
WATER

WA301*

Economic Regulation Authority Act 2003

Economic Regulation Authority (Water and Wastewater Pricing Reference) Notice 2004

Given by the Economic Regulation Authority under section 34(1) of the *Economic Regulation Authority Act 2003*.

1. Citation

This notice may be cited as the *Economic Regulation Authority (Water and Wastewater Pricing Reference) Notice 2004*.

2. Reference on water and wastewater pricing

- (1) Under section 32(1) of the *Economic Regulation Authority Act 2003*, the Treasurer has referred to the Economic Regulation Authority for inquiry the water and wastewater pricing of the Water Corporation (as established by the *Water Corporation Act 1995*) and the water pricing of the Bunbury Water Board and Busselton Water Board (as established by the *Water Boards Act 1904*).
- (2) The terms of reference for the inquiry are set out in Schedule 1.

3. Period of inquiry

The period of the inquiry is 15 June 2004 to 12 August 2005.

4. Public submissions

- (1) Members of the public may make written submissions to the Economic Regulation Authority on any matter that —
 - (a) is dealt with in the issues paper or draft report referred to in the terms of reference; or
 - (b) is otherwise relevant to the terms of reference.
- (2) The address for submissions is the Economic Regulation Authority, GPO Box 8469, Perth Business Centre WA 6849.
- (3) Submissions in response to the issues paper or draft report may be made within 6 weeks after the release of the relevant document or any longer period allowed by the Economic Regulation Authority.

5. Further information

Further information about public submissions and other matters relating to the inquiry is available on the Economic Regulation Authority's website at <http://www.era.wa.gov.au>.

Schedule 1 — Terms of reference

[cl. 2(2)]

I, ERIC RIPPER, Treasurer (following consultation with the Minister for the Environment and the Minister for Government Enterprises) and pursuant to section 32(1) of the *Economic Regulation Authority Act 2003* (the ERA Act), request that the Economic Regulation Authority (the Authority) undertake an inquiry into the water and wastewater pricing of the Water Corporation (as established by the *Water Corporation Act 1995*) and the water pricing of the Bunbury Water Board and Busselton Water Board (as established by the *Water Boards Act 1904*).

The Authority is to investigate and report on the following matters related to the pricing of water and wastewater services in Western Australia:

- the appropriate charging structures and recommended tariff levels for the Water Corporation's and the Bunbury and Busselton Water Board's urban water supply services (residential and non residential); and
- the appropriate charging structure and recommended tariff level for the Water Corporation's urban wastewater services (residential and non residential).

Section 26 of the ERA Act requires the Authority to have regard to certain matters:

- the need to promote regulatory outcomes that are in the public interest;
- the long-term interests of consumers in relation to the price, quality and reliability of goods and services provided in relevant markets;
- the need to encourage investment in relevant markets;
- the legitimate business interests of investors and service providers in relevant markets;
- the need to promote competitive and fair market conduct;
- the need to prevent abuse of monopoly or market power; and
- the need to promote transparent decision-making processes that involve public consultation.

In conducting its investigation, the Authority must review:

- the regulatory asset base of each of the service providers;
- the non capital cost forecasts of the service providers;
- the depreciation and forecast capital expenditure program of the service providers; and

- the appropriate rate of return on public sector assets, including appropriate payments of dividends to the Government of Western Australia.

The Authority must give consideration to, but will not be limited to, the following matters:

- the methodology for assessing the revenue requirements of the service providers;
- the most appropriate price path and period, including the requirement for periodic reviews of that price path;
- the current structure and level of urban water and wastewater prices;
- the cost of providing the services concerned, including
 - a target for improvement in the efficiency in the supply of services;
 - any additional resources needed to meet the required standards of quality, reliability and safety, including such matters as the protection and development of future water resources; and
 - how changes in standards and operating conditions faced by the service providers impact on its revenue requirements;
- the impact of pricing policies on borrowing, capital and dividend requirements and, in particular, the impact of any need to renew or increase relevant assets;
- considerations of demand management;
- the effect on and of general price inflation over the medium term;
- the need to maintain ecologically sustainable development, including by appropriate pricing policies that take account of all feasible options for protecting the environment;
- the social impact of the recommendations; and
- the effect of any pricing recommendation on the level of government funding (through Community Service Obligation payments).

