



PERFORMANCE AUDIT

24 SEPTEMBER 2020

Support for regional town water infrastructure

NEW SOUTH WALES AUDITOR-GENERAL'S REPORT

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In accordance with section 38E of the *Public Finance and Audit Act 1983*, I present a report titled '**Support for regional town water infrastructure**'.

A handwritten signature in black ink, appearing to read 'Margaret Crawford'.

Margaret Crawford

Auditor-General
24 September 2020

contents

Support for regional town water infrastructure

Section one – Support for regional town water infrastructure

Executive summary	1
Introduction	7
Planning for regional town water infrastructure	15
Targeting regional town water infrastructure funds	26

Section two – Appendices

Appendix one – Response from agency	41
Appendix two – Key terms	44
Appendix three – About the audit	45
Appendix four – Performance auditing	48

Section one

Support for regional town
water infrastructure

Executive summary

Safe and reliable water and sewer services are essential for community health and wellbeing, environmental protection, and economic productivity. In 2019, during intense drought, around ten regional New South Wales (NSW) cities or towns were close to 'zero' water and others had six to 12 months of supply. In some towns, water quality was declared unsafe.

Ensuring the right water and sewer infrastructure in regional NSW to deliver these services (known as 'town water infrastructure') involves a strategic, integrated approach to water management. The NSW Government committed to 'secure long-term potable water supplies for towns and cities' in 2011. In 2019, it reiterated a commitment to invest in water security by funding town water infrastructure projects.

The New South Wales' *Water Management Act 2000* (WM Act) aims to promote the sustainable, integrated and best practice management of the State's water resources, and establishes the priority of town water for meeting critical human needs.

The Department of Planning, Industry and Environment (the department) is the lead agency for water resource policy, regulation and planning in NSW. It is also responsible for ensuring water management is consistent with the shared commitments of the Australian, State and Territory Governments under the National Water Initiative. This includes the provision of healthy, safe and reliable water supplies, and reporting on the performance of water utilities.

Ninety-two Local Water Utilities (LWUs) plan for, price and deliver town water services in regional NSW. Eighty-nine are operated by local councils under the New South Wales' *Local Government Act 1993*, and other LWUs exercise their functions under the WM Act. The Minister for Water, Property and Housing is the responsible minister for water supply functions under both acts.

The department is the primary regulator of LWUs. NSW Health, the NSW Environment Protection Authority (EPA) and the Natural Access Resource Regulator (NRAR) also regulate aspects of LWUs' operations. The department's legislative powers with respect to LWUs cover approving infrastructure developments and intervening where there are town water risks, or in emergencies. In this context, the department administers the Best Practice Management of Water Supply and Sewerage Guidelines (BPM Guidelines) to support its regulation and to assist LWUs to strategically plan and price their services, including their planning for town water infrastructure.

Under the BPM Guidelines, the department supports LWU's town water infrastructure planning with the Integrated Water Cycle Management (IWCM) Checklist. The Checklist outlines steps for LWUs to prepare an IWCM strategy: a long-term planning document that sets out town water priorities, including infrastructure and non-infrastructure investments, water conservation and drought measures. The department's objective is to review and approve (i.e. give 'concurrence to') an IWCM strategy before the LWU implements it. In turn, these documents should provide the department with evidence of town water risks, issues and infrastructure priorities.

The department also assesses and co-funds LWU's town water infrastructure projects. In 2017, the department launched the \$1 billion Safe and Secure Water Program to ensure town water infrastructure in regional NSW is secure and meets current health and environmental standards. The program was initially established under the Restart NSW Fund.

This audit examined whether the department has effectively supported the planning for and funding of town water infrastructure in regional NSW. It focused on the department's activities since 2014. This audit follows a previous Audit Office of NSW report which found that the department had helped to promote better management practices in the LWU sector, up to 2012–13.

Conclusion

The Department of Planning, Industry and Environment has not effectively supported or overseen town water infrastructure planning in regional NSW since at least 2014. It has also lacked a strategic, evidence-based approach to target investments in town water infrastructure.

A continued focus on coordinating town water planning, investments and sector engagement is needed for the department to more effectively support, plan for and fund town water infrastructure, and work with Local Water Utilities to help avoid future shortages of safe water in regional towns and cities.

The department has had limited impact on facilitating Local Water Utilities' (LWU) strategic town water planning. Its lack of internal procedures, records and data mean that the department cannot demonstrate it has effectively engaged, guided or supported the LWU sector in Integrated Water Cycle Management (IWCM) planning over the past six years. Today, less than ten per cent of the 92 LWUs have an IWCM strategy approved by the department.

The department did not design or implement a strategic approach for targeting town water infrastructure investment through its \$1 billion Safe and Secure Water Program (SSWP). Most projects in the program were reviewed by a technical panel but there was limited evidence available about regional and local priorities to inform strategic project assessments. About a third of funded SSWP projects were recommended via various alternative processes that were not transparent. The department also lacks systems for integrated project monitoring and program evaluation to determine the contribution of its investments to improved town water outcomes for communities. The department has recently developed a risk-based framework to inform future town water infrastructure funding priorities.

The department does not have strategic water plans in place at state and regional levels: a key objective of these is to improve town water for regional communities. The department started a program of regional water planning in 2018, following the NSW Government's commitment to this in 2014. It also started developing a state water strategy in 2020, as part of an integrated water planning framework to align local, regional and state priorities. One of 12 regional water strategies has been completed and the remaining strategies are being developed to an accelerated timeframe: this has limited the department's engagement with some LWUs on town water risks and priorities.

1. Key findings

A program to integrate local, regional and state water planning only started in 2018–19

The department has not implemented a state-wide and regionally integrated approach to managing town water security risks and infrastructure priorities. As such, the department has been supporting planning for and funding LWUs' town water infrastructure without a long-term strategy. The New South Wales' *Water Management Act 2000* (WM Act) made provision for a state-wide, strategic water plan almost 20 years ago.

In 2018–19, the department commenced a program to develop 12 regional water strategies by 2021. The department had started a strategy for the Greater Hunter region in 2014, which is now complete but not yet implemented. The department has also outlined 'regional town water strategies' as a new approach for guiding LWUs to do cross-LWU boundary planning and has committed to co-fund these. In 2020 the department started work on a state water strategy.

The department's regulation of LWUs is poorly defined and it lacks governance arrangements to coordinate its strategic and regulatory activities

Although it is the primary regulator of LWUs, the department does not have a LWU sector regulatory policy or operational plan per departmental regulatory policy. It has also not clearly defined its oversight and support roles with regards to LWU's town water infrastructure planning via its Integrated Water Cycle Management (IWCM) Checklist and other guidance, under the Best Practice Management of Water Supply and Sewerage Guidelines. The department advises that it operates collaboratively with LWUs but the lack of clarity in its regulatory role and responsibilities limits accountability and transparency around its activities.

The department's Water Group does not have a formal mechanism for coordinating with the department's Office of Local Government on strategic approaches to town water policy, regulatory issues, or sector engagement. The department has also not established a structure to coordinate regulatory, strategic or operational responses to town water risks and infrastructure issues. This is significant given the NRAR, NSW Health, and the EPA regulate other aspects of LWUs' operations, and as water supply, safety and environmental outcomes are interdependent.

More broadly, the department has also not formalised responses to numerous inquiries and reviews since at least 2008, which have found a need to improve its regulatory approach to LWUs, including through reviewing related legislative arrangements for the State's management of town water. In 2015, the department started an internal review to investigate regulatory reform options but has yet to consult widely.

The department's oversight and reporting on LWUs' Integrated Water Cycle Management (IWCM) planning has been limited

The department does not have a clear picture of the current status of IWCM planning and implementation across the LWU sector, and the available data indicates that engagement has been limited since 2014. This lack of visibility limits the department's capacity to use IWCM strategies to build an evidence base about catchment-level risks or strategic issues, and to inform assessments of appropriate solutions.

Of the 92 LWUs, the department's records indicate that half submitted IWCM planning documents for review at some point since 2014 and only eight LWUs have a current IWCM strategy that the department has approved i.e. granted 'concurrence'. This data was compiled for the audit as the department does not have reliable IWCM status monitoring systems in place. The last information published by the department on the status of IWCM planning in 2015–16 was also poorly defined and reported in a way that overstated the progress of IWCM planning across the LWU sector. This matters as the department intended this information would encourage LWUs' performance.

In June 2020, the department released an online data dashboard with the previous six years of LWU water and sewer service performance and financial indicators. This does not include data on LWU sector progress against the BPM Guidelines, such as the status of IWCM planning.

The department's procedures for reviewing IWCM documents are unclear, impacting on LWUs engagement

The department's administration of its IWCM review processes lacks transparency and consistency. The department does not have documented internal procedures for reviewing, approving, and providing feedback to LWUs on their IWCM planning documents (issues papers or strategies). The department's practices vary without business rules to guide professional judgement. It has not set timeframes for completing the review and approval of IWCM planning documents for LWUs. In some cases, approval has taken up to three years. The LWUs that we interviewed reported that the department's IWCM review processes create inefficiencies, and many LWUs have slowed or stalled their IWCM planning.

The department has also not ensured that its supports to encourage IWCM planning are clearly communicated to LWUs, or well targeted. It has not initiated sector-wide training on its best practice guidance for strategic town water planning since 2014. It also does not have a documented approach to proactively engage the LWUs with the greatest support needs or town water risks: its support for IWCM planning has been ad hoc. Today, LWUs' understanding of what the department requires and expects varies widely. This is significant as it typically costs LWUs around \$250,000 (and often more) to engage a consultant to produce an IWCM strategy, and the size of the consultancy market is reportedly limited.

The department did not design or implement a clear approach to targeting the initial Safe and Secure Water Program (SSWPv1) funds

The department launched the \$1 billion Safe and Secure Water Program in August 2017. In the first version of the program (SSWPv1), its aim was to fund town water infrastructure projects that would deliver health, social and environmental benefits, and support economic growth and productivity. But the program's design did not reflect the evidence available to the department about how to prioritise investments towards town water risks and support the varied needs and capacity of the LWU sector. It also did not incorporate a well-defined approach to targeting the remainder of the program funds i.e. the \$592 million that was potentially available to applicants, following the NSW Government's decision to fund a pipeline from the Murray River to Broken Hill from the program.

The department-led, multi-agency Technical Review Panel (TRP) assessed the majority of SSWPv1 projects (201 or 89 per cent of project records) for eligibility. The TRP was well regarded for its technical expertise in assessing detailed applications, but it did not have adequate access to strategic information about regional water priorities or about local issues from IWCM strategies to fully inform its assessments. Overall, the projects recommended for funding through the SSWPv1 were spread broadly across the sector without a clear relationship to key LWU characteristics or levels of town water risk.

Around a third of funded projects were not assessed transparently or consistent with good practice grants administration

Thirty-nine SSWP projects (out of 108) with funds committed to LWUs as of May 2020, had not been recommended through the advertised TRP assessment process. The department led various alternative processes to recommend projects for funding around the launch of the SSWPv1 in 2017, and again in transitioning to a revised program (SSWPv2) in late 2018–19. These processes were generally used to fast-track announcements and were not consistently documented within the program. This limited transparency around those processes and the criteria applied, and the evidence used in making the decisions.

The SSWPv2 has established an approach to target funds but implementation is delayed

The department launched SSWPv2 in October 2018, but its implementation was subsequently delayed by about a year. As of August 2020, the department has not funded any projects under the revised program. The transition to SSWPv2 occurred during intense drought in NSW when LWUs and the department were carrying out emergency responses.

The SSWPv2 design includes a clear focus on town water risk reduction with defined metrics for water quality, security and environmental risks, and accounts for the socio-economic status of LWUs' communities. Using this approach, the department has identified and rated over 1,000 town water risks across regional NSW. In April 2020 the department invited LWUs to provide feedback on these risks and plans to develop projects with LWUs to address the highest priority risks. The department has also reserved SSWPv2 funds to encourage LWUs' strategic planning for town water infrastructure through processes to develop IWCM strategies, and for Joint Organisations of Councils (JOs) to develop regional town water strategies.

The department lacks systems for integrated project monitoring and program evaluation

The department does not have the systems in place to assess whether, or to what extent, its support and funding of town water infrastructure are contributing to improved town water outcomes for communities. It did not develop or implement a monitoring and evaluation plan for SSWPv1. The department outlined a plan for monitoring and evaluating SSWPv2 but has not started to implement it. Its plans require updating to incorporate data on the progress of SSWPv1 projects and to effectively monitor the impact of its efforts to resolve cross-LWU boundary water security issues across programs.

There is scope for the department to better coordinate its strategic water planning, program funding and LWU sector engagement activities

There are timing, coordination and stakeholder engagement risks to the department's integration of state-wide regional water planning with its activities to fund and support town water infrastructure planning. To date, local consultations to develop regional water strategies have been undertaken to tight timeframes. This has limited opportunities for information sharing and contributes to the department's unclear processes for how local and cross LWU-boundary town water risks will be assessed and considered for funding.

Opportunities exist for the department to better coordinate its co-funding of IWCM strategies and regional town water strategies, and the development of regional water strategies. For example, providing LWUs timely access to its climate risk modelling and water availability data. Sector engagement will continue to be integral to the effectiveness of the department's investments to build evidence about town water risks, to fund infrastructure and non-infrastructure solutions, and to work with LWUs to address these.

2. Recommendations

As a matter of priority, the Department of Planning, Industry and Environment should:

1. Develop and implement a clear policy and regulatory approach to overseeing and supporting LWUs. It should do this in consultation with the LWU sector.
2. Address coordination, timing and LWU sector engagement risks to integrating state-wide regional water planning with investments in town water infrastructure and risk reduction. This should include:
 - coordinating the development and continuous improvement of regional water strategies with current evidence of town water risks and investment priorities
 - ensuring consultations on regional water strategies provide adequate and transparent opportunities for LWUs' input about town water risks and proposals to resolve these
 - providing LWUs with timely access to its climate risk and water availability data and modelling approaches, as these become available.

By October 2021, the Department of Planning, Industry and Environment should:

3. Design and commence implementation of an outcomes-focused approach to its oversight and support of LWUs' Integrated Water Cycle Management (IWCM) planning, supported by:
 - clear definitions, assessment criteria, procedures and timeframes for the assessment of IWCM planning instruments
 - accurate data to monitor and publicly report on IWCM planning and implementation status
 - assistance to LWUs to procure value-for-money IWCM planning services, including enabling joint or regional approaches.

