Department of Water
Government of Western Australia

Your Ref:
Our ref: CEOW545/09
Enquiries: Patrick Seares ph 6364 6853

Mr Lyndon Rowe
Economic Regulation Authority
Level 6, Governor Stirling Tower
197 St Georges Terrace
PERTH WA 6000

Dear Mr Rowe

SUBMISSION TO THE DISCUSSION PAPER – INQUIRY INTO WATER RESOURCE MANAGEMENT AND PLANNING CHARGES

Thank you for the opportunity to comment on your discussion paper released on 6 August 2009 as part of the Inquiry into Water Resource Management and Planning Charges.

The Department of Water (DoW) generally agrees with the principles as they align well to those in our response to the Economic Regulatory Authority (ERA) issues paper. However, we would like the ERA to consider further the points raised below in the development of its draft report.

1. Consider fairness as well as equity

The issue of equity could be broadened to consider fairness of recovering the costs of producing a public good, such as an allocation plan, from public funds where the production of such a plan is only needed when private users use a common good for private benefit (see also point 2 below).

2. Consider beneficiaries

The DoW perceives a focus on, and uncertainty around, defining the DoW's services as public and private goods. We believe that the ERA should investigate in more detail the connections between public and private goods and public and private benefit.

To expand, we note the definition of a public good (non-exclusive, non-rival) on page 7 of the discussion paper and observe that the definition does not indicate if benefits accrue evenly or for particular groups and who the benefits accrue to. This will depend on the good in question and whether it is a pure public good or a *quasi* public good, such as an allocation plan that also has private benefits attached. In particular, we point out that public good does not equate to public benefit and vice versa and ask the ERA to more clearly distinguish between public/private goods and public/private benefits.

While the recovery of the cost of a public good is unlikely to increase efficiency, it may still be fair to make specific beneficiaries pay where they benefit from a public good. Possible

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examples are street lighting, roads and parks, which are all public goods (by definition) but have localised public benefits for which the Government tries to recover costs from developers for equity reasons **not** to increase efficiency.

In the example mentioned in the discussion paper, the DoW agrees that an allocation plan has public good characteristics because it is in the public domain and its contents are non-excludable and non-rival in consumption, that is, it can not be restricted to specific users (spill-over effects). However, the main reason for producing a plan stems from people's interest in using water as a private good. If sufficient interest exists, proclamation, followed by a plan, is necessary to provide security of supply for users (protecting the private good) while ensuring that negative externalities (environmental impacts as well as user conflicts) are kept at a minimum (or an acceptable level of risk). These public benefits, as well as the public good in the form of an allocation plan, are really a side-product.
Attachment B illustrates the relationship of externalities and allocation planning.

3. Scope of discussion paper – drainage, water source protection and metering

The DoW strongly urges the ERA to consider all key areas of our functions for cost recovery. The discussion paper focuses on water allocation and licensing and gives only passing mention the other high priority areas for cost recovery identified in our response to the issues paper. Metering, drainage assessment and planning, and drinking water source protection represent a sizable part of the department's business in which we provide services to users that derive a private benefit. We refer to the relevant sections of our response to the ERA issues paper for budget and other details.

We also note that the Department of Treasury and Finance pursues a policy that advocates full cost recovery in Government departments and that this is within the intent of the Terms of Reference.

4. Competition for services

The DoW supports greater competition in the delivery of water resource management services to users, provided those services do not attempt to replicate legislative decision-making and regulatory functions. Competition already occurs when a proponent either does its own hydrological work for a resource or employs a consultant, or, indirectly, when the DoW goes to tender and employs the winning consultant to do the work. In either case, and also in the event the DoW does the work in-house, the ultimate decision-making lies with the DoW, e.g., in proclaiming an area or setting the allocation level. There are also costs to the DoW, for example, when reviewing and assessing hydrological reports and considering operation strategies to be employed in mining operations.

In addition to the above, our principles for cost recovery also refer to consistency, transparency and practicality, which are not dealt with explicitly in the discussion paper (see Attachment A for a comparison of concepts). We think it important for the ERA to consider the need for these other principles to help achieve appropriate and community-supported implementation of cost recovery. The DoW believes that these principles are in accord with two specific elements of the inquiry's Terms of Reference, i.e. "the options are to include: the implementation impacts for various types of users, including a sensitivity analysis on capacity to pay assumptions" and "in developing its recommendations, the Authority will have regard to: the Government's social, economic and environmental policy objectives".

Water management is becoming increasingly complex as all the 'easy' water has been used in Western Australia. The cost of managing around the margins of available water or appropriate land for development will continue to increase. Without a stable stream of funds

resulting from the implementation of cost recovery, services have the potential to be impacted to the detriment of the state. Potential impacts of service reduction include:

- longer timelines for water licence assessment and approval for mining or other users
- delays in drainage assessments leading to significantly expensive delays for land developments of new housing
- reduction in allocation limits across the state due to the inability to monitor and manage the water resource or respond to water user concerns and disputes
- reduced ability to mange for environmental and business sustainability in areas with high pressure and trends in reduced rainfall.

