

FACT SHEET

IPART's approach to the Determination

Based on *Review of prices for the Water Administration Ministerial Corporation*
February 2011

IPART's approach

IPART has taken a 'building block' approach to determining water management prices. This involved:

- ▼ establishing the efficient operating and capital costs of the NSW Office of Water (NOW) for the delivery of its monopoly services
- ▼ determining the share of these costs that should be paid by water users, using the 'impactor pays' principle
- ▼ allocating costs to different valleys and between regulated, unregulated and groundwater sources
- ▼ setting the split between fixed (entitlement) charges and usage charges
- ▼ determining forecasts for entitlement and usage volumes to set entitlement and usage charges
- ▼ establishing the efficient, incremental cost of specific activities such as meter services and transaction consents, and setting separate charges for these activities
- ▼ considering impacts on users, and making relevant adjustments
- ▼ establishing a reporting framework for NOW.

This fact sheet provides a brief summary of this approach. Detailed information is available in IPART's Determination and Final Report.

All prices presented in this fact sheet are shown in \$2009/10. Actual prices charged in each year will increase in line with inflation.

Establishing NOW's efficient costs

NOW made several submissions to IPART about its proposed operating and capital costs for the review period. IPART conducted an extensive review of NOW's submissions and determined that NOW could recover \$110 million from users over the 3-year period. This is around 41% less than the forecast in NOW's submission. The main reasons for the difference between NOW's submission and IPART's Determination are:

- ▼ IPART has assessed that NOW could be more efficient in delivering core services. IPART has allowed efficient operating costs of \$53 million by 2013/14, about 24% less than NOW's proposal.
- ▼ NOW did not provide sufficient information to justify increasing the users' share of costs for activities associated with the Murray-Darling Basin Authority. The total cost of these activities to be met by users has been maintained at current levels.
- ▼ NOW proposed an additional 16 activities associated with meeting the requirements of the Commonwealth water reforms. IPART has accepted that the costs of only 5 of these 16 activities should be recovered from users. The remaining activities were not consistent with the Monopoly Services Order, or were considered inefficient or not consistent with best practice water management, or were being funded by other parties.

- ▼ NOW sought to recover depreciation and the cost of capital for past capital investments. IPART's investigations found that NOW's asset management and planning systems were inadequate to allow recovery through prices of past investments. IPART's Determination only includes depreciation and the cost of capital on efficient and prudent investments made after 1 July 2011.
- ▼ NOW proposed that its prices be set to recover the total user share of its costs (ie, 100%). However, to help mitigate the impact of price rises on water users, IPART's Determination sets prices so that NOW's estimated level of cost recovery transitions from 88% in 2009/10 to 94% in 2013/14.

Establishing the user share of costs

NOW's costs are shared between users and the Government on the basis of the 'impactor pays' principle. As with previous Determinations, this means that costs are allocated to users according to the contribution they make to the cost being incurred. Each of NOW's activities were analysed, and costs have been allocated between users and the Government on a case by case basis for each activity.

Allocating costs to different valleys and water sources

NOW does not record costs on a valley by valley basis. To assign costs to each valley, NOW identified key cost drivers for each activity. Costs associated with the Murray-Darling Basin and Commonwealth water reforms have not been allocated to coastal regions.

NOW proposed to allocate groundwater costs to 'coastal' and 'inland' regions, instead of valleys, and to set 'coastal' and 'inland' groundwater prices accordingly. IPART accepted this proposal, as it reflects NOW's cost drivers associated with managing groundwater, the limitations in available data, and the fact that in some regions groundwater sources are not confined to a valley. The Determination includes a transition towards

common prices for coastal and inland groundwater users.

NOW proposed a different method of allocating costs for this Determination. IPART views this new approach as being more robust and transparent than the method used in the 2006 Determination. This method change means that the price changes in the Determination vary between the valleys.

Establishing the 2-part tariff

IPART's Determination establishes a '2-part tariff' for all users that have a meter (as defined in the Determination). This 2-part tariff has been set so that NOW recovers 70% of forecast revenue from fixed charges based on entitlement volume, and 30% from charges based on metered usage from all valleys, except the North Coast. Where a water user does not have a meter, IPART's Determination sets a 1-part fixed charged based on entitlement. In its submission, NOW proposed that all costs be recovered from fixed charges.

Users with a meter, (as defined in the Determination) who are not currently subject to a 2-part tariff should advise NOW in writing of certain details to ensure that they are billed correctly.

In addition to the 2-part tariff, IPART has set prices for the minimum bill, supplementary groundwater and floodplain harvesting.

Establishing entitlement and usage forecasts

IPART has used estimates of entitlement in each valley based on information provided by NOW.

Usage forecasts in regulated rivers have been based on a 20-year rolling average of extractions. This is consistent with IPART's recent State Water Determination.

NOW did not provide reliable usage forecasts for unregulated rivers and groundwater sources. IPART has assumed that 100% of entitlement will be used, which is consistent with available water determinations for these water sources. This

assumption generates price outcomes that are favourable to users.

The total entitlement volumes of Hunter Water and the Sydney Catchment Authority have been included when allocating costs and setting prices for the Hunter and South Coast. This is in contrast to the 2006 Determination, which set prices for the Sydney Catchment Authority and Hunter Water based on usage.

Meter service and reading charges and consent transaction charges

IPART's Determination sets new meter service and reading charges, which relate to the costs of reading all meters and maintaining government-installed meters in unregulated rivers and groundwater areas. These charges range from \$105 to \$679 per meter.

NOW proposed increasing fees for processing consent transactions such as approvals. IPART's Determination includes costs for these activities that are reasonable and efficient.

IPART has recommended that NOW undertakes a thorough cost-benefit analysis of its policy objective to meter 95% of licensed extraction. NOW should also publish clear criteria for decision-making about what meter type is installed where, to ensure that it adequately considers minimising future operating costs to be paid by users.

Considering impacts on users

IPART acknowledges that the price increases in many water sources and regions are significant. To help mitigate the impact of increases on users, IPART has set prices so that annual increases in bills for users with assumed usage patterns should not exceed 20%.

Establishing a reporting framework for NOW

NOW has been unable to respond adequately to concerns relating to systems and performance that IPART raised in its last Determination. IPART has made recommendations about improvements to NOW's financial and reporting systems and its approach to consulting with stakeholders. The Determination establishes a reporting framework for NOW, which aims to ensure that NOW improves the transparency of its expenditure and outcomes achieved.

Where to find more information

To obtain a copy of IPART's Report, or for further information, please visit www.ipart.nsw.gov.au or call (02) 9290 8472.