4. Improve the administration and transparency of its LWU oversight, support and funding activities. At a minimum, the requirements of the New South Wales' *State Records Act 1998* should be met. Actions should also involve implementing:
 - clear procedures for key decision-making points and for quality improvement and assurance processes
 - clear procedures that delineate the delivery of its regulatory and support activities, including to identify and resolve conflicting duties
 - an evidence-based approach to targeting engagement with the LWU sector
 - customer and outcomes-focused metrics to measure impact.
5. Establish governance arrangements that coordinate its strategic planning, investment prioritisation and regulatory approaches to improving town water outcomes. This should include arrangements for:
 - coordinating LWU sector engagement with whole-of-government priorities and approaches to partnering with Local Government
 - promoting interagency coordination on LWU sector regulation issues across town water security, quality and environmental risks.
6. Formalise consultative arrangements with the LWU sector that better enables collaboration and at a minimum:
 - delivers clear and consistent communications about its regulatory purpose, oversight activities and supports especially related to IWCM planning, and funding activities
 - ensures LWU feedback is actively sought, documented and considered in its design and delivery of regulatory approaches, planning guidelines and funding programs.

On an ongoing basis, the Department of Planning, Industry and Environment should:

7. Monitor and evaluate its investments in town water risk reduction and infrastructure funding to improve transparency and enable the department to identify outcomes and the contributions of its investments towards its policy goals. This should include:
 - maintaining accurate data on the status of Safe and Secure Water Program (SSWPv1) projects, supported by formal information sharing with Infrastructure NSW
 - updating and implementing a monitoring and evaluation plan for the SSWPv2
 - monitoring the status and resolution of cross-LWU boundary town water risks.

1. Introduction

Regional New South Wales (NSW) is home to about a third of the state's population. Infrastructure that provides safe and reliable water and sewer services (also known simply as 'town water infrastructure') is essential for community health and wellbeing, environmental protection, and economic productivity. Planning for and meeting these infrastructure needs, as well as identifying when non-infrastructure options may be a better solution, involves a strategic and integrated approach to water resource management in regional NSW.

1.1 Regional town water management and regulation

The department's water management and planning role

The Department of Planning, Industry and Environment (the department) is responsible for managing water resources in NSW. This includes planning, policy development, and regulatory frameworks. The department's responsibilities are primarily governed by the New South Wales' *Water Management Act 2000* (WM Act). The WM Act aims to provide for the sustainable and integrated management of the state's water for the benefit of both present and future generations. Its objectives include:

- recognising the role of the community, as a partner with government, in resolving issues relating to the management of water sources
- encouraging best practice in the management and use of water.

The WM Act sets out an approach for strategic water management to give effect to the principles under the Act. Since its commencement in 2001, the WM Act has allowed for the establishment of a State Water Management Outcomes Plan for the 'development, conservation, management and control of the State's water resources'.

The WM Act also sets out priorities for how water is to be shared and allocated to the environment and for various water uses. Water that is required to meet 'critical human needs' is recognised in the WM Act by the priority of major and Local Water Utility (LWU) access licences above other licences, and by the high priority of water distribution for 'essential town services'.

The key piece of Commonwealth legislation relating to water management is the *Water Act 2007*, which includes the Murray Darling Basin Agreement.¹ The department is also responsible for ensuring water management is consistent with objectives set out in the National Water Initiative. The National Water Initiative was established and agreed to by the Australian, State and Territory Governments in 2004. National Water Initiative objectives that are most relevant to town water infrastructure planning in regional NSW include:

- providing healthy, safe and reliable water supplies
- increasing water efficiency
- encouraging recycling and wastewater where efficient, and encouraging innovation
- improved pricing.

In 2019 the Australian Government committed to work with State and Territory Governments to renew the National Water Initiative.

In late 2019, New South Wales' *Water Supply (Critical Needs) Act 2019* came into effect. Its stated aim is to facilitate emergency water supplies in certain towns and localities, and to declare certain water infrastructure developments as critical State significant infrastructure.

¹ The *Basin Plan 2012*, adopted under the Act, requires the NSW Government to develop water resource plans.

Commitments to town water security in regional NSW

In 2011, the NSW State Plan 2021 identified a goal to secure potable water supplies in NSW. It made a commitment to 'securing quality drinking water in towns and cities across NSW' by working with water utilities to improve the long-term security of town water supplies. Actions for meeting this goal included:

- delivering town water infrastructure funding programs
- reviewing LWUs' performance and advising on improved LWU operations.

Infrastructure NSW's 2014 and 2018 State Infrastructure Strategies also set out NSW Government objectives to:

- support the critical needs of regional industries and communities by ensuring water security and quality of supply
- support the growth, productivity and liveability of regional communities by ensuring that water security, quality and wastewater services protect public health and the environment.

In 2019, the department confirmed its role in investing in regional and local water infrastructure projects to secure water supply, and supporting local water utilities to improve water services. In line with the 2018 Water Reform Action Plan, the department has also committed to increasing its transparency by working with communities, including LWUs, to secure water by developing regional water strategies.

Regulatory context for town water services and utilities' performance

LWUs plan for, price and deliver water supply and/or sewerage ('town water') services and are individually responsible for this in the cities and towns in which they operate. The department is the primary regulator of LWUs. It states that it is responsible for ensuring that the water and sewer services provided by LWUs in regional NSW are safe, secure and sustainable.

There are 92 LWUs in regional NSW. Most LWUs (89) exercise water supply functions under Chapter 6, Part 3 Division 2 of the New South Wales' *Local Government Act 1993* (LG Act) and are operated by local councils. Four operate as water supply authorities under the WM Act.² LWUs are enabled, but not required, to exercise these water supply functions.

The department's main regulatory authority with respect to local council-operated LWUs is to require they obtain ministerial approval for certain construction works (s. 60), and comply with ministerial directions where there are safety, property or public health concerns, or in emergencies (s. 61 and s. 62). Also, where LWUs have failed to ensure the safety, quality and security of the town water supply, the NSW Government can appoint an administrator, following a public inquiry (s. 66). The Minister for Water, Property and Housing is the responsible minister for these powers, and requires the concurrence of the Minister for Local Government with respect to Section 66.³

The department oversees the performance of LWUs to reduce the risk of needing to intervene in these emergency cases and to provide assurance to the NSW Government that the requirements of the WM Act are met through the satisfactory performance of each LWU. The department also monitors LWUs as part of its commitments to water reform under the National Water Initiative.⁴

² These are Cobar Water Board, Essential Energy, Fish River Water Supply, and Central Coast Council, which also exercises some of its functions under the LG Act.

³ As the successor to the Minister for Primary Industries, referenced in sections 57–55 of the LG Act, and successor to the Minister for Energy and Utilities, referenced in Section 406(6) of LG Act. See Section 38 of the *Administrative Arrangements (Administrative Changes - Ministers) Order (No 2) 2019*.

⁴ Under National Water Initiative requirements, the department provides performance information about NSW utilities for the National Performance Monitoring Reports. This is required for larger utilities (those with over 10,000 property connections) and includes 28 of the LWUs.

In 2004 the department prepared the Best Practice Management of Water Supply and Sewerage Guidelines (the BPM Guidelines), which were gazetted under the LG Act in 2007. The purpose of the BPM Guidelines is to encourage LWUs to plan for and deliver effective, efficient and sustainable town water services. Under Chapter 13, Part 3 Division 1 of the LG Act, a council can claim a dividend from the LWU's fund if it can demonstrate that it has 'substantively complied' with the BPM Guidelines (s. 409). This section of the LG Act is extended to non-council LWUs that are established under the WM Act.

Prior to the establishment of the Department of Planning, Industry and Environment in 2019, the NSW Government's functions to oversee LWUs were administered by the Office of Water in the (then) Department of Industry. Since April 2019, these functions have been administered by the Water Group in the department. The department's Office of Local Government (OLG) regulates local council performance more generally. All local councils in NSW are required to undertake integrated planning and reporting, including asset management and financial plans.

Other state government agencies are responsible for the following aspects of LWU regulation.

- NSW Health, in exercising regulatory functions under the New South Wales' *Public Health Act 2010*, is responsible for ensuring drinking water quality outcomes. LWUs are required to develop and adhere to a Drinking Water Management System, including annual review reporting to the local Public Health Unit.
- The NSW Environment Protection Authority (EPA) regulates the quality of discharges from sewerage treatment plants under the New South Wales' *Protection of the Environment Operations Act 1997*, and is an independent statutory authority within the department.
- The Natural Resources Access Regulator (NRAR) is an independent regulator responsible for compliance with and enforcement of water management legislation in NSW. This includes granting and managing water licences and works approvals for LWUs and ensuring LWUs' compliance with water access licences.

1.2 Local Water Utilities and their operating context

The 92 LWUs in regional NSW provide town water supply and sewer services to around 1.85 million people.

Regional conditions in NSW are challenging, with drought, flood and climate variability. There is also significant variability in the geographic coverage and population trends in LWUs' areas of operation. For example, areas serviced range from 285 to over 50,000 square km while the population ranges from 1,000 to over 300,000. Remoteness can contribute to skills shortages, including in specialist water engineers and operators to maintain town water infrastructure.

In 2018–19, LWUs had an annual revenue of \$1.51 billion and combined infrastructure current replacement costs of \$28.8 billion. According to the department, larger LWUs usually have significant economies of scale with the capital and operating costs of town water infrastructure, and have better access to materials and equipment in larger urban centres. In contrast, many smaller LWUs experience relatively high capital, operating and maintenance costs per property. LWUs that service large inland areas with small populations also tend to have higher capital and operating costs than those in coastal NSW, due to the drier climate and more limited availability of water.

Our 2015 Country Towns Water Supply and Sewerage Program report found that LWUs' performance had generally improved over the last 20 years, and that the department's support (via the then Office of Water) had helped. It found that the department had promoted the adoption of better management among LWUs, according to data up to 2012–13, and its funding had made a difference in reducing a backlog of town water infrastructure. But it also found that 393 of 831 identified projects would not be funded and the infrastructure backlog would not be eliminated.

In 2016, the department estimated that LWUs would need to increase their current identified and planned capital works (at that time approximately \$11 billion over 30 years) by 30 per cent, to achieve appropriate water security for regional NSW towns.

1.3 Support for planning town water infrastructure

Integrated water cycle management planning

Integral to the department's support for LWU's town water infrastructure planning is its administration of the Integrated Water Cycle Management (IWCM) planning guidance. This is an element of the BPM Guidelines and accompanying Management Framework, along with the department's guidance to LWUs on their business planning; pricing, supply and waste regulation; and performance monitoring. According to the BPM Guidelines, the development and implementation of an IWCM strategy contributes to demonstrating the NSW Government's compliance with the National Water Initiative.

The department has encouraged LWUs to complete and implement IWCM strategies for their communities as 'best practice' since 2004. It promotes the IWCM strategy as 'critical for long-term strategic planning for ensuring that all water security, water quality and sewage management needs and risks in the LWU's urban water supply and sewerage systems are addressed within the planning horizon.' The manual for the NSW Government's Integrated Planning and Reporting framework, produced by the OLG, states that LWUs 'need to comply with' the BPM Guidelines, which includes developing and implementing an IWCM strategy.

In 2019 the department set out to achieve '100% of LWUs [to] have a current IWCM strategy'.

Exhibit 1: The purpose and features of an IWCM strategy

An IWCM strategy is a LWU's peak 30-year planning document for the provision of appropriate, affordable, cost-effective and sustainable urban water services that meet community needs and protect public health and the environment. It should:

- set the objectives, performance standards and performance indicators for the water and sewer business
- identify the needs and issues with respect to water security, water quality improvement, sewage management and distribution/collection system works based on evidence and sound analysis
- identify the 'right' water supply and sewerage scheme options and 'right size' infrastructure and non-infrastructure components
- determine implementation and investment priorities in consultation with the community and stakeholders
- identify the 'best value 30-year' IWCM scenario on a triple bottom line basis.

The department states that undertaking IWCM planning and having an approved IWCM strategy will also streamline town water infrastructure related approvals (e.g. under s. 60) and provide an evidence base to support town water infrastructure project proposals. It should inform the LWU's price path for water and sewer services.

Source: Audit Office of NSW summary from the department's 2014 IWCM Checklist and BPM Guidelines.

To facilitate LWUs to do this IWCM planning, the department developed a checklist in 2014. The 2014 IWCM Checklist aims to clarify the tasks that a LWU 'must undertake' to develop an IWCM strategy over an eight-year cycle. It is designed to be used by a LWU directly, or when engaging a consultant.

In the 2014 IWCM Checklist, the department states that it will review and approve IWCM planning documents (issues papers and strategies) to provide assurance that the LWUs' planning is 'sound'. The approval that the department applies is termed 'concurrence'. The Checklist was reissued in 2019 with additional information on data requirements and remains the most current departmental guidance on IWCM planning.

The department also provides operational and technical advice and training to LWUs on their business planning, and conducts inspections of LWU operations.

Reporting on IWCM planning as part of LWUs' performance

The department publishes data on LWUs' water and sewer system service indicators and financial indicators to promote LWU performance to provide assurance to the NSW Government that it is meeting requirements under the WM Act. The NSW Water Supply and Sewerage Performance Monitoring and Benchmarking Reports ('LWU Performance Monitoring and Benchmarking Reports') from 2009–10 to 2015–16 included this financial and performance data as well as information on LWU's implementation of the BPM guidelines such as whether there was an 'IWCM strategy commenced.'

1.4 Co-funding town water infrastructure

Context

Since 1880, some form of financial assistance has been provided by the NSW Government to regional towns for the provision of town water services. Successive NSW Governments have committed funding to town water infrastructure in recognition of the ongoing needs faced by LWUs. The department's Country Town Water Supply and Sewerage Program (CTWSSP), for example, started in 1935 and from the 1990s had a focus on funding infrastructure backlogs.

Infrastructure NSW's 2014 State Infrastructure Strategy noted the capital-intensive nature of the water sector and the need to invest in regional and town water infrastructure to ensure water security and/or to meet health and environmental standards. The department's 2016 CTWSSP evaluation noted that,

'in the absence of government intervention, there would be an underinvestment in safe water supply and sewerage services in regional towns due to the lack of economies of scale, remoteness and the small population base... Avoiding these adverse health outcomes saves public health costs and associated productivity losses. This represents a benefit to the community from the investment in safe water supply and sewerage services.'