In developing its recommendations the Authority is to have regard to the following policies:

- the pricing principles of the 1994 COAG water reform agreement (as set out in Appendix to this reference);
- the Western Australian State Government's Uniform Pricing Policy;
- the Western Australian State Government's Sustainability Policy;
- the Western Australian State Government's Community Service Obligations Policy; and

- the pricing mechanisms available to the utility service providers through the *Water Agencies (Powers) Act 1984* and the *Water Boards Act 1904*.

The Authority will release an issues paper as soon as possible after receiving the reference. The paper is to facilitate public consultation on the basis of invitations for written submissions from industry, government and all other stakeholder groups, including the general community.

A draft report is to be made available by 18 March 2005 for further public consultation on the basis of invitations for written submissions.

A final report is to be completed by no later than 12 August 2005. This will ensure that any recommendations adopted by the Government are available for implementation in 2006/07.

ERIC RIPPER MLA, Deputy Premier;
Treasurer; Minister For Energy.

APPENDIX

GUIDELINES FOR THE APPLICATION OF SECTION 3 OF THE COAG WATER REFORM AGREEMENT (THE COAG PRICING PRINCIPLES)

1. Prices will be set by the nominated jurisdictional regulators (or equivalent) who in examining full cost recovery as an input to price determinations should have regard to the principles set out below.
2. The deprival value methodology should be used for asset valuation unless a specific circumstance justifies another method.
3. An annuity approach should be used to determine the medium to long-term cash requirements for asset replacement/refurbishment where it is desired that the service delivery capacity be maintained.
4. To avoid monopoly rents, a water business should not recover more than the operational, maintenance and administrative costs, externalities, taxes or tax equivalent regime (TERs), provision for the cost of asset consumption and cost of capital, the latter being calculated using a weighted average cost of capital.
5. To be viable, a water business should recover, at least, the operational, maintenance and administrative costs, externalities, taxes or TERs (not including income tax), the interest cost on debt, dividends (if any) and make provision for future asset refurbishment/replacement (as noted in (3) above). Dividends should be set at a level that reflects commercial realities and stimulates a competitive market outcome.
6. In applying (4) and (5) above, economic regulators (or equivalent) should determine the level of revenue for a water business based on efficient resource pricing and business costs. Specific circumstances may justify transition arrangements to that level.
7. In determining prices, transparency is required in the treatment of community service obligations, contributed assets, the opening value of assets, externalities including resource management costs, and tax equivalent regimes.

Notes:

- The reference to “or equivalent” in principles 1 and 6 is included to take account of those jurisdictions where there is no nominated jurisdictional regulator for water pricing.
- The phrase “not including income tax” in principle 5 only applies to those organisations that do not pay income tax.
- “Externalities” in principles 5 and 7 means environmental and natural resource management costs attributable to and incurred by the water business.
- “Efficient resource pricing” in principle 6 includes the need to use pricing to send the correct economic signals to consumers on the high cost of augmenting water supply systems. Water is often charged for through a two-part tariff arrangement in which there are separate components for access to the infrastructure and for usage. As an augmentation approaches, the usage component will ideally be based on long-run marginal costs so that the correct pricing signals are sent.
- “Efficient business costs” in principle 6 are the minimum costs that would be incurred by an organisation in providing a specific service to a specific customer or group of customers, or the minimum amount that would be avoided by not providing the service to the customer or group of customers.
- Efficient business costs will be less than actual costs if the organisation is not operating as efficiently as possible.

LYNDON G. ROWE, Chairman,
Economic Regulation Authority.

