



Regulatory roles in consumer protection and reliability of supply

Presentation to the Water Pricing
Summit, *Moderating price rises in the
urban and rural water sectors*

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I am very pleased today to have the opportunity to address this summit today. In my presentation I am going to examine how consumer values, preferences and views are conceptualised in urban water pricing and policy debates. I'm going to argue that while these common concepts are useful, they are not comprehensive, and that their limitations are particularly obvious when it comes to the interests and needs of low-income and disadvantaged consumers. If utilities, regulators and policymakers want to understand and meet needs of this group of consumers, they will need to use complementary concepts and consultation mechanisms.

About CUAC

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Before I go on, a brief overview of my organisation, the Consumer Utilities Advocacy Centre. CUAC was established in 2002 to provide an independent, proactive, informed advocacy voice for all Victorian energy and water consumers:

- to effectively represent their interests in regulatory and policy consultation processes
- to facilitate and undertake independent research and thereby enable consumers to take full advantage of utility markets; and
- to monitor grassroots consumer utility issues with regard to low income, disadvantaged and rural consumers.

Our mandate is Victorian, however we find ourselves increasingly called upon to have input into national processes - in which we are often the only voice representing consumers. We are, for example, the sole consumer representative on the Department of Sustainability, Environment, Water, Population and Communities' Urban Water Stakeholder Reference Panel, on the Water Efficiency Labelling Scheme Advisory Group, and on the NHMRC's Water Quality Advisory Committee.

Pricing and consumer values and preferences: the traditional view

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Now that strikes me as quite interesting, because these days in the water sector we're seeing a lot of talk about the consumer voice, about empowering consumers, and about allowing them to express their values and preferences. Of course, these references to empowerment and expression are not made in the context of policy and advocacy, but in the context of pricing and individuals' participation in a market. I would like to talk a bit about these ideas about consumer values and preferences in relation to the water sector and to pricing in particular.

The current paradigm

Increasingly in the sector, we are seeing talk about customers expressing how they value water – and what characteristics of water services they value – through their purchasing decisions. The underlying idea here is that different consumers value water, and particular uses of water, differently. So, for example, an avid gardener may value water – and their unrestricted use thereof – more highly than an apartment-dweller who reads for leisure. This is, in itself, an uncontroversial notion.

In most urban water policy discussions, the analysis goes one step further by positing that consumers do (and should be freely able to) express these different values and preferences through their purchasing decisions and their willingness to pay for water. I think this position is often presented with shades of a moral – as well as an economic – argument. But the key economic rationale is that water pricing that facilitates expression of preferences will lead to an optimal – that is, most efficient – distribution of water and the other inputs used in the delivery of water.

These ideas about consumer values and preferences are linked to the general principles of user or beneficiary pays and cost-reflective pricing. Again, the ‘user pays’ principle suggests that allocation will be most efficient when consumers pay the full cost of a good or service, and when those who don’t use the service are not required to pay for it.

Policies and reforms linked to this paradigm

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These concepts about value and preferences underlie current policy approaches and proposed reforms in urban water pricing.

Customer choice

For instance, it’s the logic that underpins the present push for increased consumer choice, including the introduction of different tariff options for consumers to select from.

The economic rationale for customer choice is that it is a mechanism for more efficient allocation. Proponents – of which there are many – argue that choice will allow consumers to express their preferences on matters such as supply security and price volatility. The outcome of this is expected by proponents to be better demand management, more efficient allocation of risk, innovation and consumer benefit.

Scarcity/ flexible/ dynamically efficient pricing

In its discussion of tariff options in its recently released final report, the Productivity Commission linked the issue of customer choice to another reform being debated in the sector and variously known as scarcity, dynamically efficient or flexible pricing. The PC conceptualised tariff choice as a practical mechanism for implementing a type of flexible pricing by allowing customers to choose between a lower cost tariff with interruptible supply and a higher cost uninterrupted supply.

De-couple pricing and affordability

These ideas about preferences, price and efficiency also inform our current understandings of the appropriate relationship – or should I say lack of relationship - between pricing and affordability issues. The most common view in the water sector is that while universal access to water is important, water pricing is not the correct tool to achieve this objective. Instead, water should be priced with exclusive regard for economic efficiency. According to this argument, access and affordability should be dealt with elsewhere, variously through income support and other elements of the tax and transfer system, or through customer protection frameworks, businesses' hardship policies and so on.