Departmental estimates in 2019 projected a future investment of \$5 billion in town water infrastructure would be needed over the next decade to address emerging water security and quality challenges due to climate change and variability and increased water quality and environmental expectations.

Recent and current programs

Since 2014, the department has provided technical advice to and managed a number of town water infrastructure programs. These include the CTWSSP that continued to 2017 and some newer programs listed in Exhibit 2.

Exhibit 2: Recent town water infrastructure programs

Program	Funding announced and fund source	Program aim
Water Security for Regions Program, (WS4R), 2014–16	\$366 million Restart NSW Fund	To help regional communities improve water security and prepare for future droughts.
Regional Water and Waste Water Backlog Program, 2015–17	\$110 million Restart NSW Fund	To deliver a backlog of water and waste water projects in regional areas and to meet its targets for access to quality potable water through new infrastructure builds and infrastructure upgrades.
Safe and Secure Water Program version 1, (SSWPv1), 2017–18	\$1 billion Restart NSW Fund	To fund eligible water and sewerage projects that will deliver public health, environmental and social benefits to regional communities which in turn support economic growth and productivity in the state.
Safe and Secure Water Program version 2, (SSWPv2), 2018– ongoing	Balance of SSWPv1 Consolidated Fund	To co-fund the resolution of water security, public health, environmental outcomes and dam safety risks and issues through infrastructure and non-infrastructure solutions.

Note: Program end dates for WS4R and SSWPv1 indicate the years when applications to the program ceased.

Source: Audit Office of NSW summary.

For the programs listed in Exhibit 2 that were funded by the Restart NSW Fund, Infrastructure NSW was responsible for the funds administration component of program management. These programs were required to be consistent with the purpose of the New South Wales' *Restart NSW Fund Act 2011*, which is to 'improve economic growth and productivity in the State'. The Act allows for funding the planning, selection, implementation and delivery of infrastructure projects (Part 2 Section 6).

The department also manages the Aboriginal Communities Water and Sewerage Program, which funds the maintenance, operation and repair of water supply and sewerage systems in 62 eligible Aboriginal communities in NSW.⁵ Town water infrastructure funding programs such as those listed in Exhibit 2 can contribute to this program meeting its aims.

The Safe and Secure Water Program

The department launched the Safe and Secure Water Program (SSWPv1) in August 2017 as a \$1 billion co-funding program for town water infrastructure: specifically, for local and catchment-scale water and sewerage projects to improve the security and quality of drinking water supplies in regional NSW.

LWUs, state water corporations and prescribed dam owners in regional NSW were eligible to apply. Applications could be made for projects at the scoping, business case, or design and construct stage for the following categories:

- town water security
- catchment-scale water security solutions
- drinking water quality and wastewater management projects
- safety of high-risk dams.

⁵ This program is a joint initiative of the NSW Government, led by Aboriginal Affairs NSW, and the NSW Aboriginal Land Council (NSWALC).

The intended SSWPv1 application and assessment process is outlined below:

1. Applicants submitted expressions of interest (EOIs) for proposed projects to be assessed by a multi-agency Technical Review Panel (TRP) led by the department.
2. The TRP made a 'high level' assessment of whether the proposal is eligible.
3. Eligible applicants submitted detailed applications to the TRP for assessment against strategic, economic, affordability and deliverability criteria.
 - The economic assessment of construction phase projects required a positive benefit-cost ratio.
4. The TRP recommended projects to Infrastructure NSW's Regional Infrastructure Assessment Panel (RIAP), for consideration for funding.
5. After consideration, the Infrastructure NSW CEO submitted projects to the Treasurer who could seek endorsement of the Expenditure Review Committee of Cabinet.

In October 2018, the department relaunched the program (SSWPv2), with remaining Restart NSW funding transferred into the Consolidated Fund. The SSWPv2 has three funding streams:

- Stream 1: Funding for the resolution of priority (highest risk) town water issues and risks
- Stream 2: Funding for IWCM strategies
- Stream 3: Funding for dam safety projects.

1.5 About the audit

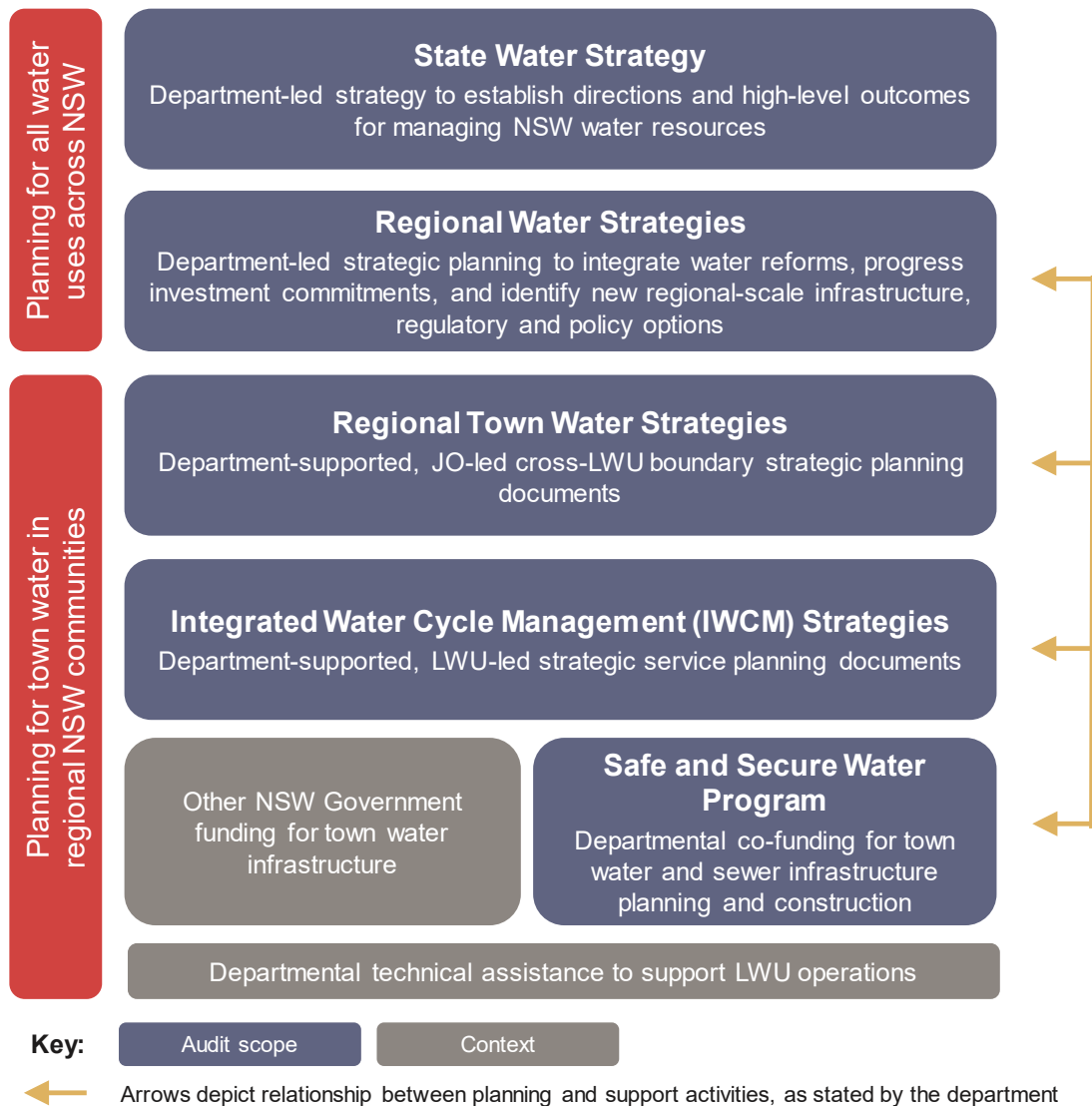
This audit assessed the effectiveness of the Department of Planning, Industry and Environment's support for planning and funding town water infrastructure in regional NSW towns and cities.

We addressed the audit objective by asking the following questions.

- Has the department effectively overseen and facilitated LWUs' planning for town water infrastructure?
- Has the department had an effective framework for assessing town water infrastructure issues to inform state and regional water planning?
- Has the department effectively targeted town water infrastructure funding to policy objectives?

The audit focused on the department's activities since 2014, as illustrated in Exhibit 3. In particular, we examined the administration of the IWCM planning guidance; the design and implementation of the SSWPv1 and the SSWPv2 (streams 1 and 2); and the progress of state-wide, strategic water planning through the Regional Water Strategies Program.

Exhibit 3: Audit scope and the department’s activities to support town water infrastructure planning and funding



Sources: Audit Office of NSW, Department of Planning, Industry and Environment.

In this report, 'town water infrastructure' is defined as infrastructure that provides for water supply and/or sewer services in regional NSW cities and towns. 'Town water security' is used broadly to refer to water supply and quality issues, unless otherwise specified. 'Town water risks' refers to risks to water security, quality or the environment.

Appendix two contains other key terms that are used in this report.

The audit approach included consultations with the LWU sector and in-depth studies of the experiences and impacts of the department's support for 17 LWUs (including a range of sizes, types and locations) in regional NSW. The audit did not assess the department's operational and technical advice to LWUs, but this report refers to these activities when relevant.

The audit did not conduct a statutory review of the department's regulatory arrangements but assessed the effectiveness of the department's oversight and support in the context of existing arrangements, and the progress and transparency of the department's responses to reported legislative and regulatory issues.

Appendix three contains more information about the audit.

2. Planning for regional town water infrastructure

We examined whether the department has effectively supported planning for town water infrastructure since 2014. This assessment was made in the context of its current approach to LWU sector regulation. The findings below focus on whether the department has an effective framework including governance arrangements for town water issues to inform state-wide strategic water planning, and whether (at the local level) the department has effectively overseen and facilitated town water infrastructure planning through its Integrated Water Cycle Management (IWCM) planning guidance to LWUs.

2.1 State-wide strategic planning and governance

A program to integrate local, regional and state water planning only started in 2018–19

The department has not implemented a state-wide and regionally integrated planning framework for management of the State's water resources. As such, the department has been supporting planning for and funding LWUs' town water infrastructure without a long-term strategy for addressing town water security risks and coordinating infrastructure priorities. LWU's planning in turn, has not been able to be informed by state government priorities.

The department's development of state and regional water strategies has been slow to progress since the NSW Government accepted a State Infrastructure Strategy recommendation in 2014 to begin this work.⁶ In 2018, a Legislative Committee Inquiry noted the absence of long-term strategic planning in regional NSW, and recommended funding its development. The department accepted this recommendation.

Formal arrangements to develop a state water strategy commenced in 2020. The *Water Management Act 2000* (WM Act) gave provision for a plan to manage the strategic outcomes of the State's water resources almost 20 years ago. The department advises the state water strategy will reflect the purpose of the WM Act and set the over-arching objectives, actions and strategic outcomes for the state's water resources and the water sector for the next 20 years. The department intends to release the state water strategy for public consultation in 2021.

Regional strategic water planning started in 2018 and in 2019 the department resourced the Regional Water Strategies Program to develop 11 new strategies for the state by 2021. This timeframe is in response to the NSW Government's 2019 election commitment to fast-track their completion. The department had started one regional water strategy earlier in 2014 for the Greater Hunter which took over four years to finalise. As of July 2020, the Greater Hunter Regional Water Strategy is yet to be implemented.

In 2019 the department adjusted its timeframes to develop the regional water strategies in recognition of the impact of the drought and bushfires on affected communities. The department also broadened the scope of its consultation activities to facilitate greater engagement on the development of regional water strategy options. The department advises draft regional water strategies for the Lachlan, Gwydir and Macquarie-Castlereagh regions are due to be released for public consultation in 2020.

⁶ This program of work was a response to the 2014 SIS recommendation to prioritise strategic water planning in the Gwydir and Macquarie catchments. The 2018 SIS reiterated this recommendation as a priority.

Under the Regional Water Strategies Program, the department has identified five strategic objectives, one of which is to 'deliver and manage water for local communities' to improve regional town water security. The department has advised that the state, regional and local strategic water planning frameworks will be integrated with aligned water management priorities.

In late 2019, the department also outlined a 'regional town water strategy' planning approach for LWUs to adopt. This is designed to facilitate cross-LWU boundary water security planning in local catchments or where there are shared water sources, and builds on the department's 2014 guidance for LWUs to consider regional options in their integrated water cycle management (IWCM) strategies where feasible. The department has made co-funding available to Joint Organisations of Councils (JOs) to develop these but has provided limited guidance on the practical integration of regional town water strategies with the outcomes of its regional water strategies, or with LWU's existing or future IWCM strategies.

The department lacks the governance arrangements needed to sustain its strategic planning, and coordinate responses to town water issues

The department has established some but not all of the necessary governance arrangements to coordinate its oversight and support to LWUs for their town water infrastructure planning, and to prioritise and continuously improve its approaches. This is a gap given the department's multiple streams of regional and town water planning and funding activity underway, and the multi-agency approach required to deliver this effectively.

The department is the primary regulator of LWUs, but it has not established whole-of-government LWU regulatory arrangements. The department's Water Group does not have a formal approach to coordinating with the department's OLG. This is needed so that the department can lead and sustain strategic approaches to town water policy and regulatory issues, reporting activities, local priorities, and sector engagement. The department does not have formal mechanisms for other regulators of LWUs such as NSW Health, the EPA, and the NRAR to coordinate regulatory, strategic or operational responses.

Agencies that were interviewed generally advised their engagement with the department on LWU planning and infrastructure was often informal and ad hoc and would benefit from stronger coordination of priorities. This is significant given the interdependencies in water supply, safety and environmental outcomes. LWUs have advised that the lack of agency coordination can lead to conflicting regulatory and technical advice, such as for the construction or modification of water or sewerage treatment works.⁷ In addition, some LWUs expressed concern that IWCM planning documents were not well aligned with and in places duplicated information to be provided through strategic planning documents required by the NSW Government's Integrated Planning and Reporting framework.

