

*Inquiry on Country Water and Wastewater
Pricing in Western Australia.*



wacoss

Western Australian
Council of Social Service Inc

*Ways to make
a difference*

Draft Report Submission to the Economic Regulation Authority

March 2006

Contact for further information
Kate Mills
Senior Policy Officer
WACOSS Consumer Utilities Project
2 Delhi St West Perth WA 6005
Telephone (08) 9420 7222

CONTENTS

BACKGROUND

EXECUTIVE SUMMARY

DRAFT FINDINGS AND RECOMMENDATIONS

Introduction

Terms of Reference

Residential Water Pricing

Objectives Underlying the Current Country Water Pricing Approach

What Would Efficient Country Water Prices Look Like?

Can Greater Efficiency be Achieved for Country Water Pricing Within the Constraint of Uniformity?

Allocation of Country Towns to Classes

Concessions

Commercial Water Pricing

Uniformity and Cost Reflectivity

Water Usage Threshold

Residential Wastewater Pricing

GRV-Based Pricing

Cost-Reflectivity

Caps on Individual Wastewater Charges

Commercial Wastewater Pricing

Cost Reflectivity

Community Service Obligation Payments

Analysis

BACKGROUND

The Western Australian Council of Social Service Incorporated (WACOSS) is the peak body of the community service sector across Western Australia. Since 1956, WACOSS has been developing and strengthening the non-government community services sector's capacity to assist all Western Australians. With over 350 members, WACOSS has strong relationships with the social services sector and seeks to represent their interests, and those of the disadvantaged individuals and families they assist at a service level. Given this relationship, WACOSS is in a unique position to comment on issues in our society that socially impact upon disadvantaged members of the community.

WACOSS is well respected within both government and non-government arenas as being an authoritative voice for consumers with regard to Utility reform in WA. WACOSS has developed a strong network with Utility Policy Workers across Australia, which provides us with information and expert opinion on these issues.

In March 2005, WACOSS commenced the Consumer Utilities Project, funded through the Department of Consumer and Employment Protection. This project will build upon the utility policy work WACOSS has undertaken over the past 4 years. The Consumer Utilities Project has been established to work with consumers and representative organisations to achieve better outcomes in the provision of essential services.

WACOSS has direct access to the issues of low-income and disadvantaged consumers through our Consumer Reference Group, which includes representatives from the Emergency Relief sector, Unions, Financial Counsellors and Community Legal Centres. These agencies provide us with policy information and direction in relation to our work and look to us to represent the interests of their clients with regard to water issues. We have taken on this role due to the level and severity of the Utility issues being raised by community agencies and the fact that there is no other resourced body in Western Australia representing these issues.

Providing a response to the Inquiry on Country Water and Wastewater Pricing draft report is an important process for WACOSS to engage in to endeavour to ensure the Economic Regulation Authority (ERA) give appropriate consideration to the social impacts when conducting their analysis and making recommendations to the State Government in their final report.

EXECUTIVE SUMMARY

Water is an essential service in maintaining life, well-being and general community health standards. Water usage can be either necessary or discretionary. That is, there is a level of water usage that is unavoidable to sustain a relative standard of life and water usage above this standard for non-essential purposes. Any changes to existing pricing structures and/or the development of new pricing structures must guarantee access to an affordable level of water, and most particularly, ensure that necessary use of water is affordable for low-income households.

In this submission, WACOSS makes a number of comments on the issues raised in the ERA draft report, including;

- WACOSS is concerned that the Terms of Reference may have limited the analysis of services and pricing of all country water services, and via consultation with regional communities have identified issues which the State Government should ensure are adequately addressed. These issues include; the cost of water cartage, the lack of adequate infrastructure and water services within particular pockets of the West Australian community, and the need to ensure any analysis of water prices includes all country towns, not only those serviced by the Water Corporation.
- WACOSS strongly supports the Uniform Pricing Policy, and believe that Governments should continue to support such pricing models. WACOSS also supports greater transparency in identifying commercial and residential costs of water supply, as well as greater transparency in the payment of CSO's.
- As highlighted in the WACOSS submission to the Urban Water Price Inquiry; Price should not be used as a demand management strategy because:
 - The social costs would outweigh the potential benefit.
 - There is a large body of research and evidence that concludes that water is price inelastic, that is demand that is not greatly affected by a change in the price of the product.
 - There is further evidence that suggests low-income households have even lower demand elasticity than high-income households.

