

1 April 2019

## WHAT

We have released for comment a Draft Report setting out our draft pricing arrangements for recycled water, sewer mining and stormwater harvesting services for Sydney Water, Hunter Water, the Central Coast Council and Essential Energy (Essential Water in Broken Hill). We also released our accompanying Draft Determination for recycled water developer charges.



## WHY

We have established draft pricing arrangements that are flexible and administratively simple to implement, which promote efficient investment in (and uptake of) recycled water.

Our review also addresses recommendations from Infrastructure NSW's review of regulatory barriers to cost-effective water recycling, released in January 2019.



## WHO

In addition to the public water utilities, this review is relevant for a wide range of stakeholders, including:

- ▼ customers of recycled water, sewer mining and stormwater harvesting services
- ▼ developers, who may be affected by recycled water developer charges
- ▼ privately owned water utilities who may wish to compete with public water utilities to provide water, wastewater or recycled water services, and
- ▼ the wider community and the public water utilities' broader customer base,

who may benefit indirectly from recycled water schemes.



## HOW

We have followed IPART's established review process. We released an Issues Paper in September 2018 for public consultation. We also held a Public Hearing in December 2018.



## WHEN

The key dates for this review are:

- ▼ 26 April 2019 - Receive submissions on Draft Report and Draft Determination
- ▼ Late June 2019 - Release Final Report and Determination
- ▼ 1 July 2019 – New recycled water pricing arrangements and developer charges take effect.



## WHAT NEXT

Submissions on the Draft Report and Draft Determination are due by **26 April 2019**.

We prefer submissions via our online form, available on our website [www.ipart.nsw.gov.au](http://www.ipart.nsw.gov.au). You can also send comments by mail to:

### Review of recycled water and related services

Independent Pricing and Regulatory Tribunal  
PO Box K35  
Haymarket Post Shop NSW 1240

Unless identified as confidential, we plan to publish all submissions on our website soon after the closing date.

## 1 What are the key draft decisions of our review?

We outline our key draft decisions below. We have established six key objectives for the regulation and pricing of recycled water and related services, which frame our approach. These include that the regulation and prices should aim to:

- ▼ achieve economic efficiency
- ▼ facilitate competition
- ▼ provide revenue adequacy
- ▼ have regard to customer preferences and impacts
- ▼ be transparent and simple, and
- ▼ reflect the National Water Initiative principles and other relevant water reviews.

### Our pricing arrangements should maximise net economic benefit

With cost of living pressures, our price regulation needs to support efficient and effective water services that draw from dams, the desalination plant and recycled water plants as appropriate.

We have refined our regulatory approach to support efficient investment in recycled water, including where it provides broader benefits to customers, while also protecting recycled water customers from any monopoly power of the public water utilities. We have ensured that the broader customer base<sup>1</sup> would be **no worse off** due to the public water utilities investing in recycled water, as per the cost recovery arrangements set out below. This is a fundamental principle guiding our draft pricing arrangements.

Under our draft framework, where recycled water is the cheapest approach to supplying water, wastewater or stormwater services, it will be funded by the broader customer base through periodic charges and developers through developer charges, where applicable. This approach treats recycled water on an equivalent basis to other regulated services, where it is a prudent and efficient way of delivering a regulated service.

We have also improved our approach to accommodate the costs of recycled water where it is not the cheapest solution, but provides other benefits. Where benefits accrue to the broader customer base, then prices paid by those customers may include an amount to reflect those benefits. Where the benefits accrue only to the customers who receive the recycled water, then those customers may pay for these benefits through higher recycled water prices or through a contribution from the developer.

This feature of our draft framework allows the costs of recycled water schemes to be considered in the context of the system-wide outcomes they achieve. It is one of the most substantial changes to our current cost recovery framework and is widely supported by stakeholders.

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<sup>1</sup> The broader customer base refers to the public water utility's 'traditional' water, wastewater and stormwater customers that are subject to postage-stamp pricing.

Specifically, under our draft framework, if a recycled water scheme is a *higher-cost* servicing solution, then part of the recycled water costs can be recovered from the broader customer base, where the scheme delivers:

- ▼ **Avoided or deferred costs** – benefits from delaying or averting the need for augmentation of a water utility’s potable water, wastewater and/or stormwater network as a result of the recycled water scheme(s) – noting that the broader customer base will be made no worse off under these arrangements than in the absence of the scheme(s).
- ▼ **External benefits** – the value attributed to the environmental, health, and liveability benefits of the recycled water scheme(s) where there is willingness-to-pay by the broader customer base.