The department advises that interagency discussions about the integration of regional and town water priorities occur at the officer level, but there is limited transparency and a lack of structure around these processes. This makes it unclear how information about town water infrastructure priorities that cross-LWU boundaries will be considered in regional water strategies, for example. Such projects are being deferred for assessment through the Regional Water Strategies Program but this does not establish a clear funding pathway.

The department also states the final regional water strategy for each region will include governance arrangements with 'well-defined opportunities for local and regional partnerships to deliver actions' but this is not planned to occur until mid-2021. What role local councils, including LWUs, will have in the delivery of agreed actions under the regional water strategies is not clearly documented.

For individual programs, the department does have governance arrangements in place. For example, since 2019, the Regional Water Strategies Program has been overseen by a whole-of-government executive committee and a departmental senior officer's group to support cross-agency coordination. The department has also previously set up multi-agency panels to assess projects for town water infrastructure funding, and since 2019 there has been a multi-agency review panel under the Safe and Secure Water Program (SSWP) to prioritise town water security risks.

⁷ Under Section 60 of the LG Act, LWUs are required to obtain ministerial approval for these works.

The department's regulatory role is poorly defined, creating a lack of accountability and transparency

The department has not defined a clear approach to overseeing and supporting LWUs, or their planning for town water infrastructure. The department states that it adopts a 'collaborative' approach to LWU sector regulation but has not documented a regulatory policy, strategy or operational plan as required by departmental policy. As such, there is a lack of accountability in why and consistency in how the department undertakes its dual responsibilities to oversee and support LWUs.

The department developed the BPM Guidelines in 2004 (updated in 2007) to identify best practice criteria for LWU service planning, pricing, performance reporting and technical considerations (see 1.1). The BPM Guidelines however do not articulate the department's regulatory role in overseeing and supporting LWUs, and this remains unclear.⁸ The department started an internal review process in 2015 to consider its regulatory approach to LWUs, and related policy options, but progress in developing a LWU regulatory policy has stalled. The department re-started its focus on this work in 2019 but is yet to confirm the status of this work, or to consult widely on the options.

A consequence of the department's unclear role in regulating LWUs is conflicting duties for officers i.e. supporting planning and funding for town water infrastructure, while also overseeing LWUs' performance and reviewing their IWCM strategies. For example, while some LWUs value the department's technical advice, other LWUs are unsure about whether (or how) to acquit comments from the department on their IWCM strategies if these do not align with a consultant's advice, and what the implications might be for subsequent regulatory assessments or funding applications. Officers have also lacked protocols to manage matters that involve multiple regulators such as reporting water quality risks to NSW Health versus maintaining positive, educative relationships with LWUs.

Further, the department has not formalised responses to reports about the need to improve its regulatory approach to LWUs more broadly, or to enhance legislative arrangements for the State's management of town water supplies. Over the past 12 years, at least seven reports have documented the need for action or reform. These include reports led by:

- an independent panel in 2008
- the National Water Commission in 2011
- the Productivity Commission in 2011 and 2017
- Infrastructure NSW in 2012
- the Independent Pricing and Regulatory Tribunal (IPART) in 2016
- the Legislative Assembly Committee on Investment, Industry and Regional Development in 2020.

Each review has made different recommendations given their respective scopes, focus and findings, but all raise common issues around the need for the department to improve its existing approaches to support more safe, reliable and affordable town water in regional NSW.

⁸ In particular, this remains unclear following the end of the CTWSSP in 2017 that attached eligibility for program funding to LWUs demonstrating compliance with the BPM Guidelines.

2.2 Support for town water infrastructure planning

This section presents our assessment of the department's activities since 2014 to oversee and support LWUs' town water infrastructure planning, particularly in accordance with the department's guidance for Integrated Water Cycle Management (IWCM) planning. A previous Audit Office of NSW report had found that the department had supported a general improvement in LWU performance across a range of measures to 2012–13. Our findings relate to the department's recent IWCM-related supports, and also consider whether the department is addressing risks associated with these and related activities underway since 2018–19.

Oversight of LWU's planning for town water infrastructure

The department has limited oversight of the status of IWCM planning

The department does not have a clear picture of the current status of LWUs' IWCM planning, which is critical for supporting strategic town water infrastructure planning. The department promotes IWCM planning as 'the best way for local water utilities to identify strategic risks and build a case for an infrastructure or non-infrastructure solution to mitigate an identified risk.' This lack of visibility limits the department's capacity to use IWCM strategies to build an evidence base about catchment-level risks or strategic issues, and inform assessments of appropriate solutions.

Exhibit 4: IWCM planning cycle as outlined in the department's 2014 IWCM Checklist

1. LWUs must first prepare an IWCM issues paper for the department's review and concurrence. This covers regulatory and contractual compliance issues, levels of service, capacity to meet current and future demands, water and sewer system performance, and a review of the LWU's total asset management plan.
 - Once the department reviews the issues paper, and if it gives 'concurrence', the LWU can start developing an IWCM strategy.
2. LWUs must then prepare an IWCM strategy, including a financial and asset management plan, for the department's review and concurrence. The LWU should also include water conservation, drought and emergency response contingency plans.
 - Once the department reviews the IWCM strategy, and if it gives 'concurrence' as representing 'sound' planning, the LWU can then implement the identified 'best value 30 year' IWCM scenario.
3. Each LWU needs to prepare and implement an IWCM strategy every eight years and review it every four years in consultation with the local community.
 - At this four-year (mid-term) review point, the LWU must update its IWCM planning in line with the department's Strategic Business Planning Checklist

Source: Audit Office of NSW summary.

Of the 92 LWUs, the department's records indicate that half (46) submitted IWCM planning documents for review at some point between 2014 to early 2020. Records show that a further eight LWUs (less than ten per cent) finalised an IWCM strategy that has been approved by the department i.e. granted 'concurrence'. The department's records also indicate that over the course of six years:

- the department confirmed the review outcomes of 13 IWCM issues papers from a total of 32 that had been submitted, or less than half (41 per cent) of the papers it received
- the department has put the review of 19 IWCM issues papers and three IWCM strategies 'on hold', which can indicate that the department is seeking further information from the LWU
- no LWU has a IWCM strategy in place as of February 2020 that aligns with the 2019 updates to the IWCM Checklist.

The department compiled these records for the purpose of this audit, so it is not possible to reliably determine the actual status of IWCM planning, or similar planning across the LWU sector. This highlights the limited visibility that the department has had of this activity to date.

A current IWCM strategy that the department has granted concurrence to represents a LWU meeting one of the core elements of the BPM Guidelines. But the department's authority to allow a local council to claim a dividend from its LWU fund if it is 'substantively compliant' with the BPM Guidelines (see 1.1 for background) has not been an effective incentive. According to the department's last published information on this, in 2015–16 only eight LWUs paid the dividend. Interviews with LWUs have also confirmed that this is generally not an effective incentive to take up IWCM planning.

Procedures for reviewing IWCM planning documents are unclear, and practice varies

The department's administration of its IWCM planning processes for LWUs lacks transparency and consistency. This limits procedural fairness and can adversely affect LWUs as the owners and implementers of these strategies. The department has not documented clear internal policies, procedures or assessment criteria to structure its approach to reviewing and approving IWCM planning documents, specifically issues papers and strategies (see 1.3 for an overview of this process).

The department advises that it applies the IWCM Checklist and BPM Guidelines to inform its assessment of LWUs' planning documents and determine if an IWCM strategy, for example, is 'sound'. But the department has not defined its authority or the implication of granting 'concurrence' to an IWCM issues paper or strategy, although it states that this is required before a LWU can implement the IWCM strategy. The Checklist was primarily designed to inform the scope of works to develop an IWCM strategy: it does not set out a framework to inform consistent, transparent assessments, or to articulate where the department's professional judgment is appropriately applied.

The department has not documented its internal delegations, quality management practices and business rules for its IWCM review and approval function either. We reviewed the department's comments on IWCM planning documents and found these varied widely in scope and focus, and requests for further information were often made without a supporting rationale. This is consistent with the reported experiences of LWUs.

Also, the department has not set target timeframes for its review and approval of IWCM planning documents. Departmental officers indicated that if a LWU submitted a document and did not hear back from the department within 30 days then the LWU should take this as a sign to proceed. But the department had not formally communicated this expectation to the sector, nor is this absence of communication a good practice.

LWUs that we interviewed consistently expressed uncertainty about the review status of their IWCM planning documents, which has at times affected the progress of other planning work or town water infrastructure funding applications. Departmental correspondence shows that in most cases the concurrence process spans over two years. Some LWUs advised repeated delays in receiving departmental advice on IWCM planning documents deterred them from finalising IWCM strategies.

Recordkeeping and monitoring systems are not in place to oversee IWCM planning

The department has not maintained full and accurate records of its activities in line with its records management obligations under the New South Wales' *State Records Act 1988*, nor has it had monitoring systems to track the progress of LWU's development and implementation of IWCM planning. These issues have limited the efficacy of the department's oversight but also its capacity to proactively plan for and target support to LWUs for their town water infrastructure planning (see section below on 'Assistance to LWUs and sector engagement' for more information).

The department has not, for example, been consistently collecting administrative data on its review and approval activity. This makes it difficult to assess its progress in administering this function and reveals an accountability gap. The department had to compile data about the status of IWCM planning since 2014 from various sources (e.g. emails, ad hoc records) for this audit.⁹ Without these monitoring systems in place, the department has not had a practice of following up with LWUs when it is time for a mid-term review of their IWCM strategy, as outlined in the Checklist.

The department has not implemented some actions to improve the transparency of its performance. For example, in 2016 the department advised an IPART inquiry that it was implementing a tracking system that would allow LWUs to view the status of their IWCM planning documents online, but this has not happened as of August 2020. The department has however stated that it has been developing an IWCM status database for its internal purposes since 2019. This, at the very least, will be necessary for monitoring and to enable the department to plan and resource its workload. It will also be important for evaluation purposes as the department has committed to funding IWCM strategies through the relaunched Safe and Secure Water Program (SSWPv2).

The department's public reporting on IWCM planning has been misleading and not consistently available to promote LWU performance

The department previously published information about the status of LWUs' IWCM planning in its LWU Performance Monitoring and Benchmark Reports.¹⁰ These reports are intended to encourage LWU performance, but its IWCM reporting was not soundly-based given the absence of systems for IWCM status monitoring (see 1.3 for background on this reporting).

Reporting issues include the 2014–15 and 2015–16 LWU Performance Monitoring reports. This was the last time that the department reported publicly in this format on the status of IWCM planning. These reports contain data on 'IWCM strategy commenced - Yes/No' for each LWU. The department's definition of 'Yes/No' changed between 2014–15 and 2015–16, but in neither year did this provide meaningful performance information. Exhibit 5 illustrates the issues with the department's definitions with an example from the 2015–16 report.

Exhibit 5: Definitions in the department's reporting on 'IWCM strategy commenced'

The department provided three definitions of 'IWCM strategy commenced - Yes'.

- 'Yes' is defined to mean the strategy is complete, approved (given 'concurrence') and ready to commence.
- 'Yes*' is defined to mean the strategy has been reviewed and there are conditions of approval.
- 'Yes*' is defined to mean the strategy is in draft, not complete.

The department did not define how a 'No' would be identified or recorded.

The 'IWCM strategy commenced' data is not included in the department's list of 'critical indicators' that require more comprehensive data validation.

Source: Audit Office of NSW analysis.

⁹ Our reporting of this information is to evidence the efficacy of the Department's oversight of IWCM planning, not to confirm the actual status of LWU's IWCM (or similar) planning across the sector.

¹⁰ Our findings are specific to IWCM commencement data in the LWU Performance Monitoring and Benchmarking Reports.

Noting these definitions, 'IWCM strategy commenced - Yes' effectively means that the department has reviewed a strategy, not that the LWU has started to implement it. As such, its reporting on the status of IWCM planning has been misleading. For example, the 2015–16 report states: 'Eighty-eight per cent of LWUs have either completed or commenced their integrated water cycle management strategy'. In fact, only one of the 92 LWUs had a completed IWCM strategy that the department had also approved as 'sound' and ready to commence. Actual IWCM implementation status is not known.

The remaining LWUs had incomplete IWCM planning documents that may have been in various stages of development. Further, in assessing IWCM strategies, the department 'briefly examined' LWUs' water conservation and drought management plans: a rationale for this level of review was not provided.¹¹

Since 2016, the department has not reported data on IWCM commencement, nor produced a full LWU Performance Monitoring and Benchmark Report for 2016–17, 2017–18 and 2018–19. The department also ceased producing annual Triple Bottom Line performance reports of LWU's implementation of the BPM Guidelines in 2016–17. The department did start a project to improve the reporting system and in 2019 released an online 'data dashboard' with LWU performance data (a subset of performance and financial indicators) for 2017–18. The dashboard is designed to enable LWUs to self-monitor and compare their performance on the reported indicators to other LWUs and to sector medians.

In June 2020, the department updated this dashboard with the annual LWU performance for the previous six years, from 2013–14 to 2018–19. This included the water and sewer service data and financial indicators. However, it does not include data on the status of IWCM planning, or overall performance against the BPM Guidelines. The department has advised that this online dashboard approach will provide a better form of support.

Assistance to LWUs and sector engagement

Assistance has been available to LWUs, but it is not driven by a clear, informed strategy

Since 2014, the department has provided supports to assist LWUs, but these have been limited overall and not informed by a clearly documented strategy based on town water risks or the range of LWU needs across the sector. As such, IWCM planning assistance has not been well targeted and the department has not effectively engaged LWUs in planning for town water infrastructure.

Exhibit 6 shows data on the department's last published data on LWUs' IWCM planning status in 2015–16, compared with the current status of IWCM planning among a sample of 17 LWUs interviewed for this audit. It highlights the limited information recorded by the department on LWUs' IWCM planning and shows the lack of progress made within this group since 2015–16.

¹¹ The 2014 IWCM Checklist was to integrate water conservation and drought management components. Agency and LWU sector stakeholders have reported that this expectation was unclear to them. Public Works Advisory, in the Department of Regional NSW, is now auditing some LWUs' drought management planning.