DRAFT FINDINGS AND RECOMMENDATIONS

Introduction

Terms of Reference

The Inquiry on Country Water and Wastewater Pricing in Western Australia focuses on the provision of water services to the community by the Water Corporation. A significant proportion of citizens residing in country areas are either not provided water via a scheme or the Water Corporation is not their Water Service Provider.

Feedback received from regional areas includes concern regarding the provision of water services to citizens who use tanks as their primary water source and during periods of low rainfall either resort to water cartage, severely limit their water use, or utilise water sources which may not meet health standards. In particular, issues were raised about the cost of water provided via cartage services. An example was also provided that in times of low rainfall families of 8 would share bath water in order to clean themselves and then this water would also then be used to flush the toilet.

In the WACOSS Issues Paper submission to the ERA, we made the following comments;

“The vast geography of Western Australia poses challenges for governments and service providers in the delivery of all manner of essential and other services and infrastructure. Often the costs associated with the service provision and development of new infrastructure leads to remote and regional areas of Western Australia missing out. This is a reality for many remote and regional communities, in particular indigenous communities, who do not have even basic services which could be compared to or at a level acceptable to metropolitan members of the community.”

“WACOSS understands that many of the Terms of Reference of the Inquiry refer specifically to the Water Corporation; however we also believe that recommendations and any potential impacts also need to be considered in broader terms, of all water consumers, regardless of who provides their water service. For example, customers of private providers will also be impacted upon if changes are made to the uniform tariff policy, however if their demographics and issues are not factored into ERA modelling, then they are at risk of being disadvantaged by any changes.”

WACOSS is concerned that the Terms of Reference may have limited the analysis of services and pricing of all country water services, and via consultation with regional communities have identified issues which the State Government should ensure are adequately addressed. These issues include; the cost of water cartage, the lack of adequate infrastructure and water services within particular

pockets of the West Australian community, and the need to ensure any analysis of water prices includes all country towns, not only those serviced by the Water Corporation.

Objectives Underlying the Current Country Water Pricing Approach

The ERA has made the following comments regarding the Uniform Pricing Policy:

There is no formal policy statement that sets out the social objectives of the uniform pricing policy. However, the social objectives currently underlying the uniform pricing policy can be discerned from observing country prices and appear to include: the provision of water for basic needs at a uniform price; the provision of an average amount of water at a location at a uniform price; and the provision of water to customers who use up to 150 kL/year more than the average at a particular location at a discounted price to the charge that applies in Perth.

WACOSS strongly supports the Uniform Pricing Policy, and as stated in the WACOSS Issues Paper submission, supports the uniform tariff threshold being set at a level of agreed water use for individuals to maintain a reasonable quality of life, recognizing the essential nature of water services.

As identified in the OECD report into *Social Issues in the Provisions and Pricing of Water Services*:

“One such approach would define the basic needs part of water demand, access to which should be guaranteed for all (especially low income) households and beyond which the prices for water services should reflect economic and environmental policy objectives.”

A level of agreed water use for individuals to maintain a reasonable quality of life is different to the use of an ‘average’ to set the threshold. Strict averaging based on current consumption may result in some towns who may be using more water than necessary automatically being placed in a higher class than those towns who are currently using less water and as WACOSS identified in the Urban Water Price Inquiry, large households are often penalised under pricing models which do not take into account household size, and rely on average water use.

WACOSS comments in the Urban Price Inquiry submission are therefore also relevant to the Country Water Price Inquiry;

Pricing models that reflect the size of the household (number of occupants) and can therefore better assess discretionary use, and the ability of the household to respond to price signals would be more appropriate to ensure efficient pricing, increased water conservation, and lower social costs.

