

## **Energy Probe Research Foundation's Recommendations for Public Hearing No. 1: Guiding Principles and the Role of Government**

### **Guiding Principles**

Incentives matter. It is essential to create institutions and rules that encourage responsible parties to work for public health, environmental sustainability, and economic efficiency. The costs and benefits of behaviours should be internalized: Pressure to perform well should come from within rather than from without. Conflicts of interest should be eliminated through structural solutions.

Please see *Energy Probe Research Foundation's Principles*, attached, for an explanation of the 10 guiding principles that have evolved from the foundation's 22-year-long analysis of the root causes of environmental destruction and of the elements of a sustainable society.

### **Application of Guiding Principles to Specific Areas: Detailed Recommendations**

***The government should strictly regulate water and wastewater systems.***

The provincial government's role should be to regulate water and wastewater systems and to enforce the law.

Government's enforcement of public health and environmental laws should be conducted as a normal police operation through the Ministry of the Solicitor General.

No one should have the right to contaminate a source of water. Farmers, industrial polluters, and sewage treatment plant owners should be responsible for ensuring that their wastes do not impair the quality of water. Criminal and tort liability should apply.

Statutes and regulations should supplement rather than replace common law remedies. In order to allow tort liability to function properly, and to empower affected individuals, the provincial government should eliminate the numerous protections from tort liability that it has created.

Because water and wastewater services are monopolies, they should be subject to economic regulation. Water and wastewater utility rates should be determined by an independent, quasi-judicial economic regulator charged with determining just and reasonable rates and protecting the public interest. Public participation in the regulatory process should be encouraged. Due process should apply. Regulators should be subject to judicial review.

The regulation and law enforcement functions of government should be separate from the ownership, operation, and financing of water and wastewater utilities. When governments regulate systems on one hand, and finance and operate them on the other hand, conflicts of interest often prevent them from

enforcing strict standards.

The provincial government should disband the Ontario Clean Water Agency (OCWA). OCWA has performed poorly, is too close to the government, enjoys a host of subsidies, and discourages private-sector involvement in the industry.

***The private sector should finance, own, operate, and manage water and wastewater systems.***

Water and wastewater utilities should be owned, operated, and financed by the private sector. If municipalities choose to retain ownership, they should enter into long-term operating and maintenance agreements with private firms. The benefits of the private provision of water and wastewater services may include: access to expertise; access to private capital; de-politicization of management decisions; staffing and operating efficiencies; willingness to charge prices that fully reflect costs; direct liability; and increased accountability.

The provincial government should remove barriers to privatization, including the provision in Bill 107 preventing a municipality from selling its water works unless it has paid back all provincial grants for these works.

Water and wastewater utilities and their employees should be liable for the consequences of their actions. Liability creates accountability, providing proper incentives and ensuring that parties are interested in their contribution to a safe water supply. When making spending or operational decisions, the operator's interests are congruent with the public interest if and only if he is responsible for all cost consequences. Government ownership or operation of utilities undermines the effectiveness of liability.

Water and wastewater utilities should be subject to thorough disclosure requirements for economic and quality data.

***Consumers should pay the full costs of constructing and operating water and wastewater systems.***

No level of government – federal, provincial, or municipal – should directly or indirectly (e.g., through loan guarantees or indemnities) subsidize the construction or operation of water or wastewater systems. Removing subsidies improves accountability, disciplines providers, reduces the existing dependence of municipalities, reduces perverse incentives (including the incentives to overbuild facilities and to allow facilities to run down), encourages conservation, and rationalizes decisions regarding where individuals and industries locate.

Water and wastewater prices to users should reflect the full cost of service. Full cost pricing and user pay encourage the efficient use and conservation of water resources, provide the means to support the provision of the service, rationalize investment, and encourage private sector investment.

If particular users cannot afford to pay the full cost of water and wastewater services, the provincial government should provide these individual users with cash subsidies unrelated to their usage. This will encourage equity, efficiency, conservation, and rational location decisions.

## **Energy Probe Research Foundation's Principles**

The Energy Probe Research Foundation is an environmental and public policy research institute. EPRF strives to promote social, economic, and environmental well-being. The following principles have evolved from EPRF's 22-year-long analysis of the root causes of environmental destruction and of the elements of a sustainable society.

1) EPRF works for environmental sustainability by promoting property rights (private or communal), markets, the rule of law, the right to know, accountability through liability, cost and risk internalization, economic efficiency, competition, consumer choice, and an informed public.

2) EPRF strives to eliminate tragedies of the commons<sup>1</sup> by advocating property rights where resources can be exclusive, divisible, and alienable. In these situations, EPRF believes resources are most sustainably managed by the users of the resources themselves. EPRF advocates property rights:

- to establish and preserve rights and responsibilities;
- to account fully for social and environmental costs based on the values assigned by the rights holders; and
- to internalize risks and costs (and to eliminate moral hazards<sup>2</sup>) in decision making.

3) EPRF favours court actions based on the common law of nuisance, trespass, and riparian rights to empower individuals to protect themselves from environmental harm. It does not believe that governments should have the discretion to negotiate with polluters, or with other parties, to override traditional common law protections.

4) EPRF generally opposes expropriation, which often results in environmental harm. It believes that voluntary agreements more fully internalize costs, protect the environment, and ensure economic efficiency.

5) EPRF argues for the break up of unnatural monopolies, created by political or regulatory decree. Where natural monopolies exist, EPRF advocates regulation that is mandated to protect the interests of consumers.

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<sup>1</sup> The tragedy of the commons, popularized by Garrett Hardin's essay in 1968, explains individuals' incentives to exploit common resources for personal gain and the exhaustion of the resources in the process. "Ruin is the destination toward which all men rush, each pursuing his own best interest in a society that believes in the freedom of the commons. Freedom in the commons brings ruin to all."

<sup>2</sup> "Moral hazard" refers to people's increased incentives to take risks when insured.

6) Where property rights cannot easily or affordably be assigned or enforced, EPRF strives to eliminate tragic commons through statutory law and regulation. Although rigorous regulation is often required, regulatory authority must seek to avoid creating barriers to entry, stifling innovation, interrupting the flow of information, and forcing regulated parties to act against their best judgement.

7) EPRF works to ensure the integrity of regulatory systems and the strict enforcement of laws that penalize unauthorized pollution. To eliminate biases and conflicts of interest, and to ensure that public and private sector polluters are treated equally, EPRF advocates independent regulators, who are subject to due process and judicial review, and regulatory processes that require full disclosure of information.

8) EPRF works to establish decentralized decision-making processes and to devolve decision making to the lowest practicable level – that which is closest to the individual.

9) EPRF opposes subsidies to resource use. Where society favours subsidies to ensure social equity, EPRF favours subsidizing resource users with direct payments, untied to the level of consumption, rather than subsidies that lower the apparent cost of the resource.

10) EPRF opposes the socialization of private sector costs and risks through government subsidies and indemnities to the corporate sector. For example, while EPRF approves of private insurance as a way to internalize risks and costs, EPRF opposes government indemnities to resource or financial sectors, particularly if those indemnities protect risk takers and polluters from the risks and costs of their activities.