Exhibit 6: Current status of IWCM planning among sample of LWUs, compared with departmental data from 2015–16

Local Water Utilities in interview sample	Departmental data		Audit Office analysis	
	Last reported IWCM planning status 2015–16	Has the LWU applied for future IWCM funding? 2019–20	LWU reported status of IWCM issues paper 2020	LWU reported status of IWCM strategy 2020
A	Started	--	✓	—
B	Started	--	✓	—
C	Started	--	—	—
D	Started	Yes	✓	—
E	Started	Yes	—	—
F	Started	--	—	—
G	Started	Yes	—	—
H	Started	--	!	!
I	Started	--	—	—
J	Started	Yes	—	—
K	Started	--	—	—
L	Started	--	✓	—
M	Started	Yes	✓	—
N	Started	--	—	—
O	Started	--	—	—
P	Completed	--	✓	✓
Q	Started	--	—	—

Key ✓ **Complete** — **Still in progress** ! **Not progressing**

Notes: 'Last reported IWCM planning status' is drawn from the 2015–16 LWU Performance Monitoring and Benchmarking Report. LWUs shown in the exhibit were selected randomly within a stratified sampling framework to ensure at least one LWU in each DPIE planning region, and a range of LWU sizes and types. IWCM 'still in progress' includes documents submitted to the department with no review outcome.

Sources: Audit Office of NSW analysis (LWU interview data) and Department of Planning, Industry and Environment data.

In view of the department's stated aim to be a 'collaborative regulator', its sector-wide activities related to IWCM planning have been limited overall. Over the past six years, these have involved:

- developing guidelines such as the 2013 draft guidelines on undertaking secure yield studies, the 2014 IWCM Checklist and the 2019 IWCM Checklist, although the checklists were developed without consultation with the sector and widely considered to be 'too detailed', not 'fit-for-purpose' and 'increasingly complex and prescriptive'
- best-practice seminars to LWUs and consultants about the IWCM Checklist, although these occurred once in 2014 and 2015 respectively and reached about 50 per cent of LWUs
- since 2020, co-funding for IWCM planning and catchment-scale regional town water strategies under the Safe and Secure Water Program, which was supported by a series of regional roadshows in mid-2019.

As part of its day-to-day assistance, the department provides individual advice to LWUs via telephone or email on technical and strategic planning matters, or site visits to engage LWUs in IWCM planning. While the LWUs we interviewed have indicated this advice has been useful when available, especially face-to-face contact and engagement with regionally-based officers, the department's support activities have been ad hoc in response to LWU-initiated requests for assistance. At the same time, the department does not hold records that evidence the frequency or nature of this assistance.

The department also has not had a continuous improvement strategy to ensure its support activities are customer-focused and regularly reviewed to remain current. There is consistent sector feedback that the department has not achieved the intent of the 2014 (and updated 2019) IWCM Checklist to simplify processes and minimise the regulatory burden and cost to LWUs.

The department has not consistently communicated and applied IWCM planning guidance

The department's communication and application of IWCM planning processes has been inconsistent. This has created a range of inefficiencies from delaying the finalisation of IWCM strategies and associated council plans to duplicating existing strategic planning documents and missed opportunities to apply for town water infrastructure funding.

The department's published guidance materials (the 2014 and 2019 IWCM Checklists) outline specific procedures for LWUs to undertake, but the department does not consistently adhere to the steps in practice. Examples of requirements stated in the Checklists and our findings about what happens in practice is summarised below:

- The Checklists require that LWUs finalise an IWCM issues paper before starting to develop an IWCM strategy, but in practice this process does not need to be followed and issues papers and strategies can be developed in parallel.
- The Checklists advise LWUs that departmental concurrence is needed on their IWCM planning documents before implementing the IWCM plan or 'scenario', but:
 - in practice, LWUs have received funding from the department for town water infrastructure projects when these documents are in draft or awaiting departmental concurrence
 - when the department has issued concurrence letters, these have contained 'conditions of approval' that LWUs need to action yet the department does not monitor the completion of these conditions, nor does the Checklist outline this aspect of the concurrence process.
- The Checklists indicate a flexible approach may be taken to the applicability of items for LWUs, but sector feedback suggests the department enforces a strict interpretation of the Checklist items, requiring LWUs to submit plans in the Checklist format and structure with evidence of why items may not be applicable.

The department has held regular liaison meetings with LWU sector groups to discuss ongoing policy and program matters, but it has not routinely engaged with LWUs in a way that clarifies the impacts of its new IWCM planning processes, requirements or expectations. While some stakeholders we interviewed reported a general improvement in the department's approach to sector consultation over the last 18 months, many LWUs suggested that a more collaborative relationship was required to practically support the different needs of LWUs in IWCM planning.

The department did not, for example, sufficiently engage LWUs when it updated the IWCM Checklist in 2019 with an additional 106 data requests and did not provide supporting advice to communicate the intent of this update. Feedback from LWUs and JOs indicate the process of IWCM planning has become more costly and resource intensive, with IWCM strategies costing in excess of the department's estimates of \$250,000 and taking at least 12 months to complete.

Opportunities and risks

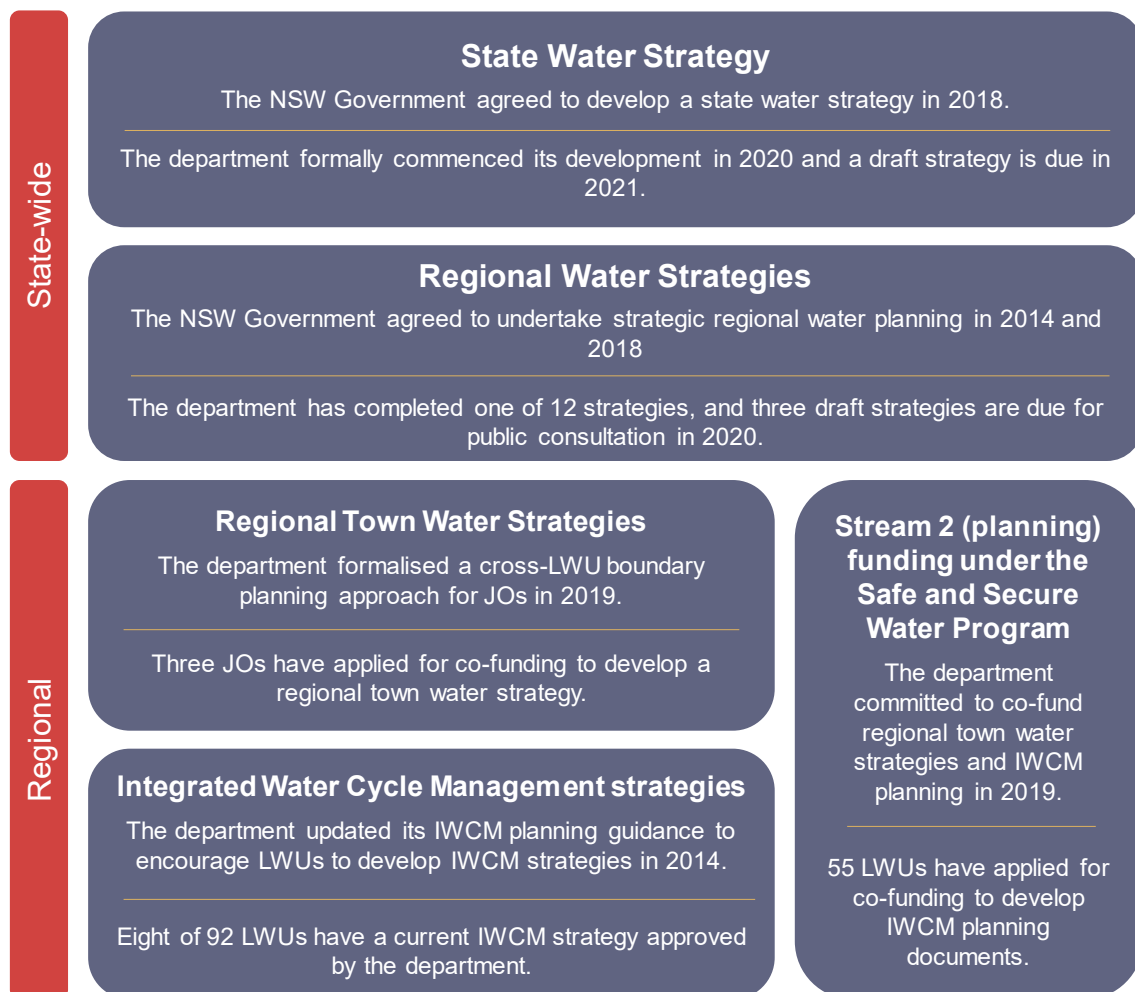
The department has plans to improve its oversight and has developed some new approaches to support town water infrastructure planning

Overall, the department's administration of its guidelines for LWU's IWCM planning has not been managed effectively over the period since 2014. Significant areas of reform were identified in internal reviews of the department's regulation of LWUs in 2015 and 2019, but its response to improve this has been slow.

In 2019, the department developed a plan to consult with the LWU sector on better regulatory approaches, and updated its business planning documents with clearer performance indicators. These are yet to be implemented. A key development has been the department's 2020 update and release of an online LWU performance monitoring data dashboard.

Also, as part of the relaunched Safe and Secure Water Program (SSWPv2) in 2019, the department has allocated up to \$18.5 million to co-fund LWUs to develop or update IWCM strategies in line with the 2019 Checklist requirements, and for JOs to develop regional town water strategies. The LWUs that we interviewed generally considered co-funding to be a good incentive to undertake IWCM planning. The department's data shows that 55 LWUs have applied for IWCM strategy co-funding and about \$2.4 million has been committed to 16 LWUs as of August 2020. Exhibit 7 summarises the current status of the department's activities and supports for strategic water planning which relate to planning for town water infrastructure.

Exhibit 7: Status of the department's activities and support for strategic water planning



Sources: Department of Planning, Industry and Environment data and Audit Office of NSW analysis.

There is room for the department to better coordinate and address risks in its approaches

The efficacy and impact of the department's strategic water planning and town water infrastructure co-funding programs are mutually dependent, and there is room for the department to address coordination issues to realise the full benefits of its regional and town water planning frameworks and investments.

As yet, the department has not developed an implementation plan or risk register to monitor the delivery of its new funding for IWCM strategies or regional town water strategies. There are also implementation risks that the department has not addressed that could limit the efficacy of funding, in particular:

- reported capacity constraints of the consultancy market to procure the relevant services that may delay delivery and limit the value-for-money of IWCM strategies and regional town water strategies, for LWUs, and for the department
- inflexible SSWP funding rules in the application of subsidies to LWUs seeking to jointly procure services to develop an IWCM planning document, which creates planning and funding inefficiencies
- the limited guidance and support provided to JOs to progress regional town water strategy planning, and their readiness to participate.

Additionally, the activities above are not well coordinated with the Regional Water Strategies Program. For example:

- The department's climate risk modelling and water availability (streamflow) data for regional water strategies may not be available to inform newly co-funded IWCM strategies or regional town water strategies. The department advises that it intends to share this data but has not clarified when and is advising LWUs and JOs to use other approaches to this modelling in the interim.¹² This creates a risk that local planning will be out of date or not easily integrated with regional strategies.
- The department has had a limited evidence base of available IWCM strategies on which to draw to inform its list of options for the Regional Water Strategies Program. The delivery and continuous improvements of strategic water planning at the regional level will in part depend on the efficacy of the department's current work to improve its oversight and support to LWUs for their IWCM planning, and JO's regional town water strategies.

¹² Specifically, the approach outlined in the draft 2013 Assuring Water Security guidelines.

3. Targeting regional town water infrastructure funds

We examined whether the department has effectively targeted town water infrastructure funding to policy objectives, with a focus on the design and implementation of the Safe and Secure Water Program (SSWP) since its commencement in 2017. The program's aim was to fund town water infrastructure projects that would deliver health, social and environmental benefits, and support economic growth and productivity. We also assessed the department's capacity to demonstrate the outcomes of the SSWP funding and the contributions of its town water infrastructure investments more broadly. Finally, we identified risks to the effectiveness of the department's work underway since 2018–19, which is intended to enhance its strategic water planning and approach to prioritising investments in reducing town water risks.

3.1 Program design and implementation

Program design

The design of the first Safe and Secure Water Program (SSWPv1) was not well evidenced, creating risks

The design of the first version of the Safe and Secure Water Program (SSWPv1), launched by the department in August 2017, did not address evidence and recommendations about how to prioritise investments towards risks and effectively target town water infrastructure funding. The 15 months over which this program ran represented an opportunity cost in time and resources.

On its launch, the \$1 billion program already included a \$408 million NSW Government commitment for the Broken Hill Water Supply Project (i.e. the Murray to Broken Hill pipeline). Effectively, the SSWPv1 was designed as a \$592 million funding pool for eligible applicants. The department released a summary of the final business case for the project, but we have not seen evidence for the merit of the relative priority of this project in the context of the SSWPv1 eligibility and assessment criteria or process.

The program's design lacked a clear approach to targeting the remaining funds and incorporated project assessment processes that did not adequately account for levels of town water risk and variations in LWU sector capacity to successfully prepare applications.

Exhibit 8 outlines key evidence that was available to the department in 2017: this highlights the need for a prioritised, risk-based approach, as does the broader context of LWU capacity and their operating environment (see 1.2).

Exhibit 8: Snapshot of evidence about effective program responses to town water issues

- The 2015 Audit Office of NSW report of the department's Country Town Water Supply and Sewer Program (CTWSSP) noted the evidence of the need for a future, long-term assistance program that would include prioritised means-tested funding to recipients (primarily LWUs). It also noted that, in cases where priority is high but the LWU may not be able to meet the co-payment, this would entail that the department accept this risk or develop a strategy to address genuine hardship.
- The department's 2016 evaluation of the CTWSSP set out the rationale for ongoing funding primarily in terms of reducing risks to public health, noting that such investments can have economic benefits. Departmental planning documents in 2016 similarly outlined that the 'investment logic' for ensuring safe water and sewer services, with the majority of benefits relating to risk management.
- In 2017, the Productivity Commission Inquiry Report found that funding via the Restart NSW funded Water Security for Regions and the Backlog programs had 'not been provided on the basis of need.' The report also reiterated the 2011 recommendation that, where it is not possible or desirable for a utility to achieve full cost recovery through customer charges in view of social, health or environmental expectations, the State Government should provide explicit Community Service Obligation payments.

Source: Audit Office of NSW analysis.