A crack in the logic: social equity issues

I think that the ideas I outlined above about value, preferences and willingness to pay are useful concepts and that they have an important play in informing urban water policy.

But while all of these are useful ways of thinking about water pricing and water policy, I think it is important to remember that they are also limited. They don't encompass everything that policymakers, regulators and utilities need to consider. For instance, it's worth remembering that this paradigm doesn't provide much in the way of insight, let alone solutions, on social equity issues and the interests and preferences of low-income consumers.

Defining equity

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I would like to pause here for a moment to clarify what I mean when I refer to equity, because it's another term that is used by different people to mean different things. At the most basic level, equity has to do with fair distribution – both of resources (in this case water) and of burdens and responsibilities.

Debate about what constitutes a 'fair' distribution has been going on for centuries and will no doubt continue. There are a number of different and conflicting principles as to what is a fair distribution. Four of the most common are outlined on this slide. The first principle, proportionality, is really about applying the same rules to everyone, which aligns very well with an economic efficiency focus and with the user pays principle.

The latter three (equality, need and social utility) relate more to outcomes. Their application to water today could be fairly controversial, implying, for example, pricing on the basis of capacity to pay, or geographical equalisation of charges. At the most basic and uncontroversial level, however, they provide philosophical justification for the objective of maintaining universal access to the water needed for an adequate standard of living.

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In practical terms, when we talk about equity we are talking about vulnerable and low-income consumers: consumers who are more likely to struggle to afford to pay for and maintain access to water, and who are less likely to have the knowledge, confidence and resources to ensure their interests and rights are protected.

I've got some quotes up on the slide here that put this in human terms. One is a direct quote from an Aboriginal consumer who we heard from recently in our Aboriginal Energy and Water Project, which looked at the experiences of Aboriginal consumers in Victoria. This is one person's account of the impact that restriction has had on him, and as you can see, it's quite heartbreaking. The second is from hardship research recently commissioned by the Essential Services Commission. The researchers found that the consumers they spoke with were fearful about the future, their capacity to pay for utilities and to maintain a level of usage needed for an adequate standard of living.

Equity and efficiency: aligned or opposed?

For some consumers who are on a low income, cost-reflective and more efficient pricing will be of benefit. For example, many critics of Inclining Block Tariffs argue that they are not only inefficient but that they actually disadvantage many low-income consumers. Low-income consumers with high essential water needs – large households, for example – are disadvantaged by the higher marginal rate they pay for water. At the same time, low-income consumers who consume well below the first threshold benefit only minimally from a discounted volumetric rate, and this is offset by high fixed charges, meaning that, counter-intuitively, smaller users can be made worse off comparative to a two-part tariff.

But while efficiency-focused pricing and the interests of some low-income and disadvantaged consumers can align, they will not always do so. The goal of efficiency is net benefit, and ensuring any particular distribution to disadvantaged consumers is not its concern. Often, social equity and efficiency are actually opposing goals, and where equity is discussed in the literature on water pricing, this tension is often recognised.

The Productivity Commission acknowledges this in its final report on Australia's urban water sector, released a couple of weeks ago. The PC argued that "all of the valid objectives for the urban water" sector could be "encapsulated but the concept of economic efficiency," but with "universal and affordable access" a "possible" exception.

Undervaluing the preferences of low-income consumers

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In fact, one of the implications of the dominant way of thinking about value in relation to price and preferences, as presented earlier, is it has the effect of systematically giving less weight to the experiences and preferences of low-income consumers. For example, when we see customers as expressing the value they place on something through consumption decisions, when a low income consumer chooses to forego gardening because of concern about the cost of water, this is not viewed as a cost, but as an expression of that consumer's preference for another product or service

over water. This positive interpretation holds regardless of any distress the individual feels at foregoing gardening.

Essentially, a person with less money has fewer preferences to 'spend' on the goods and services that they desire. The preferences that a low-income person can afford to express through consumption choices are only a sub-set of their actual preferences, which may be strongly felt. Moreover, the inability to realise these preferences due to lack of money may have negative consequences for health and wellbeing. In fact, a wealth of research on poverty and financial disadvantage suggests that this is indeed the case.