The Independent Pricing and Regulatory Tribunal (IPART) of NSW, *Investigations into price structures to reduce demand for water in the Sydney basin* report commented on the use of price structures to reduce demand for water;

"...larger households are likely to use more water to meet basic, non-discretionary needs and so have less ability to respond to price signals by reducing their consumption. IPART believes that, ideally, the retail price structure should not expose a high number of vulnerable customers to higher water bills, should target discretionary water use, and should be set to minimise the extent to which larger households are required to pay higher charges for efficient or non-discretionary water use."¹

WACOSS believes that the objectives of the Uniform Pricing Policy include;

- Enabling citizens to access an essential service;
- Acknowledging climatic and other impacts on water use; and
- Providing a comparable water service to all West Australians at comparable prices.

What Would Efficient Country Water Prices Look Like?

The ERA comments:

Application of economic principles on a town-by-town basis without reference to the uniform pricing policy would almost certainly result in significantly different usage charges and fixed charges between towns with higher payments being made in total by customers in the country systems.

In order to achieve more efficient water pricing, the Corporation would need to develop better systems to differentiate commercial and residential costs and to identify the forward-looking supply costs for towns or groups of towns that are approaching capacity and need to increase their water supplies.

WACOSS offers two comments regarding the application of strict economic theories to country water services.

The view expressed by the Department of Industry and Resources (DOIR), quoted in the draft report, that:

"it is important that any pricing (and policy) structures proposed reflect the need to encourage, where economically feasible, additional water providers. Creating a competitive environment that sponsors full contestability in providing water and wastewater services to industry (and the residential sector) will enhance the State's long term development potential."

¹ *Investigations into price structures to reduce demand for water in the Sydney basin*. Independent Pricing and Regulatory Tribunal of NSW, 2003 pg 5

is a statement of opinion, rather than fact. The benefits to industry of competitive markets may be clear to the DOIR, however it remains to be seen whether full retail contestability within the essential service markets for residential customers benefits them. Indeed, since Full Retail Contestability has been introduced to the WA gas market the cost of gas services has increased.

The second comment relates to the application of forward-looking supply costs, noting that as outlined in the State Water Strategy, the highest projected increase in water demand between 1999 and 2020 will be in the irrigated agriculture and mining sectors, commercial rather than residential.

WACOSS supports greater transparency in identifying commercial and residential costs of water supply. Acknowledging that significant increased water demand in regional areas of Western Australia is more than likely to be the result of new commercial activity (or an expansion of current activity) which may result in increased employment and therefore additional residential water demand, it is important that the commercial sector rather than the residential sector be identified as the reason for the forward-looking cost and water charges apportioned respectively.

In a user-pays system, household budgets need to take account of water use and cost, and it is entirely reasonable that business also accounts appropriately for this business cost. That is not to say that as part of the State Government's commitment to Regional and Rural Western Australia, that they don't offer incentives or financial assistance for business to develop in those regions, however; it should be a transparent process, and costs should not be shifted from commercial to residential water uses through the process of forward-looking supply costs.

To this extent, WACOSS supports the comment made by the Chamber of Commerce and Industry, if it also applies to commercial customers;

"...social objectives (of encouraging regional development) be delivered in a way that minimise as far as possible the distorting of price signals...it is better to pay the cost of...guaranteeing access to affordable water in the regions by a direct subsidy from general government, rather than through cross-subsidies from other (residential) consumers."

WACOSS is also concerned about the calculation of forward-looking supply costs, as the information is not as reliable as the current calculation method of the previous three-years cost of supply. In addition, as identified above, the need to provide increased supply of water to a region will be based significantly on commercial activity; it is unreasonable that this future cost be shifted to current residential water users.

Can Greater Efficiency be Achieved for Country Water Pricing Within the Constraint of Uniformity?