This evidence was not adequately reflected in the design of the SSWPv1, which created risks to the program's effectiveness during implementation. The department did develop a catchment needs assessment that it advises informed its program planning. It also established an assessment process and selection criteria for SSWPv1 projects. But there were still key shortcomings in the design of the program. These shortcomings and the associated risks are summarised below:

- The application process:
 - required that LWUs have the resources to proactively identify town water risks and develop EOIs for projects, although the evidence was that LWU capacity is highly variable and IWCM strategies were not consistently in place
 - was open on a rolling basis, which could only allow the department to make relative comparisons of projects based on applications received at a point in time, and not enable a strategic approach to investment decisions.
- The project assessment framework:
 - did not include a prioritization approach, although the program documents stated that 'prioritisation tools will support decision making'
 - included assessment criteria for projects at the construction stage which required that a positive economic benefit be demonstrated by applicants, although the measurable economic benefits of projects may be less for LWUs that service small populations and/or are more expensive to deliver in more remote locations
 - required that project applications 'demonstrate alignment with sound strategic planning, such as an IWCM strategy,' but the department provided limited information on what alternative documents could be used in the absence of an IWCM strategy, and how it would determine that sound strategic planning was otherwise demonstrated
 - did not require that LWU applicants had IWCM strategies in place and did not document an assessment of the merits and risks of removing this requirement which had been in place during the CTWSSP.

Departmental officers adopted practices to address some of these program risks. This included providing additional support to LWUs on their EOIs, funding applications and cost-benefit analyses. The department, for example, designed and made available a cost-benefit analysis tool for LWUs to use.

LWUs that were interviewed and received the department's assistance reported that this was valuable, but the department has limited documentation on the nature and scope of assistance provided to LWUs through this process.

This is an issue because of the potential for conflicting duties for officers providing support to LWUs and advising the Technical Review Panel (TRP) on project applications.

To mitigate this, the department reduced the involvement of officers in SSWPv1 project assessments where a potential conflict was identified, and provided guidance to officers and an economic consultant on the panel about how to handle LWUs' requests for advice. In the context of the department's poorly defined regulatory role (see 2.1) and the department's limited documentation, we are not able to conclude whether actual or potential conflicts in duties were managed effectively.

The department did incorporate LWU means testing by way of funding bands¹³ and provisions for additional funding in hardship cases—although the parameters for that assessment were not clearly specified in the SSWPv1 program documents. The department has also advised that a benefit of the applicant-led approach was that it provided an opportunity for LWUs to bring town water issues to the department's attention.

Program implementation

Technical assessments occurred but did not result in a clear approach to targeting the SSWPv1 funds

Most SSWPv1 projects were assessed by the department-led multi-agency Technical Review Panel (TRP) but there were shortcomings in the program's design, combined with limitations in the evidence available to the TRP to apply the 'strategic assessment' criteria. This resulted in funds being broadly distributed across the LWU sector and without clear targeting. The department cannot demonstrate that it facilitated a strategic investment approach through the SSWPv1.

The department's records show that the TRP started operating in August 2017. Interviews with agencies consistently found that the TRP was well regarded for bringing sound technical expertise and knowledge of town water risks and issues to project assessments.

- Of the 226 SSWP records in the database, 201 were assessed by the TRP at the EOI stage and 112 as detailed applications. This means that most (89 per cent) of the potential projects were assessed for eligibility by the TRP.
- Of the 108 SSWP projects with funds committed as of May 2020, 95 had records of an EOI being received and 77 had records of detailed applications being received by the TRP. The department ran some alternative processes for recommending funds, other than the TRP, which account for these gaps in the records. This is outlined in more detail in Exhibit 11.

The strategic assessment criteria required that the TRP consider whether a proposed project aligned with a state or regional strategic planning framework, as well as an infrastructure planning framework (an IWCM strategy, 'or similar'). The TRP did not, however, have adequate access to well-documented strategic planning information to inform its strategic assessments and funding recommendations. Specifically:

- the department did not have regional water strategies in place, nor articulated regional priorities, that might have otherwise provided LWUs and the TRP with a clear, well-defined strategic framework on which to base project assessments
- the department did not provide adequate program guidance on what other strategic planning documentation might be relevant in the absence of an IWCM strategy, and IWCM strategies were generally absent
- analysis of 39 detailed applications found just six cases where a current IWCM strategy was in place to inform the TRP's assessment. Of the 22 detailed applications that were also recommended for funding in this sample, 16 were recommended in the absence of an IWCM strategy. As such, about \$21 million from this sample was offered to LWUs for projects where there was no available or current IWCM strategy to support it or an assessment of its relative priority.

¹³ Specifically, LWUs with an annual revenue of >\$20 million could be eligible for up to 25 per cent of the total project cost funded; LWUs with annual revenue of \$5 million to \$20 million could be eligible for up to 50 per cent funding; and LWUs with revenue <\$5 million could be eligible for up to 70 per cent funding.

The department advises that it considered that IWCM strategies were not always needed for a strategic assessment of 'less complex projects that... had insignificant impact on typical residential bills'. Business rules guiding the department's use of this discretion (e.g. a benchmark for the level of project complexity or the significance of a project's impact on residential bills at which point an IWCM strategy is needed) are not documented.

Our analysis of the distribution of funds allocated to LWUs through SSWPv1 projects did not reveal a clear relationship between the support provided across the sector and LWU capacity to self-fund town water infrastructure. This is consistent with the limitations we found in the program's design and some features of its implementation. According to May 2020 program data, the total number of projects (representing 55 LWUs) were broadly spread across small to major LWUs and the overall value of funds committed favoured larger LWUs and those with stronger financial indicators, as reflected in Exhibit 9.

Exhibit 9: Number and value of SSWP projects compared to key LWU characteristics

LWU characteristics	Number of LWU projects	Value of SSWP funds committed to LWUs as at May 2020
Small LWUs (average ERRR, 0.77)	18	\$32 million
Medium LWUs (average ERRR, 1.41)	40	\$67 million
Big LWUs (average ERRR, 1.81)	21	\$50 million
Major LWUs (average ERRR, 3.00)	27	\$111 million

Notes: LWU 'size' is the number of property connections according to the LWU Performance Monitoring data 2017–18: small (≤ 1,500 properties), medium (≤ 4,000 properties), big (≤ 10,000 properties) and major (>10,000 properties). The economic real rate of return (ERRR) is used by DPIE as an indicator of LWU financial management. Analysis excludes non-LWU projects as there is no LWU size data matching. Funds are rounded to the nearest million.

Sources: Department of Planning, Industry and Environment data and Audit Office of NSW analysis.

This finding which indicates the absence of a clear targeting approach is also consistent with information collated from interviews with 17 LWUs, when combined with data on their SSWPv1 funding. In that sample, there was no clear relationship between the level of LWU risk¹⁴, and the amount of funding recommended through the program. Only one LWU in that sample had a current, approved IWCM strategy (see Exhibit 6).

¹⁴ In this analysis, LWU risk was a composite measure of the department's ranking of 'high need' LWU and those that had one or more 'level 5' (highest) risk rating according to the department's Prioritisation Framework.

Around half of all SSWP projects were town water infrastructure planning studies

The SSWP supported town water infrastructure planning studies as well as construction projects. About half of the proposed projects were for infrastructure planning, including scoping studies and business cases, as shown in Exhibit 10. This relates to 40 of a total of 55 LWU applicants. Town water infrastructure involves complex technical and strategic planning. The limited effectiveness of the department's support to encourage LWUs to adopt IWCM planning since 2014 (see 2.2) may explain the distribution of applications to planning studies, given LWUs generally did not have projects ready for construction.

Exhibit 10: Summary of SSWP projects by application type

Project application type	Proposed projects 2017–18	Assessed projects 2017–2019	Projects with an active funding deed as at May 2020
Scoping studies	69	43	23
Business cases	32	18	17
Other planning*	8	2	6
Sub-total (planning types)	109	63	46
Design and construction	105	49	21
Total	214	112	67

* Other planning' refers to other types in the data: concept study, options study, and detailed design and tender.

Source: Department of Planning, Industry and Environment data.




The department intends that the IWCM planning process should facilitate a strategic and evidence-based approach to LWUs' town water infrastructure planning, including by ensuring that issues papers and other analyses are complete. Only eight of 92 LWUs have a current, complete IWCM strategy (see 2.2). There were investment risks associated with the department recommending funding for planning studies in the context of an infrastructure program, if the LWU had not already done sound IWCM planning to ensure full and strategic consideration of infrastructure and non-infrastructure options.

Around a third of funded SSWP projects were not assessed transparently or consistent with good practice grants administration

The department did not apply consistent or well-documented processes to assess and recommend about a third of projects for funding under the SSWP. This occurred around the time that the SSWPv1 was launched and in the transition period to the SSWPv2, and was often associated with the fast-tracking of announcements. The department stated that the program would be implemented in accordance with the NSW Department of Premier and Cabinet (DPC) Good Practice Guide to Grants Administration, but did not consistently do so.

Exhibit 11 summarises information about the funds committed to projects that the department recommended via the advertised SSWPv1 process ('TRP rounds') and those recommended via alternative processes (the six initial and 33 transitional projects). The department's alternative processes involved a broad consideration of the rationale for projects in view of town water risks, but applied various assessment approaches which were not consistently documented or clearly communicated to the sector. This has reduced transparency around the evidence that the department used to recommend these 39 projects (36 per cent of 108 projects that have funding committed).

Exhibit 11: Summary of the SSWP program data funds committed for projects recommended for funding via TRP rounds and alternative process

Program funding process	Were projects assessed in accordance with the advertised assessment process?	Projects with SSWP funds committed as at May 2020	Value of SSWP funds committed as of May 2020
Initial projects, 2017	 See Exhibit 12	6	\$30 million
TRP rounds, 2017-19	TRP assessments occurred but with gaps in scoring information and limited capacity to assess strategically.	69 [^]	\$113 million
Transitional projects, 2018-19	 See Exhibit 13	33	\$133 million
Total	--	108	\$276 million
Key	 Processes lacking in transparency and consistency		

[^] The 69 projects here is less than the 77 projects referred to in section 3.1, which includes projects that had a TRP assessment at some point, although it was through an alternative funding recommendation process that funds were committed. Funds are rounded to the nearest million. Sources: Department of Planning, Industry and Environment data and Audit Office of NSW analysis.

Out of the 39 initial and transitional projects shown in Exhibit 11, records show that eight projects (total value of about \$56 million) did have a detailed application that had been previously assessed by the TRP. But, another eight projects totalling about \$64 million had funding committed but incomplete TRP assessment data. The remainder had no consistent records of detailed applications being assessed. In total, about \$107 million (31 projects) was committed via alternative processes and had incomplete or inconsistent information about the detailed project assessments leading to funding recommendations, limiting the department's ability to demonstrate how effectively funds were targeted across the program.

Exhibit 12 illustrates how the department's assessment of and recommendations for the initial projects in 2017 was not well documented, and that some have progressed slowly to construction. This is notable because these projects were recommended for funding because they were considered to be 'shovel-ready' i.e. able to commence quickly following their announcement.

Exhibit 12: The 'initial projects' process in 2017

Identification

- In February 2017, the department led a multi-agency workshop with an expert to identify 'shovel-ready' projects from a pool of 17 projects in areas of town water risk*. These were to be announced for the launch of the SSWPv1. Nine projects (relating to nine LWUs) were identified from this workshop, which the department's internal documents stated as being 'most aligned to the SSWP criteria'.

Approval

- In July 2017, the department wrote to Infrastructure NSW seeking review and consideration of eight projects (relating to eight LWUs) to be funded to launch the SSWPv1. Three projects from the workshop were removed in this recommendation, and two different projects were added. The department advises that the three projects were removed from the initial recommendation after it was identified that these were either projects primarily for economic growth (rather than primarily for addressing town water risks) or were not ready to progress to construction.
- Among the eight LWUs to which the recommended projects referred, there were no current, approved IWCM planning documents, although some draft documents were in place.
One of the projects that the department added at the recommendation stage was noted to have a 'significant asset replacement component,' as did two other projects already on the list. The SSWPv1 guidelines allowed for asset replacement funding in exceptional cases where the LWU could demonstrate that this could not have been reasonably provided for. This did not happen.
- The department announced via media release that these eight projects were 'shortlisted as part of the 2017–18 budget announcement'.
- In October 2017, six of the department's eight recommended projects were approved for funding.

Outcome (as at early 2020)

- Of the approximately \$30 million allocated to the six recommended projects, about \$9 million of government funds have been expended.
- Three of the six projects that the department had recommended as 'shovel ready' in early 2017 are at or near completion. The other three have not commenced i.e. no funds expended.

* This involved testing a catchment needs assessment framework, which the department had engaged an expert to develop with the intention of using it during the implementation of the SSWPv1.

Sources: Department of Planning, Industry and Environment documents and Audit Office of NSW analysis.

The department's approach to assessing projects in the transitional period from the SSWPv1 to its re-design as the SSWPv2 in 2019, also lacked transparency and was not always consistent with good practice grants administration (Exhibit 13). The remaining SSWP funds had been transferred from Restart NSW to the Consolidated Fund and the department became responsible for funds administration as well as program implementation.

Exhibit 13: Three different transitional project assessment processes in 2019

1. The department recommended and approved seven projects for SSWP funding, with an estimated total cost at the time of \$72 million.
 - Notes accompanying the recommendation provided some rationale for the projects insofar as these relate to town water security or quality issues, but no clear evidence of what process or assessment criteria were used.
 - Records also show that officers noted that one project valued at \$6.9 million did not align with the SSWP eligibility criteria, and another project valued at \$10 million was approved for 100 per cent subsidy, although it was not considered to be eligible for a full subsidy. The department has not provided evidence as to whether these issues were resolved prior to approving the funding.
2. The department recommended another 23 projects for SSWP funding, representing a commitment of about \$43 million, after convening an expert panel to apply a combination of seven 'guiding principles', the SSWPv1 program criteria, and the draft SSWPv2 prioritisation framework.
 - It was recorded that these were 'no regrets' projects and election commitments. There are limited records of these deliberations, but the various principles and criteria applied did not establish a rigorous, well-defined, internally consistent or transparent assessment framework: for example, the approach involved criteria that prioritised risks but also aimed to achieve an even spread across the State and an even mix of project types and sizes.
3. The department separately approved another two SSWP projects, each valued at \$5 million, that were recorded as drought emergency measures.
 - There is some provision in the SSWPv2 Prioritisation Framework that additional emergency funding may be sourced from the SSWP for activities that provide temporary and immediate water, but few records and explanatory notes document these decisions.