Because it undervalues the preferences of low-income consumers, a classical economic paradigm is not, on its own, sufficient for a full analysis of urban water policy issues, particularly when it comes to considering the needs of disadvantaged groups.

Theoretical assumptions vs. consumer experiences

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Another shortcoming of the conventional way of thinking about consumer values and preferences in relation to pricing is that many of the assumptions don't fit with the actual experiences of individuals. This has been highlighted to us by some recent research in Victoria.

Next month CUAC will be launching our report on a research and action project which examined the experiences of Victorian Aboriginal consumers. The project looked at the issues and challenges facing Aboriginal consumers of both energy and water and considered the most effective means to address them. We gathered information from Aboriginal consumers at ten community discussion groups held in Melbourne and in regional Victoria. Data was also collected from service providers and advocates, energy and water businesses and regulators through semi-structured interviews and a questionnaire.

The research findings show that the actual experiences of this group of consumers often don't fit with the assumptions about consumer behaviour that underpin water pricing and policy thinking. For instance, two issues that came up repeatedly in our research were:

- that the housing available to the Victorian Aboriginal community – in the public and private market – is often inefficient or in need of repair. The Office of Housing has a long back-log of necessary repairs, some of which directly impact on the capacity of householders to control their water consumption.
- Aboriginal households have a higher number of occupants on average than non-Aboriginal households.

To take a simple example, then, a large Aboriginal family that consumes more water because of a leaking pipe which the housing authority has not repaired, cannot be assumed to have placed a higher value on the water used, or be willing – or able - to pay more for it.

Similarly, the consumers in the above example cannot be assumed to have received, understood, and acted rationally upon a price signal about the cost of providing water services. In theory, water prices give information to consumers about the implications of their consumption decisions. Consumers are then able to act on this information in their future consumption decisions. In practice, however, the relationships are less straightforward, and policymakers must consider consumers' capacity and inclination to interpret price signals and respond to them with appropriate behaviour change.

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When we think about this in relation to low income and disadvantaged consumers, a whole range of issues and complications come into view. For example, poor literacy and numeracy skills will limit some consumers' ability to interpret price signals. Even if such signals are received and correctly interpreted, the capacity to respond may be limited. For example, tenants have no legal right to change fixtures such as toilet cisterns and flow-control valves. Low-income consumers are also likely to be unable to afford water-efficient appliances or, for homeowners, improvements to the water efficiency of fixtures. Because of cash-flow difficulties, these consumers are unlikely to be able to act on any long-run incentives to purchase more efficient – but more expensive – appliances and fixtures.

Our research with Aboriginal consumers brought into focus some further issues, such as the larger household sizes I mentioned earlier, and the cultural practice of hosting extended relatives for long periods of time. Bill-payers in such circumstances have little capacity to reduce consumption in response to price signals.

The assumptions that I outlined at the beginning of my presentation do not hold for many consumers, and we should not infer the exercise of consumer choice or that consumers are empowered by choice where their options, practically speaking, are limited or non-existent.

Other ways to 'empower' consumers

Given that the dominant paradigm in water policy isn't quite adequate for the task, how do we ensure that the preferences of low-income and disadvantaged consumers are taken into consideration? I won't pretend to have all the answers here, but I do think have some suggestions, and it's something that the sector needs to be thinking about more than it does at present.

Businesses' planning

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Firstly, businesses need to make understanding the diversity of the consumer base a fundamental consideration in planning.

On that topic, one of the points I was asked to address in my presentation today was "promoting representation in stakeholder committees overseeing decision making". These committees are – or

can be, when they are done well – a good thing, but engagement with customers needs to go a lot further than this.

There is clearly a difference between the engagement businesses are able to have with those consumers who are actively interested in or are able to articulate their priorities and values, as opposed to those who may not be in a position to represent their views for a range of reasons, such as a lack of time, resources, knowledge or confidence to participate.

CUAC believes that water businesses should be able to differentiate between these consumer groups in the planning process, and ensure that both the broad interests and needs and the specific interests and needs of different consumer groups are included in planning processes. This will mean businesses need to employ a range of engagement methodologies, for example, in considering the impacts of capital infrastructure works on the diverse consumer base and the equity issues associated with the various cost/benefit impacts. Engaging with consumers directly (for example, through market research focus groups or through Consultative Committees) is to be encouraged, but it will also be helpful to engage with representative groups such as non-government agencies and consumer advocates representing vulnerable and disadvantaged people. Businesses also need to think creatively about other means of ascertaining the needs and preferences of low income and vulnerable consumers.