The broader customer base will not pay any more than the (alternative) least-cost solution, plus an appropriate contribution for the external benefits. To qualify for funding from the broader customer base, external benefits must be additional to any outcomes already mandated by Government and specific to the recycled water scheme(s) in question. Most importantly, a public water utility must demonstrate the broader customer base’s willingness to pay for these external benefits. We consider this approach protects the interests of customers, while also recognising the benefits that recycled water schemes can generate.

### **We recognise benefits from stormwater harvesting and sewer mining**

We have made a draft decision to extend the recognition of avoided and deferred costs to sewer mining and stormwater harvesting customers. This would ensure that the benefits (in the form of avoided or deferred costs) of recycled water investments made by third parties connected to a public water utility’s network are recognised in our cost recovery framework.

Recycled water investments made by third parties can potentially deliver the same benefits to the broader customer base as recycled water investments made by the public water utilities. Recognising these avoided and deferred costs via the cost recovery framework will assist in achieving economic efficiency and consistency with integrated water cycle management principles.

In addition, we have made draft decisions to incentivise public water utilities to seek out opportunities for stormwater harvesting and sewer mining arrangements that could produce significant avoided or deferred costs. We do this by allowing the public water utility to retain 50% of the net avoided and deferred costs, as opposed to passing the full savings through to customers in the form of lower prices.

### **We take a more responsive and flexible approach to regulation**

Our draft decision is to adopt a **more responsive and flexible** approach to regulating prices for recycled water, sewer mining and stormwater harvesting services.

We have made a draft decision to defer regulation and only step in and determine maximum prices for these services when there is a need to. This approach provides public water utilities with more flexibility in how they deliver recycled water services. It also maintains protection to customers through the credible threat that we will intervene, where necessary.

Specifically, our draft approach to regulating recycled water and related services is as follows:

- ▼ For voluntary recycled water schemes, sewer mining and stormwater harvesting, we encourage unregulated pricing agreements and would step in when warranted to set prices under scheme-specific reviews.
- ▼ For mandatory recycled water schemes, we will monitor prices and would step in and set scheme-specific prices during the course of a broader price review where we deem that a public water utility's pricing approach is inconsistent with our pricing principles.<sup>2</sup>

We have also revised our recycled water pricing principles and developer charges methodology to be less prescriptive, allowing for more flexibility for prices to be set in a manner that reflects the purpose and users of the scheme.

### **We have designed our draft framework to be dynamic and flexible**

This review replaces our 2006 Guidelines<sup>3</sup> and the accompanying determination of recycled water developer charges. It also replaces our 2011 Guidelines<sup>4</sup> on assessing the level of avoided or deferred costs arising from water recycling schemes that could be allocated to the broader customer base.

We are proposing that the guidance set out in our Draft Report will be reflected in our *Guidelines for Water Agency Pricing Submissions* as the key reference document for guidance on matters such as the evidence required to demonstrate external benefits, avoided costs, willingness to pay, and prudent and efficient expenditure.<sup>5</sup>

We intend for our guidance to evolve over time as IPART and the public water utilities gain more experience in the implementation of the framework, and in particular, in the development and assessment of claims for avoided and deferred costs, and in demonstrating customer willingness-to-pay to the external benefits of recycled water.

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<sup>2</sup> The element of effective choice is the principal criteria in determining whether we would consider a recycled water scheme mandatory (ie, ability to opt-in to and opt-out of recycled water).

<sup>3</sup> IPART, *Pricing arrangements for recycled water and sewer mining – Sydney Water Corporation, Hunter Water Corporation, Gosford City Council and Wyong Shire Council - Final Report*, September 2006.

<sup>4</sup> IPART, *Assessment Process for Recycled Water Scheme Avoided Costs*, January 2011

<sup>5</sup> The latest version of these guidelines is IPART, *Guidelines for Water Agency Pricing Submissions*, April 2018, which can be accessed here

<https://www.ipart.nsw.gov.au/Home/Industries/Water/Public-water-utilities-we-regulate/Link-documents/Guidelines-for-Water-Agency-Pricing-Submissions-November-2018>