

Pricing of backlog sewerage services for Gosford City Council

Issues Paper



IPART

**INDEPENDENT PRICING AND
REGULATORY TRIBUNAL**
of New South Wales

Pricing of backlog sewerage services for Gosford City Council

Issues Paper

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Submissions must be made in writing and should be sent to the postal address, fax number or email address below. Where possible submissions should be provided in a computer readable format (eg, word processor, PDF or spreadsheet) either on disk or by email.

Submissions from water agencies should be received by 16 September 2005

Submissions from other stakeholders should be received by 30 September 2005

Submissions should be sent to:

Review of Backlog Sewerage Services
Independent Pricing and Regulatory Tribunal
PO Box Q290
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Email: ipart@ipart.nsw.gov.au

Submissions will be treated consistent with the *Privacy and Personal Information Act 1998*.

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Special reference must be made to any issues in submissions for which confidential treatment is sought and all confidential parts of submissions must be clearly marked. *However, it is important to note that confidentiality cannot be guaranteed as the Freedom of Information Act and section 22A of the Independent Pricing and Regulatory Tribunal Act provide measures for possible public access to certain documents.*

Public Information about the Tribunal's activities

Information about the role and current activities of the Tribunal, including copies of latest reports and submissions can be found on the Tribunal's website at www.ipart.nsw.gov.au.

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1 THE REVIEW

The Independent Pricing and Regulatory Tribunal (the Tribunal) is conducting a review of pricing arrangements for backlog sewerage services in the Gosford City Council area of operations.

In July 1997, the Tribunal determined a methodology for fixing backlog sewerage capital contributions under section 13A of the *Independent Pricing and Regulatory Tribunal Act (1992)* (the IPART Act).

On 14 March 2005, the Minister for Energy and Utilities wrote to the Tribunal outlining additional project costs for backlog sewerage customers due in part to recent changes to the Country Towns Water Supply and Sewerage (CTWSS) Program in the Gosford area in the order of \$6,000 per property.

The Minister noted that these costs represent a significant additional impost on property owners within the backlog sewerage areas of Gosford City and that these costs may be seen as inequitable when compared with residents in the Sydney Water area of operations.

To address this concern the Minister requested that the Tribunal re-open its 1997 determination of backlog sewerage services in order to examine spreading the additional backlog sewerage costs associated with the reduced CTWSS subsidy over the entire Gosford Council customer base.

Given that it has now been eight years since the original determination was made, the Tribunal has decided that it would be appropriate to review its 1997 determination of backlog sewerage services in light of current circumstances.

The Tribunal has decided to limit its review to those backlog communities within the Gosford City Council area of operations by reviewing only Determination 4.2, 1997.

The review is being conducted under Section 11 of the *Independent Pricing and Regulatory Tribunal Act 1992* (the IPART Act).

1.1 Submissions

This Issues Paper is intended to help Gosford City Council and interested parties prepare submissions to this review. The issues raised in this paper are those the Tribunal considers to be relevant for assessing potential changes to the methodology for fixing backlog sewerage capital contributions for customers currently covered by Determination 4.2 of 1997.

1.2 Matters to be considered

When setting prices for water businesses the Tribunal addresses broad social concerns and specific agency matters, as required by Section 15 of the IPART Act.

The broader issues include:

- **consumer protection** – protecting consumers from abuses of monopoly power; standards of quality, reliability and safety of the services concerned; social impact of decisions; effect on inflation
- **economic efficiency** – greater efficiency in the supply of services; the need to promote competition; effect of functions being carried out by another body
- **financial viability** – rate of return on public sector assets including dividend requirements; impact on pricing of borrowing, capital and dividend requirements of agencies
- **environmental protection** – promotion of ecologically sustainable development via appropriate pricing policies; considerations of demand management and least cost planning.

Many of these factors are pertinent to the provision of reticulated sewerage in sewer backlog areas and will therefore be explored further in this review.

1.3 Context

The 2006 review of backlog sewerage services takes place at a time of broader Government consideration of, and consultation on, strategies to manage the growing supply/demand imbalance of water.

In addition, this review will form part of the Tribunal's consideration on its 2006 review of water, wastewater and stormwater prices for Gosford City Council and Wyong Shire Council which will set prices for the period commencing 1 July 2006.

1.4 2006 determination of prices for water, wastewater and stormwater services

Having set prices for water, wastewater and stormwater services for Gosford City Council and Wyong Shire Council for the period 1 July 2005 to 30 June 2006, the Tribunal will shortly commence a review of prices to apply for the period commencing 1 July 2006.

Should the Tribunal's review of pricing arrangements for backlog sewerage services identify the need for a new methodology for fixing the backlog sewerage capital contribution charges for Gosford Council customers, it is the Tribunal's intention that any new pricing arrangements will apply from 1 July 2006 to coincide with the new prices for water, wastewater and stormwater services.

