

# WaterShed

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## The Smart Regulator

by Professor Peter Cullen

The role of the regulator has so far escaped the spotlight of reform that has shone on much of the water industry. This has now changed with the Productivity Commission releasing a report on 'Setting Drinking Water Standards' (<http://www.pc.gov.au>). This report provides an outstanding analysis of many of the issues facing regulation in complex areas like public health and environment, where technical inputs must be weighed against social and economic factors in the setting of standards.

The time has come to examine what we expect of a smart regulatory system.

- What are the appropriate standards required to deliver societal objectives?
- How can catchment and water managers ensure that they meet societal objectives in a cost-effective way?
- How can society be assured that the required standards have been met?

### SETTING STANDARDS

The desired outcomes must be determined before setting the required standards. These might be a mix of environmental, health and financial outcomes. We need a system of evidence-based regulation where we spend to achieve an agreed and clear outcome.

Evidence-based regulation has not always been the case, especially with strategies like "Best Management Practice" (BMP) that are input driven rather than outcome driven. The engineering profession quite likes BMP approaches because it means there is a continuity of work in upgrading facilities as technology leads to improvements. A bit like upgrading your computer each year although the old system does what you want. For Directors of water utilities who now carry personal responsibility for performance – why take risks with old technologies?

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On the other hand, evidence-based standards are driven by the desired and specified outcomes. The CRC for Water Quality & Treatment has recently released a \$3 million epidemiological study of 600 households in Melbourne that showed no health benefits for providing filtration in the Melbourne context. Such filtration would have cost water users some \$500 million. The study concluded "we have found no evidence of waterborne gastroenteritis from a chlorinated unfiltered water supply drawn from a protected catchment" indicating that the desired outcome of improving public health would not be achieved by such filtration.

### **MEETING AGREED STANDARDS**

Catchment and water managers have to meet agreed standards. If financial reasons prevent this, they should make it clear for what uses the water is safe. Where management agencies do not have the technical skills, and where this function is not outsourced, Governments should consider establishing new management arrangements. Where managers have been captured by a particular user of the resource, then consideration should be given to privatizing them and establishing a broad based regulatory manager to work in the wider public interest.

### **MONITORING STANDARDS**

Regulators are needed to ensure standards are being met. This is a policing function, and is a necessary part of any regulatory system. Regulators need to ensure that cost-effective monitoring programs are in place. This requires better planning and specification of what has to be achieved than is common. Many argue that regulators should ensure monitoring data is available on the web. These data should be used to improve management and for prosecution where necessary.

### **ENCOURAGING INNOVATION**

It is important to separate the three elements of regulation: standard setting, meeting standards and monitoring compliance. Regulators, industries and the wider public all have an interest in what standards are adopted. These are often lowest common denominator standards agreed across a number of political jurisdictions. Openness and transparency are required to help this process work well.

It is important for regulators to encourage managers to be innovative with different ways of delivering

standards, which can involve taking risks. Never let us assume that what passes as BMP is in fact best, or even acceptable. There are probably always "better practices", and we need to encourage managers to trial and innovate. Regulators determine whether the industry operates in a climate of innovation or in a comfort zone equating expenditure with effectiveness.

Regulatory agencies are capable of being innovative in how they achieve goals, and this needs to be encouraged. Working with industries to improve practices and better feedback and reporting mechanisms are important examples.

### **SEPARATION OF REGULATORS**

The States have separate systems for regulating human health, environmental and financial aspects of the water industry. Would we be better served by integrating these separate regulatory roles into one system? We commonly have price setting regulators, and we have the National Competition Council assessing progress under the COAG water reforms. Many regulators are under-resourced in comparison to the organisations they are attempting to regulate.

### **PRODUCTIVITY COMMISSION**

The Productivity Commission has reported on its benchmarking study of a number of countries. It claims that water quality regulation in Australia does not meet BMP and is well behind the USA where consultation is better and standards rigorously assessed. Also, regulatory agencies in the US are better staffed than their Australian counterparts. The Productivity Commission Report says that Washington State, which has a similar population to NSW, has 80-90 people involved in this area, compared to 4 in NSW.

### **REGULATORY REFORM**

The Australian water industry has achieved an impressive suite of reforms since the release of the COAG Water Resources Policy in 1994. The Productivity Commission's report focuses our attention on the complex issues facing regulators and clearly there is scope to improve Australia's fragmented regulatory systems. The next wave of water reform should address Australia's current regulatory systems and practises.