The ERA comments:

The commitment to and the specific implementation of uniformity limits the options available to use price as an incentive to achieve greater efficiency. Setting the threshold differently across groups of towns, at say the average water use for the group, would ensure that a similar percentage of households in each group exceed the threshold and pay cost reflective prices. The usage charge below the threshold and fixed charge could be adjusted to achieve the average payment (which could be set, say, at the average payment for Perth). This would allow the usage charge above the threshold to be set in relation to LRMC, where appropriate, thereby introducing an efficiency incentive for above average users.

Using price as an incentive to achieve greater efficiency is based on the assumption that residential consumers a) have the capacity to respond to price increases and b) will respond to price increases by reducing their water use.

As highlighted in the WACOSS submission to the Urban Water Price Inquiry; Price should not be used as a demand management strategy because:

- The social costs would outweigh the potential benefit.
- There is a large body of research and evidence that concludes that water is price inelastic, that is demand that is not greatly affected by a change in the price of the product.
- There is further evidence that suggests low-income households have even lower demand elasticity than high-income households.

Allocation of Country Towns to Classes

The ERA comments:

Grouping of towns should ideally be based on forward looking cost of providing water services and additionally account for non-health related aspects of water quality and differences in weather conditions between groups of towns. Whilst such a classification is dependent on data that is not readily available from the Corporation, it is the case that the current classification needs to be reconsidered to ensure that a reasonable balance is achieved between efficiency and social objectives.

Grouping towns that are approaching the need to increase their water supplies would allow (possibly imprecise) estimates of LRMC to be applied while the usage charge above the threshold for towns that are unlikely to need to increase their water supplies could be set to at least recover the avoidable costs of providing water services and, where appropriate, also make a contribution to the Corporation's return on its investment.

WACOSS supports a flexible approach in the classification of country towns, and supports the annual review process, however as outlined above, grouping towns based on forward-looking costs would negatively impact on residential consumers.

Concessions

The ERA has made the following draft findings in relation to Concessions:

There are various options for restructuring existing country water pricing arrangements including basing the threshold below which concessions apply on a value such as average consumption for a group of towns to help achieve clearly specified objectives.

In the WACOSS issues paper submission we made the following comments about the extension of concessions;

As identified, different concessions apply to Metropolitan, Group A and Group B customers. WACOSS supports an extension of concessions on water usage for Perth and Group A residents up to 600kL/year. Under the current usage charges for group A residents (Attachment one) for amounts between 400 and 600 kL/year, residents pay up to 95.2 cents/kL more than group B residents. When current concession are applied, eligible concession card holders in Group A pay as much as 138.6 cents/kL more than eligible concession card holders in Group B.

WACOSS acknowledges the Water Corporation position expressed in the Draft Report which indicates to re-align concessions down, would have a significant impact on household budgets if they lose part of their concession and the alternative to re-align the concessions up, would have a significant impact on the State Government budget. WACOSS favours the impact to be made on the budget that can most afford the re-alignment; the State Government.

The ERA also comments:

The concession arrangements may require further consideration by Government. Any such review might consider, among other things, the objectives of the policy, criteria for eligibility, the options for providing assistance, and the consistent treatment of those appropriately considered eligible for assistance.

WACOSS has been urging a review of State Concessions for a number of years now. In the absence of this review being undertaken, given that an analysis of water concessions clearly falls within the terms of reference of this review, it may be useful for the ERA to provide increased analysis, information, and specific recommendations regarding CSO payments and concessions. It would be useful to know the impacts on household budgets and the State Government budget of the various re-alignment options identified by the ERA.

It is also important to acknowledge that access to water services and use of water resources can be influenced by:

- Tariff amount/Price: that is how much it costs per kilolitre of water
- Tariff design; including the structure prices take such as price increments at certain steps
- Allocation; whether or not restrictions are in place, and how much discretionary water use you have (particularly relevant for large families)
- Concessions: including horizontal based such as rebates for the whole of the community, and vertical based which acknowledges the inability for low income households to cover the full cost of essential services
- Attitudes; what education campaigns are effective and are being run, and how is the community responding to the campaigns

In that context, the ERA can not rely on concessions alone to ensure the social welfare and equity considerations of a public interest test are met.