Research

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Secondly, because engaging low-income and disadvantaged consumers in traditional consultation processes is likely to be particularly difficult, there is an important place for focused research projects investigating the experiences and requirements of particular consumer groups.

Aboriginal Energy and Water Project

I have already spoken today about CUAC's research into the experiences of Victorian Aboriginal consumers of energy and water. This work identified a range of practical measures which, if implemented, will make a difference for Victorian Aboriginal consumers of energy and water and have benefits for marginalised consumers beyond the Aboriginal community.

Hall & Partners | Open Mind study

Another important piece of recent Victorian research was the Hall & Partners | Open Mind study of energy and water consumers receiving financial hardship assistance, commissioned by the Essential Services Commission. For this project, the researchers interviewed 53 consumers across the state, including 18 Melbourne residents who were receiving hardship assistance from their water business. The people in the study said they were 'overwhelmed' by rising utility prices and 'bills piling up on top of each other,' and expressed a 'sense of helplessness at being unable to cope.'

Thinking about the future, these consumers were fearful about their ongoing capacity to pay and to maintain a level of usage needed for an adequate standard of living. This was compounded by confusion about why their utility bills continue to rise. Many described how hard they are trying to conserve water, however they feel frustrated when they put significant effort into keeping their costs down yet their bills don't reflect this downward trend.

The findings of this project give us a deeper understanding of the relationships between consumption, consumer preferences, pricing and affordability.

CUAC & La Trobe rural seniors project

This year, CUAC will also be supporting La Trobe University researchers in a project investigating the perceptions, attitudes and preferences of rural seniors. This research will explore how water impacts on the lives of these consumers, how they perceive its importance to their personal health and wellbeing. It will also seek their responses, attitudes and perceptions in relation to urban water policy and pricing issues including tariff options and water product design. While the findings of this project might be used to develop a larger willingness-to-pay type study, this first project will be broader than a willingness-to-pay study. Firstly, the study will give a deeper insight into the preferences and values of these consumers because it won't be limited to considering only those that they are willing and *able* to pay for. Secondly, we will be hearing this groups' response to tariff options and other water policy and pricing issues in their capacity as both consumers *and* citizens. In other words, we won't simply be asking "Which tariff option would you choose?" but also "How do you feel about choosing?" and "Do you think that individual customer choice is a good way for society to manage water supply and demand challenges?"

We are excited about commencing this project because it will allow us to bring some much-needed empirical data on consumer preferences to a policy discussion that has to date mostly relied upon theoretical assumptions.

Consumer advocacy

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Related to research, consumer advocacy groups such as my organisation can also, I believe, fulfil important functions representing consumers generally and low income and disadvantaged consumers specifically. There is an immediate need for a stronger consumer voice in national water reform processes. Effective professional consumer advocacy is an important means through which this can be achieved, but professional advocates require detailed and specific knowledge to contribute effectively, and this is currently impeded by lack of resources.

CUAC has been pleased with the Productivity Commission's acknowledgement the important role of consumer advocacy in its urban water sector report findings and recommendations. The PC's report recognised that individuals often do not have the time, resources and expertise to represent their views in policy and regulatory decision-making processes. The PC noted that in their early

consultations, they had received substantially less input from individuals and consumer groups than from government and industry representatives, in part due to lack of resources. They suggested that the government should consider models for supporting consumer advocacy in the water sector.

While highlighting the importance of consumer policy advocacy, however, the Commission adopted a fairly narrow view of its role and argued that consumer advocacy presently focuses too heavily on vulnerable and low-income consumers. Related to this, the PC suggested that any consumer advocacy arrangements funded by government 'should include governance arrangements that ensure that the interests of all consumers are represented in a balanced way.'

While CUAC believes that generalist consumer advocacy is important, there is also a need for advocacy that focuses on disadvantaged consumers – who are not, in fact, an insubstantial group. Such consumers are more likely to have difficulty maintaining their access to essential services. They are also less likely to have the knowledge, confidence and resources to ensure that their interests and rights are protected, both in interactions with service providers and through input into policy and regulatory processes. For these reasons, it is critical that consumer policy advocacy pays specific attention to the interests of disadvantaged consumers.