Sources: Department of Planning, Industry and Environment documents and Audit Office of NSW analysis.

The SSWPv2 establishes a clear approach to targeting funds

In October 2018, the department launched a re-designed program, the SSWPv2. The transition to the SSWPv2 involved transferring the balance of unallocated SSWPv1 funds (about \$532 million) from the Restart NSW fund to the Consolidated Fund. The program re-design also involved:

- shifting program fund administration from Infrastructure NSW to the department
- shifting the program approach from an applicant-driven to priority-based process, and removing the mandatory criteria on projects to have a positive benefit cost ratio
- establishing a program management office with additional resourcing to provide technical and strategic assistance to LWUs.

The re-designed program addressed some of the design weaknesses and implementation risks associated with the applicant-led approach under the SSWPv1. Features of the SSWPv2 program also reflect some recommendations from a SSWPv1 program review commissioned by the department in 2018, such as clarifying program outcomes and objectives, and enhancing assessment methods and definitions.

Exhibit 14: Assessment of key SSWPv2 (stream 1 and 2) design features

Program design features	Potential impact on implementation risk
Program objective	
Program guidelines clearly state that the program is designed to address key risks to town water security, quality and environmental impacts, and defines this terminology.	Improves transparency, clarity and reduced risk that funding is not targeted as intended.
Program stream 1 – Funding for the resolution of priority (highest risk) town water security	
A Prioritisation Framework for centrally identifying and maintaining a list of eligible town water risks and issues (ERIL), which includes socio-economic disadvantage and remoteness to target need.	Removes applicant-led and multi-stage approach, and the risk that high-need LWUs do not apply for funding.
An ERIL Review Panel chaired by the department with representation from the OLG, NSW Health, DPC, EPA, NSW Treasury and Infrastructure NSW.	Reduces some risk that co-funding is not well-targeted to program and policy objectives.
Process for the department to invite LWUs to submit a project proposal, which can include non-infrastructure solutions, to address priority risks from the ERIL.	Reduces risk of poor investments by funding LWU capability building to plan these and consider non-infrastructure options.
Program stream 2 – Funding for strategic town water infrastructure planning	
The allocation of funding for LWUs to undertake IWCM planning and produce an IWCM strategy, and related strategic business planning. Also, for JOs to develop regional town water strategies.	Reduces some cost barriers to LWU's planning and may contribute to the department's evidence-base of town water risks and issues.

Sources: Department of Planning, Industry and Environment documents and Audit Office of NSW analysis.

The department developed documents to support the SSWPv2. These include a program management framework with a process for grants management, a prioritisation framework, review panel terms of reference, a risk management framework, project assurance framework, and stakeholder engagement strategy. The department also commissioned an internal compliance audit of the SSWPv2 program documents and controls in July 2019, which found these to be 'effective'. At the time, that audit could not comment on the implementation of these procedures as the SSWPv2 was yet to fully commence.

We note that in April 2020 the department advised LWUs of the town water risks identified in their areas, and that the program budget is not sufficient to co-fund the resolution of all of the highest risks. Rather, funding will be prioritised further based on the socio-economic profile of the community. This is an update to the approach outlined in the 2019 SSWPv2 program management framework, which intended to allocate funds to the highest priority risks over the life of the program or until funds are exhausted.

The department's implementation of the SSWPv2 has been delayed by a year, and funding for priority projects has not commenced

The department established a plan for the implementation of the SSWPv2 but this was delayed by about a year. The plan involved transitioning existing SSWPv1 applications that were part-way through the assessment process to SSWPv2, engaging with the LWU sector to confirm risks and issues, and announcing projects from the priority list of town water risks from May 2019. But formal LWU sector engagement on these risks started in April 2020 rather than April 2019. As shown in Exhibit 15, as of August 2020, no projects had been announced for funding, or commenced, under the new prioritisation approach.

Exhibit 15: The department's intended vs actual timeframes for the SSWPv2 transition

Activity	Plan	Actual timing
Launch SSWPv2	October 2018	✓
Assess transitional projects	November 2018 to April 2019	✓
Announce transitional projects	Early 2019 to June 2019	✓
Develop priority list (ERIL)	By February 2019	! <p>The Priority Framework for ERIL was finalised in April 2019 and approved in September 2019.</p>
Liaise with the sector including LWUs to refine the priority list	By April 2019	! <p>April 2020</p>
Announce projects from priority list	From May 2019	! <p>Not commenced as of August 2020</p>

Sources: Department of Planning, Industry and Environment documents and Audit Office of NSW analysis.

In launching the SSWPv2 in October 2018, the department did deliver presentations to the LWU sector and JOs and provided factsheets that outlined an 'extended transition period' for accepting SSWPv1 project applications. It also emailed LWUs about the revised guidelines in December 2018. However, interviews with LWUs and sector groups reported that, in 2020, they remained unsure about the department's timeframes and processes for the implementation of the SSWPv2. Some LWUs that had SSWPv1 applications underway advised they were also unsure about the status of their application or whether to seek alternative co-funding sources.

The transition to the SSWPv2 occurred during a time of intense drought across regional NSW, involving departmental responses, such as funding for drought infrastructure projects and town water carting, as well as LWUs' emergency responses.

3.2 Reducing barriers and improving outcomes

The department does not have robust systems for integrated project monitoring and program evaluation

The various aims of town water infrastructure funding programs have been broadly aligned with the department's policy objectives to promote safe, secure and sustainable water (see Exhibit 2, 1.4). The department's systems for monitoring and evaluating the impacts of these programs and the contributions of State Government investments towards these outcomes are however lacking.

The department did not have a documented plan in 2017, at the start of the SSWPv1, for evaluating the program. The NSW Government Program Evaluation Guidelines state that building evaluation plans and methods into program design is best practice. The 2015 Audit Office of NSW report on the CTWSSP recommended that similar assistance programs be evaluated in the future.

The department did however commission a review of the SSWPv1 procedures and processes in 2018, which produced recommendations largely consistent with how the department re-designed the program. The department also outlined a monitoring and evaluation approach for the SSWPv2, as part of the overall program management framework in January 2019.

Exhibit 16: Key commitments in the department's monitoring and evaluation approach for the SSWPv2

The SSWPv2 program management framework sets out key performance indicators for the department's processes, commits to a continuous quality improvement approach that includes stakeholder input, and identifies how benefits could be measured against targets. It includes a target for 100 per cent of LWUs to have a current IWCM strategy, and for reducing the number of water supply systems with water quality and security risks. It also outlines how the program should be assessed from an investment perspective, i.e. through its contribution towards the State Government outcome of 'safe, secure and sustainable water and wastewater services to regional NSW towns.'

Source: Audit Office of NSW analysis.

Although the department's approaches for monitoring and evaluating the SSWPv2 have been outlined, this planning is incomplete and lacking in detail. For example, baseline data sources and timeframes for measuring some indicators are not identified. The department's monitoring and evaluation planning is also not fully resourced for implementation. The department has advised that, within existing program resources and as part of the project assurance process, it has established a framework for LWU's project finalisation reports to include information on town water risk reductions, and for the list of eligible town water risks and issues to be updated with this information. The department also advises that this work will start once funding to resolve town water risks (stream 1) commences. The SSWPv2 has been listed as a departmental program that will require evaluation.

The department was to review its monitoring and evaluation approach on an annual basis starting in January 2020, but this has not yet been done. Accordingly, it does not reflect recent developments in the department's activities to support and fund town water infrastructure, such as a clear process for monitoring and measuring the outcomes of:

- SSWPv1 projects and integrating this with information about the status of town water issues and risks in SSWPv2
- SSWPv2 funding for regional town water strategies (stream 2)
- cross-LWU boundary and catchment-scale issues that are identified through the SSWPv2 prioritisation process.

This means that the department has not established systems to combine data from various sources to understand and report on the degree of contribution of SSWPv2 investments towards state outcomes: this would involve combining information about the status of SSWPv1 projects and other town water infrastructure co-funding programs, with data on town water risks/issues and LWU performance. These systems will need to be addressed so that the department can robustly and transparently demonstrate the outcomes of its co-funding and the contribution of its investments to reducing town water risks and issues.

The department has not addressed timing, coordination and sector engagement risks to the integration of strategic water planning and supports for town water infrastructure

The department has a number of activities underway related to water resource management and town water security. Since 2018–19, this has included new planning approaches and funding mechanisms for identifying and addressing issues relevant to LWU's planning and town water infrastructure options. There are signs that elements of these activities are not strongly coordinated and that the sequencing of activities may be sub-optimal, limiting their effectiveness.

In 2019 the department has, for example, articulated a clear commitment to stakeholder engagement in its delivery of its new programs and planning approaches. In the Regional Water Strategies Program, the department states it is adopting a 'partnership' approach to the development of strategies with local communities, including LWUs. Similarly, the department has committed to partner with LWUs to co-fund the resolution of town water risks under the SSWP. While the department has identified stakeholder support as critical to achieving its outcomes, around mid-2020 we identified emerging risks.

These include:

- timelines for developing regional water strategies not enabling meaningful stakeholder engagement with LWUs, including those part of JOs and utility alliances, who have also commented that the 'rushed time frames' have not been 'conducive to genuine engagement'
- the department not consistently engaging with the relevant subject matter experts (that is, LWU managers) for its Regional Water Strategies Program consultations. Some LWUs situated across catchment boundaries have also expressed concern that they are not being involved in all relevant strategies
- the department not consulting LWUs before the delayed release of its prioritised list of town water risks and issues for the SSWPv2. The list requires LWU agreement prior to confirming risks for co-funding and resolution, and some LWUs have indicated they will be challenging the department's assessment of town water risks and additional time may be needed to engage and confirm responses.

The department states the regional water strategies will be adaptive and regularly reviewed to remain effective and relevant. It also advises it will continually update the prioritised list of issues and risks in the SSWPv2 and refer relevant cross-LWU boundary matters to the Regional Water Strategies Program. But the department has not articulated a clear approach for ensuring the ongoing integration of town water issues over the lifecycle of its regional water strategies.

There is also no clear funding pathway to resolve cross-LWU boundary or catchment-scale risks with the cessation of funding for these projects under SSWPv2, even though these may be identified through regional town water strategies co-funded by the department. As a result, there may be delays in the resolution of high-priority town water risks that are transitioned to the Regional Water Strategies Program.

Section two

Appendices

Appendix one – Response from agency



Our ref: BN20/4808
Your ref: D2016148/PA6660

Ms Margaret Crawford
Auditor-General for New South Wales
Audit Office of New South Wales
GPO Box 12
SYDNEY NSW 2001

Dear Ms ^{Margaret}~~Crawford~~

Performance audit – Support for regional town water infrastructure

Thank you for your correspondence regarding the final report for the performance audit on the support provided by the Department for regional town water infrastructure.

The Department of Planning, Industry and Environment (the Department) acknowledges that a greater emphasis on strategic planning for town water supplies is needed and supports the audit recommendations. It agrees with the report's findings that there are opportunities to improve oversight of and support for councils' strategic urban water service planning, including planning for town water supply infrastructure.

Safe, secure and sustainable water supply and sewerage services provided by council local water utilities in an efficient and customer focussed manner are essential for community wellbeing and the provision of social and economic opportunities in regional NSW towns.

Since the formation of the Department and the recruitment of a CEO for the NSW Water Sector, the Department has made considerable progress towards building a long-term strategic planning framework of water management, reform and investment. As the audit recommends, this will ensure the Department has in place a strategic planning framework that integrates and aligns local, regional and state priorities and supports councils' strategic service and infrastructure planning for town water supplies in regional NSW.

The Department has commenced work on a State Water Strategy to outline the NSW Government's long-term vision and performance expectations for the sector. This first 20-year State Water Strategy will be part of a long-term strategic planning framework of water reform and investment that:

- recognises water as a finite resource, essential for life and economic prosperity;
- will put water on the same footing as other key state resources and services; and
- identifies water infrastructure as catalytic for place-making, in the same way as transport.

The State Water Strategy will reflect the purpose of the NSW Water Management Act (2000) and set the over-arching objectives, actions and strategic outcomes for the state's water resources and the water sector for the next 20 years. It will be underpinned by 12 regional water strategies, and two metropolitan strategies - the Greater Sydney Water Strategy and the Lower Hunter Water Security Plan. Together, these strategies will make up the Water Strategy Program and the strategic planning framework for water management in NSW.

The State Water Strategy will reflect the recommendations of the audit report and identify outcomes and actions to support their achievement.

Public exhibition of the State Water Strategy is scheduled for early 2021; the Greater Sydney Water Strategy is to be released for public consultation by mid-2021, and the Lower Hunter Water Security Plan by the end of 2021. The 12 regional water strategies are being progressively developed, with all strategies to be published by the end of 2021.

Regional water strategies will set out a long-term 'roadmap' of actions in their areas to deliver five objectives:

- deliver and manage water for local communities;
- enable economic prosperity;
- recognise and protect Aboriginal cultural values and rights;
- protect and enhance the environment; and
- affordability - identify least cost policy and infrastructure options.

Councils are being involved in the development of the regional water strategies and the consideration of options, including infrastructure options to address water security, quality and environmental risks and priorities.

The Department will continue to work with councils to ensure their strategic service planning for town water supplies and the Department's regional water strategies can fully leverage each other, including by:

- facilitating coordinated risk and options analysis across councils' strategic service planning and regional water strategies to ensure strategies inform each other and efficiently align solutions to town water risks;
- encouraging and supporting the development of regional town water strategies led by Joint Organisations of Councils;
- where possible and suitable, for sensitivity analysis and stress testing, providing access to the climate and water data and modelling outputs of the regional water strategies; and
- developing a best-practice approach to modelling climate impacts on water security and incorporate this approach across departmental planning and councils strategic urban water service planning.

The Department will continue to work with the local government sector and other regulators on ways to improve and support councils' ability to manage strategic urban water priorities and risks and reduce existing risks to tolerable levels.

Despite its limited legislative and regulatory authority, the Department developed and has been implementing its predominantly voluntary, best practice water supply and sewerage management framework under section 409 of the *Local Government Act (NSW) 1993*. This framework constitutes a holistic system for the support and oversight of strategic service planning, pricing, performance reporting and technical considerations.