2 REVIEW PROCESS

As part of its public consultation process, the Tribunal invites submissions from water businesses and other interested parties. Submissions should address issues raised in this paper as well as any alternative options for the pricing of backlog sewerage services that stakeholders consider appropriate.

The Tribunal will hold a public hearing to discuss issues raised in this paper, in Council's submission and by other key stakeholders. Submissions and other materials will also be made publicly available on the Tribunal's website.

The proposed timetable for the review is as follows:

Action	Date
Release of Issues Paper	5 August 2005
Gosford submission due	16 September 2005
Stakeholder submissions due	30 September 2005
Public hearing	14 October 2005
Final report	December 2005

Please note that the above dates are indicative and are subject to change.

3 WHAT ARE BACKLOG SEWERAGE SERVICES?

Backlog sewerage services refer to the provision of environmentally acceptable sewage management services in urban areas that are served by a water authority where these services are not available.

The provision of sewerage in urban and semi-urban areas is important for the protection of the environment and maintenance of public health. Benefits from these projects are often shared by all, not just those in the communities concerned. In the past, backlog communities were often physically isolated which meant that there were substantial costs involved in providing sewerage services to these communities.

In many cases, backlog sewerage residents are already connected to the water system and have their own on-site sewerage system. However, there are a number of backlog areas which may be served in the future which are not connected to either a water or sewerage system at all. In the past, on-site sewerage systems represented an acceptable waste management option. However, increasing urban density and a greater appreciation of environmental impacts means that better waste management measures are often called for.

The key task for the Tribunal during this review will be to determine how prices for backlog sewerage services should be set to best balance the competing objectives of consumer protection, economic efficiency, financial viability and environmental protection.

3.1 Environmental benefits arising from the provision of backlog sewerage services

Backlog communities are often communities which are relatively isolated and for which the provision of sewerage services does not involve simple extension of the existing reticulation system. The provision of sewerage infrastructure represents an important community investment in the protection of the environment and the maintenance of public health.

In 1999 the then Environment Protection Authority (EPA) undertook an environmental assessment of the impacts and human health risks of 64 unsewered areas within the Sydney, Hunter, Gosford and Wyong areas. This environmental assessment ranks the identified unsewered areas based on an assessment of the likely environmental and human health impacts taking into account the existing sewage management arrangements. Each unsewered area was assessed against key environmental parameters and allocated an "A", "B" or "C" environmental ranking, where A is the highest environmental priority for the provision of sewerage services.

The EPA's environmental assessment ranked unsewered areas according to the following categories:

- **Category A (High environmental ranking).** The receiving waters are a sensitive environment (drinking water catchment, primary contact recreation area, or of high ecological value) and are currently degraded, or a significant risk is posed, by inadequate sewage management. System upgrade is considered to result in significant environmental improvements and a significant reduction in human health risks.
- **Category B (Medium environmental ranking).** Present sewage management arrangements are contributing to the degradation of the receiving waters, but not

resulting in a significant impact. System upgrade could result in some environmental improvement and a reduction in human health risks.

- **Category C (Low environmental ranking).** Present sewage management arrangements represent only a minor contribution to the degradation of receiving waters, with minimal environmental impact or human health risk. Marginal improvements would derive from sewerage system upgrade.

Given that the communities of Mooney Mooney, Cheero Point and Brooklyn/Dangar Island have all been classified as Category A backlog projects, the Hawkesbury Villages system upgrade is expected to result in significant environmental improvements and a significant reduction in human health risks.

The towns of Little Wobby, Patonga Creek, Bar Point and the unsewered areas in Benseville, Empire Bay and South Kincumber were also classified as Category A backlog projects.

For this reason, it will be important for the Tribunal to ensure that any changes that it makes to the pricing arrangements for backlog sewerage services do not discourage connection to the sewerage system.

4 HISTORY OF PRICING OF BACKLOG SEWERAGE SERVICES

In the mid-1970s, Gosford City Council established a regional sewerage scheme which continued until the mid 1990s. This scheme applied to a defined area in and around Gosford for which the eventual provision of water and sewerage services was planned

For the 20 year period between the mid 1970s and mid 1990s, residents located within this defined sewerage financing scheme area were required to pay “sewerage loan charges” regardless of whether or not they were connected to the Gosford sewerage system on the assumption that they would eventually be connected to the system. Many residents who were initially within the Gosford sewerage financing scheme area paid sewerage loan charges for up to 20 years.

Initially, it was Gosford Council’s intention that only properties inside the area covered by this scheme would be provided with sewerage services from loan scheme funds and the Tribunal’s 1997 determination of backlog sewerage services was set to take account of this situation.