If you wish to discuss the above in further detail, please contact Mr Patrick Seares, Manager Strategic Water Policy and Planning, the Department of Water on telephone (08) 6364 6853. We look forward to continuing to assist the ERA with this important inquiry.

Yours sincerely

Kim Taylor
DIRECTOR GENERAL

31 August 2009

Attach

Attachment A

Comparison of concepts - ERA discussion paper and DoW response to the ERA issues paper

The ERA discussion paper focuses on the economic concepts of efficiency, market failure and cost allocation, whereas the DoW response to the issues paper outlines principles for cost recovery, i.e. equity and fairness, transparency, practicality, consistency and equity, that are not purely economic.

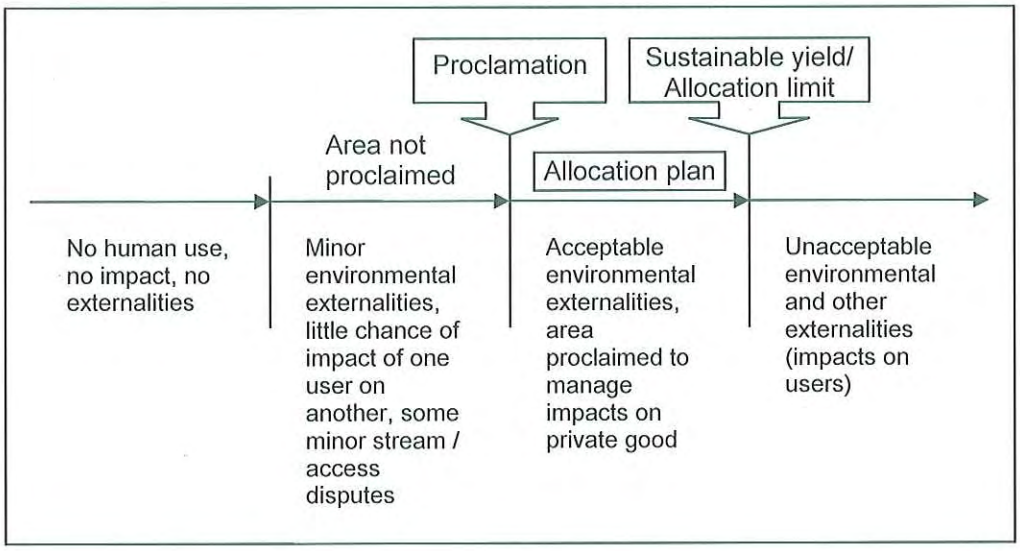
Economic concepts - ERA discussion paper	**Principles for cost recovery – DoW response to issues paper**
Efficiency: • Allocative efficiency: resources are allocated to their most productive use in society • Productive efficiency: goods and services are provided at least cost • Dynamic efficiency: investments are optimal over the long term, in their timing and location.	Efficiency: • Where there is a significant and potentially avoidable marginal cost associated with providing a service to users, the charge for that service should incorporate that cost.
Cost allocation: • in an efficient market, costs are generally allocated to those who cause the costs to be incurred. • Overheads: can be recovered • Lumpy investment costs: are shared between existing, new and future users • Equity: customers in similar circumstances should be treated similarly (horizontal equity) and those in different circumstances should be treated differently (vertical equity)	Equity and fairness: • Costs will be recovered on activities (or a portion thereof) that are attributed to a private benefit. • Charges will be based on the level of effort required to deliver the product or service. • Ability to pay will be considered and appropriate mechanisms established to ensure that support is provided to disadvantaged socio-economic groups.
Equity: • Horizontal equity: customers in similar circumstances should be treated similarly • Vertical equity: customers in different circumstances should be treated differently	Consistency: • Cost recovery for products and services will be applied consistently throughout the state, that is, if people are charged for a service in the Pilbara they will also be charged for that service in the South West. However, depending on the model adopted, actual charges may be different across areas to reflect the difference in effort required to deliver the service. • Charges and fees will be applied using the appropriate legislation and regulatory framework. • All proposed cost recovery models will be in line with the Department of Treasury and Finance's guideline on costing and pricing for government services[1]

[1] Department of Treasury and Finance (2007) *Costing and pricing government services* 5th edition

	• All proposed cost recovery models will be in line with the national water reform agenda (in particular the National Water Initiative).
Market failures • Public goods • Common property goods • Externalities • Lack of competition	No equivalent identified in DoW response to issues paper
No equivalent identified in ERA issues paper or discussion paper	Transparency: • Users will be provided with detail on what activities, products and/or services their charges have covered. • Any income from charges will be based on discrete activities and costs and transparently reported on an agreed term. • The Economic Regulation Authority will periodically review any fees and charges.
No equivalent identified in ERA issues paper or discussion paper	Practicality: • The system associated with implementing or administering charging arrangements would not be so complex as to diminish the benefit of a charge. • A phased-in approach will be ensure that charges are applied appropriately and accurately.

Attachment B

Relationship of externalities and allocation planning



An important point to note is that environmental externalities occur as soon as humans use water in an area, even if that 'use' is for aesthetic or 'non-consumptive' uses. Planning is done to manage those impacts relative to their magnitude. Hence, the only reason for the Department of Water to do the work associated with allocation planning is because people use water (as a private good) which impacts on the public good (environment and social amenity).