Effectiveness of this framework could be improved by providing the Department with greater authority to set best practice management policies and enforce their requirements. Importantly, the Department recognises that a critical part of addressing effectiveness will be about improving how the Department regulates, supports and engages with council local water utilities.

The Department is progressing improvements to its internal processes and data management and monitoring systems, especially with respect to its oversight of local water utility strategic service planning and risk management.

The Department is also considering broader improvements to its oversight and support functions, including:

- reviewing and making the regulatory framework for local water utility strategic urban water service planning and risk management more effective, proportionate, transparent, and accountable;

- improving engagement and formalising consultative arrangements with the sector and among regulators to address uncertainties and improve collaboration;
- enhancing the Department's local water utility performance, risk and maturity monitoring to inform proportionate regulation and support activities that help build a better performance culture;
- working with the sector to identify critical skills shortages in the sector and co-designing options to address these;
- facilitating greater support for councils to obtain value-for-money strategic planning services, including through enabling joint or regional approaches and partnerships across utilities and agencies; and
- continuing to improve coordination between local water utility strategic service planning and the NSW Government's regional water strategies to ensure strategies inform each other and align solutions to town water risks.

Further, the Department will continue to implement the Safe and Secure Water Program. This program provides co-funding to councils to address water security, water quality and environmental impact risks in urban water systems across regional NSW.

To improve the Department's ability to identify risks and target funding to solutions to the highest priority risks, in October 2018, the Department re-designed the Safe and Secure Water Program. This re-design transitioned the program from an application-based program to a program based on comprehensive and systematic risk identification, prioritisation and monitoring. The Department assesses and prioritises all risks in urban water systems in regional NSW and, starting with the highest priority risks, works with councils to identify the best solution to address the risk and provides co-funding to implement the solution.

In addition, to further improve risk identification and targeting of government support, the Department established a funding stream that provides co-funding for the development of local water utility strategic service plans as well as where Joint Organisations of Councils lead the development of regional town water strategies. This will improve councils' strategic risk management and inform the identification of high priority risks and their solutions, including in a regional context.

The roll-out of the re-designed program from April 2019 has been constrained as a result of the NSW Government's focus on the emergency response to one of the worst droughts on record; assisting councils with avoiding acute water supply failure by committing over \$275 million to critical water infrastructure projects and town water carting for regional NSW. The infrastructure delivered during the drought is likely to mean that in several town water systems risk-based funding from the Safe and Secure Water Program will not be required. Despite this constraint, the Safe and Secure Water Program is providing funding for the development of 17 council strategic service plans, with a further 39 funding requests under assessment.

The Department has been working with local water utilities and key stakeholders to address the issues raised in the audit report.

If you have any questions, please contact Mr Jim Betts, CEO of the NSW Water Sector on 0448 762 851.

Yours sincerely

Jim Betts

Jim Betts

Secretary

15/9/2020

Once again, I'd like to record my appreciation for the professionalism of Audit Office staff, and note the strong alignment between your office's recommendations and the reform directions BWE wishes to pursue.

Appendix two – Key terms

Key term in the report	Description
Best Practice Management (BPM) Guidelines	The Best Practice Management of Water Supply and Sewerage Guidelines Guidelines first produced by the NSW Government in 2004, updated in 2007 and gazetted under the New South Wales' <i>Local Government Act 1993</i> . The Minister for Local Government has concurred with the BPM Guidelines.
Integrated Water Cycle Management (IWCM) planning guidance	Guidance produced by the department to inform LWUs' planning This guidance accords with the IWCM section of the Best Practice Guidelines. Since 2014, the department's key requirements are presented in the form of the IWCM Checklist. This checklist connects IWCM planning to guidance on strategic business planning. Planning by LWUs that reflects this guidance is assessed by the department as 'sound'.
Integrated Water Cycle Management (IWCM) planning documents	Documents produced by LWUs in accordance with IWCM guidance IWCM issues paper, IWCM strategy, and a Strategic Business Plan. The department intends that these IWCM planning documents inform a sound, strategic approach to LWUs' town water infrastructure planning.
Local Water Utilities (LWUs)	Water and/or sewer service providers in regional NSW cities and towns There are 92 LWUs in NSW, 89 are operated by councils under the New South Wales' <i>Local Government Act 1993</i> , and the remainder are operated by authorities under New South Wales' <i>Water Management Act 2000</i> . LWUs are regulated by the department.
Regional town water strategies	Planning to facilitate town water security across LWU boundaries The department developed guidance in 2019 for Joint Organisations of Councils (JOs) to undertake this planning.
Regional water strategies	Planning to set objectives and coordinate priorities for water resource management across regional NSW catchments Department-led planning that considers a range of water uses and users: town water is one element.
Town water	Water for consumptive use in regional NSW cities and towns
Town water infrastructure	Infrastructure that provides water supply and/or sewer services in regional NSW cities and towns
Town water infrastructure funding programs	Programs managed by the department that provide funding for town water infrastructure This is usually provided as co-funding grants, and can include funds for infrastructure scoping and planning, and construction. LWUs are the core applicant group.
Town water infrastructure planning	Planning for the provision of infrastructure for town water and/or sewer services LWUs and JOs may undertake this planning in various forms. It can include project-specific planning (e.g. scoping studies or business cases) and planning that considers non-infrastructure solutions. When done by LWUs, the department expects the town water infrastructure plans should have strategic alignment with the IWCM planning documents.
Town water security	A safe and reliable supply of town water.

Appendix three – About the audit

Audit objective

This audit assessed the effectiveness the Department of Planning, Industry and Environment's support for planning and funding town water infrastructure in regional NSW towns and cities.

Audit criteria

We addressed the audit objective by assessing whether the department has:

- effectively overseen and facilitated Local Water Utilities' (LWUs') planning for town water infrastructure
- had an effective framework for assessing town water infrastructure issues to inform state and regional water planning
- effectively targeted town water infrastructure to its policy objectives.

Audit scope and focus

In assessing the criteria, we focused on activities since 2014 and checked the following aspects:

- The department's oversight and support to LWUs for their strategic town water planning, via its administration of the Integrated Water Cycle Management (IWCM) planning guidance, which is part of the Best Practice Management of Water Supply and Sewerage Guidelines. Specifically, we checked whether the department:
 - effectively assisted LWUs to develop sound IWCM strategies
 - effectively reviews and approves IWCM strategies using clear processes and a governance framework
 - has robust monitoring and evaluation that continuously improves these processes.
- The department's plans, activities and progress to develop integrated approaches to local, regional and state water planning, particularly via the Regional Water Strategies Program and insofar as these activities relate to town water infrastructure planning. Specifically, we checked whether the department had:
 - defined objectives for this strategic water planning, with aligned priorities, at local, regional and state-wide levels
 - clear plans to engage local stakeholders on town water infrastructure issues when developing state and regional water strategies
 - identified issues in IWCM strategies to inform state and regional water strategies.
- The department's role in the design and implementation of town water infrastructure funding programs, with a focus on the Safe and Secure Water Program (SSWP) i.e. program approaches to targeting funds in the first version (SSWPv1), and in stream 1 and stream 2 of the re-designed version (SSWPv2). Specifically, we checked whether the department had:
 - designed the program to align to its policy objectives
 - addressed barriers to effectively targeting funds
 - targeted funds as intended.

Audit exclusions

The audit did not conduct a statutory review of the department's regulatory arrangements for the LWU sector, and did not assess the effectiveness of the department's operational and technical advice to LWUs across all aspects of their businesses (other than for IWCM planning and the related strategic business planning activities). The audit did comment on these matters where they affected our findings or for context.

Audit approach

Our procedures included:

1. Interviewing officers and other staff from:
 - the department's Water Group, including the Water Utilities and Regional Water Strategy teams and the Chief Water Strategy Officer
 - other departmental areas and cluster entities, including the Office of Local Government (OLG), the Natural Resources Access Regulator (NRAR), the NSW Environment Protection Authority (EPA), the Regional Town Water Coordinator, the Natural Resource Commission (NRC), and Water NSW
 - other state government entities including Infrastructure NSW, NSW Health, Regional NSW (including Public Works Advisory), NSW Treasury and the Office of the Productivity Commissioner
 - the Independent Pricing and Regulatory Tribunal
 - Local Water Utilities (including local council and non-council operated utilities)
 - Seventeen LWUs were selected via a stratified random sampling approach to ensure coverage across all 12 departmental planning regions, and a mix of LWU sizes and types.
 - Industry and sector groups, including the Water Directorate and Local Government NSW
 - the Australian Government Productivity Commission
 - University-based experts in water resource management.
2. Examining and analysing:
 - legislation, policy, program documents and reports related to the department's regulatory role, activities, and priorities for supporting and funding regional town water infrastructure, and its oversight approach and support to LWUs
 - processes and procedures relevant to the administration of the IWCM element of the BPM Guidelines, and LWU sector engagement activities
 - administrative data about the review process and status of IWCM planning documents, and information about IWCM planning in the department's LWU Performance Monitoring and Benchmarking reports
 - plans, status updates and risk registers related to regional and state water planning, evidence of LWU sector engagement and IWCM strategies informing regional water strategies, current versions of draft regional water strategies, and minutes from relevant meetings
 - policy and program documents related to the design, implementation, monitoring and reporting on the department's town water infrastructure co-funding programs (including the SSWP), and partner programs with Infrastructure NSW
 - administrative data on town water infrastructure co-funding, including SSWP application data (n=226). Additional sampling of the completeness of project assessment data for 40 per cent of SSWP detailed applications across four TRP meetings; and records of all projects recommended through alternative processes
 - submissions from LWU sector groups including the Water Directorate, Local Government NSW, Joint Organisations of Councils and water utility alliances
 - reports from inquiries, reviews and previous performance audits relevant to regional town water management and LWU sector regulation in NSW.

The audit approach also involved developing an in-depth IWCM process study combining qualitative information from LWU interviews and submissions with the department's records.

We engaged an expert in water resource management and IWCM planning to provide technical advice on the audit procedures.

The audit approach was complemented by quality assurance processes within the Audit Office to ensure compliance with professional standards.

Audit methodology

Our performance audit methodology is designed to satisfy Australian Audit Standard ASAE 3500 Performance Engagements and other professional standards. The standards require the audit team to comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance and draw a conclusion on the audit objective. Our processes have also been designed to comply with requirements specified in the *Public Finance and Audit Act 1983* and the *Local Government Act 1993*.

Acknowledgements

We gratefully acknowledge the co-operation and assistance provided by the Department of Planning, Industry and Environment, other Local, State and Australian Government agencies, and water utility sector groups.

Audit cost

The estimated total cost of this audit is \$520,000.

Appendix four – Performance auditing

What are performance audits?

Performance audits determine whether state or local government entities carry out their activities effectively, and do so economically and efficiently and in compliance with all relevant laws.

The activities examined by a performance audit may include a government program, all or part of an audited entity, or more than one entity. They can also consider particular issues which affect the whole public sector and/or the whole local government sector. They cannot question the merits of government policy objectives.

The Auditor-General's mandate to undertake performance audits is set out in section 38B of the *Public Finance and Audit Act 1983* for state government entities, and in section 421D of the *Local Government Act 1993* for local government entities.

Why do we conduct performance audits?

Performance audits provide independent assurance to the NSW Parliament and the public.

Through their recommendations, performance audits seek to improve the value for money the community receives from government services.

Performance audits are selected at the discretion of the Auditor-General who seeks input from parliamentarians, State and local government entities, other interested stakeholders and Audit Office research.

How are performance audits selected?

When selecting and scoping topics, we aim to choose topics that reflect the interests of parliament in holding the government to account. Performance audits are selected at the discretion of the Auditor-General based on our own research, suggestions from the public, and consultation with parliamentarians, agency heads and key government stakeholders. Our three-year performance audit program is published on the website and is reviewed annually to ensure it continues to address significant issues of interest to parliament, aligns with government priorities, and reflects contemporary thinking on public sector management. Our program is sufficiently flexible to allow us to respond readily to any emerging issues.

What happens during the phases of a performance audit?

Performance audits have three key phases: planning, fieldwork and report writing.

During the planning phase, the audit team develops an understanding of the audit topic and responsible entities and defines the objective and scope of the audit.

The planning phase also identifies the audit criteria. These are standards of performance against which the audited entity, program or activities are assessed. Criteria may be based on relevant legislation, internal policies and procedures, industry standards, best practice, government targets, benchmarks or published guidelines.

At the completion of fieldwork, the audit team meets with management representatives to discuss all significant matters arising out of the audit. Following this, a draft performance audit report is prepared.

The audit team then meets with management representatives to check that facts presented in the draft report are accurate and to seek input in developing practical recommendations on areas of improvement.

A final report is then provided to the head of the audited entity who is invited to formally respond to the report. The report presented to the NSW Parliament includes any response from the head of the audited entity. The relevant minister and the Treasurer are also provided with a copy of the final report. In performance audits that involve multiple entities, there may be responses from more than one audited entity or from a nominated coordinating entity.

Who checks to see if recommendations have been implemented?

After the report is presented to the NSW Parliament, it is usual for the entity's audit committee to monitor progress with the implementation of recommendations.

In addition, it is the practice of Parliament's Public Accounts Committee to conduct reviews or hold inquiries into matters raised in performance audit reports. The reviews and inquiries are usually held 12 months after the report received by the NSW Parliament. These reports are available on the NSW Parliament website.

Who audits the auditors?

Our performance audits are subject to internal and external quality reviews against relevant Australian and international standards.

The Public Accounts Committee appoints an independent reviewer to report on compliance with auditing practices and standards every four years. The reviewer's report is presented to the NSW Parliament and available on its website.

Periodic peer reviews by other Audit Offices test our activities against relevant standards and better practice.

Each audit is subject to internal review prior to its release.

Who pays for performance audits?

No fee is charged for performance audits. Our performance audit services are funded by the NSW Parliament.

Further information and copies of reports

For further information, including copies of performance audit reports and a list of audits currently in-progress, please see our website www.audit.nsw.gov.au or contact us on 9275 7100.

OUR VISION

Our insights inform and challenge government to improve outcomes for citizens.

OUR PURPOSE

To help parliament hold government accountable for its use of public resources.

OUR VALUES

Pride in purpose
Curious and open-minded
Valuing people
Contagious integrity
Courage (even when it's uncomfortable)

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