Deliberative processes

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Finally, I would like to suggest that the governments consider greater use of deliberative processes that have the potential to illuminate the preferences, values and choices of consumers and community members as part of the urban water policy process.

Deliberative processes give lay citizens the opportunity to consider facts and perspectives, talk with each other, and evaluate opinions and options. For example, a typical "citizens' panel" process engages a randomly selected group of citizens in a structured, facilitated discussion. Experts such as academics and representatives of interest organisations present their perspectives to the group and answer questions. The citizens' panel considers and discusses the issues and develops written recommendations, which are then fed into the policy process. Other examples of deliberative processes include televotes and deliberative surveys (in which respondents are given the opportunity and time to take in and digest information as part of the questionnaire process).

Deliberative processes have been used to gain community input on a number of policy issues such as urban planning in a rapidly growing Perth; the Australian Capital Territory response to climate change and container deposit legislation in New South Wales.

As a complement to professional advocacy, CUAC believes that the careful and appropriate use of deliberative processes may be an effective way of incorporating consumer views into the urban water policy process, in turn improving policy outcomes.

Conclusion

In my presentation today I have tried to counter the view that cost reflective pricing, customer choice and so on, on their own, sufficient as a means of empowering consumers and allowing them to express their values and preferences. In particular, I have argued that the dominant ways of thinking about pricing and consumer preferences is not up to the task of understanding and addressing the interests of low income and disadvantaged consumers. Mechanisms such as improved consumer engagement and consultation processes, focused research, professional consumer advocacy and deliberative processes can and should be used to enhance our understanding of the needs and preferences of this group of consumers. In turn this will contribute to development of urban water policy that better meets the needs of the community.



Regulatory roles in consumer protection and reliability of supply

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About CUAC

- Established in 2002 to:

Represent all Victorian energy and water consumers in policy and regulatory processes

Facilitate and undertake research on consumer utilities issues

Monitor grassroots consumer utilities issues with particular regard for low-income, disadvantaged and rural consumers

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Expression of consumer preferences and values

... the allocation of water to users is optimal when the value of the water to a customer is reflected in the prices they pay... Prices more closely aligned with value would result in prices changing for various segments of customers based upon the choices they make.

- Living Victoria Ministerial Advisory Council, *Living Melbourne, Living Victoria Roadmap* (2011)

The Commission's objectives require an urban water sector in which ...

- *Customers are provided with value-for-money services and have the opportunity to express their values and preferences*

- National Water Commission, *Urban Water in Australia: Future Directions* (2011)

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Related reforms: Customer choice and flexible pricing

Customer choice

Outcomes sought or predicted:

- better demand management
- more efficient allocation of risk
- driving water sector innovation and productivity
- material benefit to consumers
- increased customer satisfaction



Flexible pricing

Although, in the strictest sense, 'flexible' retail pricing refers to the one-for-one pass through of the marginal opportunity cost of water to consumers, there are many ways in which flexible pricing can be implemented — it does not need to be introduced in a prescribed way [...]

The Commission favours an approach where utilities have the flexibility to offer a range of tariffs to consumers.

- Productivity Commission (2011) *Australia's Urban Water Sector*

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Equity: different meanings

Principle	Meaning	Applications to urban water & pricing
Proportionality	Each receives in proportion to their contribution	<ul style="list-style-type: none"> • Each consumer pays the costs they individually impose on the system • No cross-subsidisation
Equality	All receive (or contribute) the same amount	<ul style="list-style-type: none"> • Each consumer able to access the same amount of water • Postage-stamp pricing – geographical equalisation of charges?
Need	Each receives the amount they need	<ul style="list-style-type: none"> • Universal access • Each consumer to be charged according to ability to pay • Those with greater needs receive more water to meet those needs
Social utility	Distribution in the best interest of society as a whole	<ul style="list-style-type: none"> • Universal access • Consideration of liveability and social cohesion

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Equity: in human terms

You can't wash so you've got a that shame factor of, I'm living my past, I'm living my childhood again. Back when you're younger you can't wash and all that as much as you'd like to. I'm a grown-arse adult, I should be able to wash, I should be able to... but if I can't do that what does that mean for me as a person, as a human being let alone an indigenous person? Pride. Your pride takes a beating.