To this extent, WACOSS does not support the Chamber of Commerce and Industry comment that "...social objectives be delivered in a way that minimise as far as possible the distorting of price signals, and the economic efficiencies and inequities that would result. ...it is better to pay the cost of community service obligations guaranteeing access to affordable water in the regions by a direct subsidy from general government, rather than through cross-subsidies from other consumers."

Whilst the Chamber of Commerce and Industry may view price signals as an effective demand management tool for commercial customers, it is not evidenced to WACOSS that residential water use is price elastic, and therefore, price signals would not result in more efficient use of water in the residential sector.

Price should not be used as a demand management strategy because:

- The social costs would outweigh the potential benefit.
- There is a large body of research and evidence that concludes that water is price inelastic, that is demand that is not greatly affected by a change in the price of the product.
- There is further evidence that suggests low-income households have even lower demand elasticity than high-income households.

WACOSS is disappointed that the particular comments raised in the Public Interest Advocacy Centre submission, in particular the comments regarding; caps on annual residential bill increases; alternative tariff structures, and demand management programmes linked to household size; special tariffs for vulnerable customers; non-price measures such as community-wide restrictions, retrofits, rebates and hardship programmes; and discontinuation of penalty fees for vulnerable customers; were not considered by the ERA, and instead that they "could be considered within a review of the concessions policy" when clearly

many of these issues raised fall within the terms of reference of the inquiry, and would not be relevant to be considered within a review of state government concessions.

Commercial Water Pricing

Uniformity and Cost Reflectivity

The ERA comments:

It is not clear that it is the Government's intention in its uniform pricing policy to provide discounts to commercial users. In the absence of residential and commercial cost information by scheme it is not possible to conclude the extent to which the CSO payment is benefiting commercial customers rather than residential customers.

WACOSS supports greater transparency in identifying commercial and residential costs of water supply. Acknowledging that significant increased water demand in regional areas of Western Australia is more than likely to be the result of new commercial activity (or an expansion of current activity) which may result in increased employment and therefore additional residential water demand, it is important that the commercial sector rather than the residential sector be identified as the reason for the forward-looking cost and water charges apportioned respectively.

In a user-pays system, household budgets need to take account of water use and cost, and it is entirely reasonable that business also accounts appropriately for this business cost. That is not to say that as part of the State Government's commitment to Regional and Rural Western Australia, that they don't offer incentives or financial assistance for business to develop in those regions, however; it should be a transparent process, and costs should not be shifted from commercial to residential water uses through the process of forward-looking supply costs.

To this extent, WACOSS supports the comment made by the Chamber of Commerce and Industry, if it also applies to commercial customers;

"...social objectives (of encouraging regional development) be delivered in a way that minimise as far as possible the distorting of price signals...it is better to pay the cost of...guaranteeing access to affordable water in the regions by a direct subsidy from general government, rather than through cross-subsidies from other (residential) consumers."

Residential Wastewater Pricing

GRV-Based Pricing

The ERA comments:

Under GRV-based pricing, customers within towns, and in different towns with identical wastewater costs, pay different amounts for the same wastewater service.

In the Urban Water Price Inquiry, WACOSS commented that:

It is important that progressive wastewater charges, based on property valuation, continue to be applied. This ensures that those in our community who have the greatest capacity to pay make an additional contribution to important services.

As identified by the ERA, a form of GRV based pricing exists, however it is significantly distorted by a complicated system of cross-subsidisation and price caps.

WACOSS believes a strict GRV pricing system would be more equitable; as regardless of where people live (metropolitan or regional) they would pay similar prices. WACOSS does not oppose a cap, however this could be more equitably distributed and offered as a percentage discount for all regional residential consumers on the GRV amount; meeting the objective of the Government providing incentives/support for people living in regional areas. This would be more a more transparent, more equitable, and easier to calculate than the current model. This would also mean that although for some towns, they may pay more for their wastewater service, some towns may pay less

Cost-Reflectivity

The ERA comments:

While the current approach allows for wastewater charges to reflect costs on a town-by-town basis (subject to a cap for towns with expensive wastewater systems) actual charges show no relationship to actual costs, despite a policy since 1993 to gradually align charges with costs.

