. That is, they should be transparent and include appropriate consultation. Additionally, all projects within the estimated budget are listed, justified, estimated, and a percentage contribution weighted according to its demands resulting from the growth of the catchment. This cost is distributed across the catchment or developable area (like NCCs).

We also note the State Government has recently announced a review of the broad network of existing developer contribution regimes. UDIA Victoria is representing the urban development industry on a select Working Group that has been established to advise on prospective reforms. We consider it important that any changes to NCCs are considered in the context of these reforms and others.

Additionally, projects that form part of a negotiated contribution package should relate specifically to the impact that the development will have on the sewer and water supply systems.

UDIA's submission responds to the topics listed on page 5 of the ESC's Review Paper, including:

- Unjustified cost attribution
- Standard pricing preference
- Negotiating framework requirements inadequately met
- Industry and stakeholder engagement issues
- Application of an overage incremental cost approach
- Uncertainty around gifted or reticulated assets
- Timing of development and development servicing plans

Additionally, the following were suggestions raised in UDIA's previous submissions regarding NCC reviews, that we wish to bring to the Commission's attention:

- Inclusion of a statement on how the cost of assets are apportioned to growth when there are multiple drivers, and how costs allocated to growth are attributed to new customers (as opposed to climate change, for example).
- Inclusion of a statement on the treatment of sunk costs and any conditions precedent for their inclusion in any NCCs applied. This should include a statement on how water authorities will ensure fair treatment between developers and between pricing periods.
- Inclusion of a statement on the calculation of net revenues and net costs included in NCC calculations, and how any postage stamp pricing of service and usage charges is accommodated.
- Inclusion of a statement on the treatment and explicit exposure of any geographic cross-subsidies and who pays (new customers only or the whole customer base).
- Inclusion of a statement on the treatment of the uncertainty inherent in these inputs and calculations how the uncertainty will be accommodated.

Unjustified cost attribution

It is our experience that some water authorities identified projects in their respective catchments and attributed some of the cost to growth. In these instances, it was not necessarily clear how this growth allocation was calculated.

In the case of Coliban Water's 2023 NCC Review, an analysis by FTI Consulting found a *medium level of confidence* that $207.6 million of this capital expenditure should be included in the NCC's.

Standard pricing preference

Some water authorities have an approved standard NCC. These standard NCC's apply across whole catchments and includes projects that may not relate to specific subdivisions within the respective areas. This potentially leads to cross subsidisation by developments in certain areas and is a significant concern in smaller townships.

Negotiating framework requirements inadequately met

Some water authorities have NCC Negotiating Frameworks. The authority considers that any negotiated NCC is in addition to the Standard NCC is as follows:

“Should the particular Application require a Non-standard/Negotiated NCC Charge, in addition to the Standardised NCC Charge, this will arise from the relevant negotiation, subject to the Regulatory Instruments in place at the time.” (Paragraph 12 p6 refers).

The ESC principles establish that the use of negotiated NCC’s should be undertaken where the standard charges would not be fair or reasonable and do not have a clear connection to the development being assessed.

We also note that some water authorities have equated negotiated NCCs to nonstandard uses and developments such as caravan parks, commercial developments or nursing homes rather than to residential subdivisions.

For example, the Coliban Water Negotiated NCC Framework restates the ESC pricing principles in Section 9 of the Framework. It is also publicly available. However, the Framework is not adopted by the authority as it focuses on applying standard NCC’s.

Industry and stakeholder engagement issues

UDIA Victoria acknowledges that various water authorities conducted extensive community consultations in preparation for their Pricing Submission, 2023. Many authorities, including South East Water, Greater Western Water and Yarra Valley Water conducted strong industry engagement. However, in some circumstances engagement with industry was, by contrast, limited and late.

In the case of Coliban Water, information provided at a public forum and in subsequent presentations was also largely focused on their intentions without clarifying the detail of their underlying assumptions, plans or calculations behind the proposed pricing strategy. Our members remained uncertain about how the authority had arrived at the more than 100 per cent increase in NCCs, compared to a 7 per cent increase for existing customers.

Application of an average incremental cost approach

The UDIA notes the use of an average incremental cost model adopted by some water authorities against the net incremental costs supported by the ESC. The issue is not so much the model chosen, but if the costs are fair and reasonable, and whether it is transparent as to which costs are attributable to growth and can be tied to a specific project. As the submission outlines above, UDIA is concerned that there is not sufficient clarity as to how costs are attributed.