- Aboriginal consumer, Melbourne

... When asked to think about what the future might hold, for many there is little optimism. Those who have the least flexibility in relation to income and outgoings tend to express a sense of desperation. They imagine, not only difficulty in relation to keeping up with utility payments, but potentially a future situation where they may have to reduce their usage to an extent that their standard of living will be severely affected.

- Hall & Partners Open Mind, *Customers of water and energy providers in financial hardship: a consumer perspective*

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Low-income consumer preferences

Essentially, a person with less money has fewer preferences to 'spend' on the goods and services that they desire. The preferences that a low-income person can afford to express through consumption choices are only a sub-set of their actual preferences, which may be strongly felt.

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Victorian Aboriginal consumers

Aboriginal consumer, Melbourne

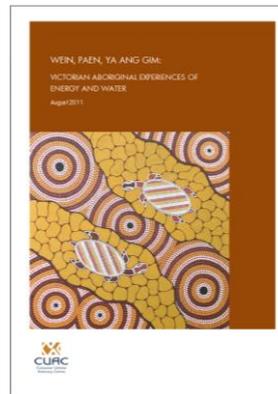
'My toilet was broken for about a month. It was running constantly. I knew it was going to put up my bill because it was using so much water. I didn't call the water company for a while though because I was scared that if I did, the water would be cut off.'

Aboriginal Consumer, the Mallee region

'There are always loads of people staying in Aboriginal houses. No one turns anyone away. Only one person ever pays the bill though.'

Aboriginal Consumer, Melbourne

'The biggest problem is the quality of housing. The older ones [public housing properties] are really bad, and even some of the newer ones are a bit dodgy, and this impacts on the bills for our mob.'



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Low income and vulnerable consumers – who are they?

- Australians on income support: Age Pension = 2.16m; Disability Support Pension = 792,000; Newstart = 556,000; Youth Allowance = 405,000
- Adult literacy and numeracy: close to half of Australian adults with skills below the minimum considered necessary 'to cope with the demands of everyday life and work'
- Social exclusion: "the level of marginal exclusion ranged between 26 and 33 per cent.... Between four and six percent were 'deeply excluded' and less than one per cent were 'very deeply excluded'"



what are the implications for...?

- capacity to interpret and act on price signals
- capacity to select an appropriate tariff
- 'willingness to pay'

Sources: DEEWR, Labour Markets and Related Payments; FAHCSIA, Annual Report; ABS, Adult Literacy and Life Skills Survey; Brotherhood of St Laurence/ MIAESR

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Businesses' planning

go beyond consultative committees

different engagement methodologies for different customer groups

liaise with welfare service providers and advocates

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Research



customers in the research...

- were 'overwhelmed' by rising utility prices and 'bills piling up on top of each other'
- expressed a 'sense of helplessness at being unable to cope'
- were frustrated when they put significant effort into keeping their costs down but don't see this reflected in bills

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Consumer advocacy

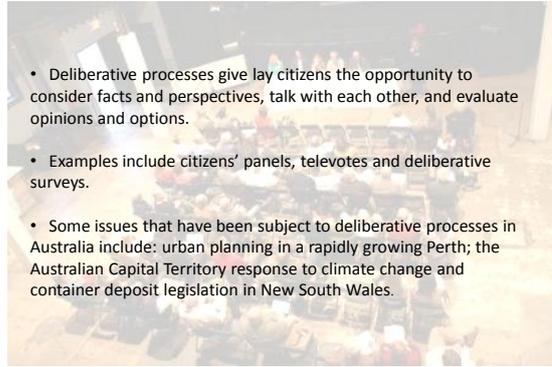
Individuals often lack the means — time, money and know-how — to represent their views as consumers in policy and regulatory forums [...]

Consumer policy advocates can overcome this problem by ensuring that consumer interests are represented in both policy and regulator decision making. Having effective consumer involvement in these forums will reduce the risk of regulators and ministers making poor decisions because of poor information on consumer preferences.

- Productivity Commission (2011) *Australia's Urban Water Sector*

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Deliberative processes



- Deliberative processes give lay citizens the opportunity to consider facts and perspectives, talk with each other, and evaluate opinions and options.
- Examples include citizens' panels, televotes and deliberative surveys.
- Some issues that have been subject to deliberative processes in Australia include: urban planning in a rapidly growing Perth; the Australian Capital Territory response to climate change and container deposit legislation in New South Wales.

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