The cap on the recovery of costs from an individual town (currently \$0.12 per dollar of GRV) is applied for affordability reasons but is inconsistent with the principle of cost-reflective pricing.

Cost-reflective prices for wastewater services would provide important information to alternative service providers who may be considering offering wastewater services, particularly in new developments.

Cost-reflective pricing of residential wastewater services would require the Corporation to develop more detailed data on the costs of service provision, including differentiation between servicing residential and commercial customers.

WACOSS comments above cover many of these issues. However we also re-iterate our comments regarding the higher costs of providing services and infrastructure in regional areas; which to a certain extent are the responsibility of the Government to provide. Full cost-reflective pricing shifts this infrastructure burden onto individual citizens; many of whom may not have the capacity to pay full-cost recovery prices, and arguably the Government has the responsibility to provide, which is why WACOSS recommends any shortfall between GRV residential pricing with equitable discount, and full costs be met with the payment of a CSO.

Caps on Individual Wastewater Charges

The ERA comments:

The effect of the cap on individual country residential wastewater charges is to shift the relative contribution from customers in high-value properties towards customers in low-value properties. In fact, country customers in low-value properties pay, on average, higher wastewater charges than customers in the same value properties in Perth. This is inconsistent with the principles of the uniform pricing policy. However, the individual cap serves to spread wastewater payments more evenly between households in a town, and results in more cost-reflective pricing because the costs of wastewater provision do not differ significantly between households. The Authority is not suggesting that the cap be removed but is particularly interested in the views of interested parties on this matter.

WACOSS does not oppose a cap, however this could be more equitably distributed and offered as a percentage discount for all regional residential consumers on the GRV amount; meeting the objective of the Government providing incentives/support for people living in regional areas.

Commercial Wastewater Pricing

Cost Reflectivity

The ERA comments:

There is an inconsistency between the approaches to commercial and residential wastewater pricing. Uniform pricing for commercial users coupled with

a cost-recovery pricing approach for residential users means that residential users in towns with high wastewater costs currently have to pay more relative to commercial users. The Authority's preliminary view is to recommend cost reflectivity for commercial customers.

WACOSS does not view inconsistency between wastewater charging as an issue in itself, but to the extent that residential consumers are burdened with higher costs as a result of commercial wastewater charges not being set in an appropriate manner, then we would support reform in this area.

Community Service Obligation Payments

Analysis

The ERA comments:

CSOs are not clearly related to specific policy objectives. Although used primarily to fund the uniform pricing policy, CSOs are also used to fund residential wastewater customers and are likely to be benefiting commercial customers.

CSO's exist to ensure universal access to services, and in the case of Water Corporation services, CSO are utilised as a 'subsidy' for the provision of country water supplies, and as a means of providing a concession for low income and disadvantaged members of our community. CSO payments are an integral part of the range of support needed by disadvantaged individuals and families. It is important to provide concessions for equity purposes, not as purely a form of charity. It is vital that concessions are accessible, equitable and adequate and these principles should guide the payment of CSO's.

The ERA also comments:

As currently understood, the uniform pricing policy applies to residential water pricing. Yet, other aspects of pricing such as the imposition of caps on individual wastewater charges appear contrary to the social objectives underlying uniform pricing. The Authority's preliminary view is that the uniform pricing policy would benefit from being clearly defined and documented.

WACOSS supports the development of a policy, with clearly defined objectives of the Uniform Pricing Policy, however the most important position regarding the uniform pricing policy is that Governments continue to support this pricing model.

The ERA also comments:

CSOs could be made more transparent at the town level. The benefit of doing so would be to provide the opportunity for competitive tenders for water and wastewater services.

The benefit of making CSO payments more transparent should relate to the need for accountability, rather than only expressed as necessary to induce competition.

WACOSS recommends that CSO payments for pensioner concessions be extended to all water providers, as many rural/regional water consumers are disadvantaged if their water provider is not the Water Corporation, and as a result not automatically eligible for the State Government concession.