Timing of development and development servicing plans

In relation to the timing of servicing plans, it is submitted that the detailed approach undertaken by Barwon Water is preferred to the ad hoc approach take by some other water authorities. For instance, Coliban Water published information for Greater Bendigo sewer and water supply plans with no timeframes other than delivery in the current pricing period.

Barwon Water’s approach to NCCs provide extensive documentation including sequencing plans. These identify the delivery sequence for water and sewer between 2023 and 2034. The plans also identify developer funded works and clearly outlines growth assumptions. Additionally, it clearly outlines the process for gifting assets.

Recommendations

1. A statement that Negotiated NCCs are the default basis of calculating NCCs, and Standard NCCs will apply for administrative ease in some cases. For example, water authorities may decide that any subdivision of less than "X" lots will be required to pay a Standard NCC.
2. A statement that it is a landowner or developer's right to seek a Negotiated NCC, not for it to be at the sole discretion of the water authority.
3. Removal of an error – the current framework states Negotiated NCCs apply in addition to Standard NCCs, whereas our understanding of the Commission's material is that it is one or the other.
4. Dispute resolution - better practice might be to offer a disaffected landowner or developer an escalation process before referral to VCAT. This might be:
    a. referral to more senior officers within the organisations of both parties; and/or
    b. referral to a mutually agreed independent arbiter. A choice of one or both or neither of these processes could save both parties time and money.
5. A statement on guiding pricing principles that are to be used, those being soundly based on Water Law, Planning Law, VCAT precedents and the Water Industry Regulatory Order. This should include any principles for the consideration of infrastructure other than pipes, such as pumping stations, re-treatment facilities, rising mains, pressure reduction, network monitoring equipment etc. In particular:
6. Clarification as to "reticulation" assets for which a developer is responsible? Pipe size alone should not be the sole criterion as there are pipe depth and onsite versus offsite issues to consider as well as non-pipe infrastructure.
7. Clarification as to "headworks/tail works" assets and how costs are apportioned to existing customers and future customers. Together with treatment plants, consideration needs to be given to back-bone infrastructure such as balancing tanks, transfer water mains, main and trunk sewers, and rising mains.
8. Clarification regarding "shared" assets and how costs are apportioned to existing customers and future customers.
9. Inclusion of a statement on how reimbursements will be administered.
10. Inclusion of a statement on how the cost of assets are apportioned to growth when there are multiple drivers, and how costs allocated to growth are further apportioned to new customers (as opposed to climate change, for example).
11. Inclusion of a statement on the treatment of sunk costs and any conditions precedent for their inclusion in NCCs applied. This should include a statement on how water authorities will ensure fair treatment between developers and between pricing periods.
12. Inclusion of a statement on the calculation of net revenues and net costs included in NCC calculations, and how any postage stamp pricing of service and usage charges is accommodated.
13. Inclusion of a statement on the treatment and explicit exposure of any geographic cross-subsidies and who pays (new customers only or the whole customer base).
14. Inclusion of a statement on the treatment of the uncertainty inherent in these inputs and calculations how the uncertainty will be accommodated.

Permanent Infrastructure Solutions

Whilst this review primarily addresses pricing, UDIA Victoria reiterates its position that water authorities should play a more proactive role in facilitating development. Specifically, we encourage water authorities to engage in forward planning in alignment with the Precinct Structure Plan (PSP) process. By actively participating in the timely provision of assets, either through collaboration with private landowners or using Land Entry Notices when applicable, authorities can help achieve more efficient and cost-effective infrastructure delivery. Currently, the 'hands-off' approach from water authorities has led to increased costs within the development sector, as reliance on developers for temporary infrastructure solutions is both costly and unsustainable.

Temporary assets add to the industry's cost base, ultimately stalling housing supply and impacting the affordability of new housing. Additionally, the continued construction of these temporary assets creates 'sunk' costs that do not contribute to the enduring infrastructure necessary for Victoria's long-term growth. To address this, we advocate for water authorities to prioritise permanent infrastructure solutions within reasonable timeframes, ideally matching the gazetting of PSPs. Reducing the dependency on temporary assets would not only support affordability but also ensure a more predictable and resilient infrastructure foundation for communities.

Conclusion

We thank you for your consideration of this submission and would value the opportunity to continue our engagement on these important matters as they progress.

The UDIA values it the close working relationship it has with many of the state's water authorities and with the ESC. We look forward to continuing to work with the ESC to meet our shared objectives.

If you wish to discuss any of these matters further, please do not hesitate to contact UDIA's Director of Policy, Jack Vaughan at [redacted].

Yours sincerely,

Linda Allison
CEO, UDIA Victoria