While the sewerage financing scheme area covered the majority of the Gosford area of operations, there were some remote communities on the periphery which were not included. These included; Fishermans Parade, Mooney Mooney, Cheero Point, Little Wobby, Bar Point, Patonga Creek, and areas within Bensville, Empire Bay and South Kincumber.

In the mid 1970s, these communities were isolated from the major metropolitan centres of the Central Coast and for this reason were not to be connected to the metropolitan water or sewerage system. Many properties in these areas were purchased on the assumption that “on-site” water and wastewater systems would be required and residents of these communities were not required to pay sewerage loan charges to Council.

Growth on the Central Coast and more stringent public health and environmental guidelines for on-site wastewater systems during the late 1990s resulted in building approval difficulties for some of these communities (eg, Fishermans Parade) and calls to provide sewerage services to these communities.

To address this issue, the Tribunal considered backlog sewerage services in 1997. The Tribunal’s determination is discussed further below.

4.1 1997 Determination of Backlog Sewerage Services

In 1997, the Tribunal provided its view on what it considered to be appropriate principles for the pricing of backlog sewerage services.

The Tribunal noted that backlog sewerage prices should be based on only efficient costs and that backlog sewerage service providers should not be entitled to charge more than required for efficient service provision. In addition, the Tribunal noted that by setting cost reflective prices, the correct pricing signals in relation to resource utilisation would be sent to customers.

In making its 1997 determination of backlog sewerage services, the Tribunal considered each of the following:

- the pricing principles for water and sewerage services adopted by the Council of Australian Governments (CoAG)
- the objective of full cost recovery
- the efficient costs of service provision
- the potential for private sector involvement in the provision of backlog sewerage services
- the “polluter versus beneficiary pays” principle, and
- the idea that backlog sewerage services are a “public good” as they offer benefits for the wider community.

The 1997 determination consists of two parts, Determination 4.1 and Determination 4.2. Each sets a methodology for fixing the backlog sewerage capital contribution charge payable for the provision of backlog sewerage services, but reflects an attempt by the Tribunal to treat customers covered by Gosford regional sewerage financing scheme differently to those customers in remote communities who are now required to connect to the Gosford sewerage system for public health or environmental reasons.

Key features of the Tribunal’s 1997 determination of backlog sewerage services were as follows:

- The cost of capital works associated with the provision of sewerage in backlog areas should be recovered from users or beneficiaries of these services (Determinations 4.1 and 4.2).
- The methodology applied to backlog sewerage areas in which the provision of the backlog sewerage services delivers substantial environmental and public health benefits to both the local and the wider community (Determination 4.1).
- Where substantial environmental and public health benefits flow to the wider community, a maximum of 25 percent of the capital costs of backlog projects would be recovered from local residents who directly benefit from the projects via the capital contribution charge while the remaining capital costs were to be paid by the wider community via an increase in the common sewerage charge (Determination 4.1).
- The Tribunal considered that the EPA, acting in consultation with the NSW Department of Health, should be the arbiter of the environmental and public health risks associated with a particular project. Ideally, backlog sewerage projects would form part of an overall program of environmental improvement which would be approved by the Government after consideration of the relevant priorities and the costs involved (Determinations 4.1 and 4.2).
- Operating costs for backlog sewerage projects should be recovered through the annual sewerage charge common to all customers (Determinations 4.1 and 4.2).
- The backlog sewerage capital contribution charge:
 - was capped and fixed at \$3,000 per property (Determination 4.1 only) to ensure affordability and to minimise disincentives to connect to the new sewage management system.

- could either be paid up-front or by instalments over a period of up to 20 years (Determinations 4.1 and 4.2). Any amount outstanding as a result of extended time payment was to attract interest at a rate equivalent to the interpolated secondary market NSW Treasury Corporation 10-year bond rate (including any appropriate fees) for an organisation with a similar credit rating to the water agency under consideration.
- To ensure transparency, the increase in the common sewerage charge attributable to backlog scheme costs could be separately identified in sewerage bills (Determinations 4.1 and 4.2).
- Fishermans Parade in Gosford was considered a special case because residents had not contributed to a specific financing scheme for sewerage in past years. These residents were therefore required to pay for the full cost of the scheme. The Tribunal determined that charges for the provision of water and sewerage to areas where residents had not contributed to a specific water and/or sewerage financing scheme should be worked out according to the Tribunal's developer charges methodology (Determination 4.2).

4.1.1 Determination 4.1

The first part of the Tribunal's 1997 determination of backlog sewerage services (Determination 4.1) sets a methodology under Section 13A of the IPART Act for fixing the backlog sewerage capital contribution charge for Sydney Water Corporation, Hunter Water Corporation (excluding properties listed under the HWC Sewerage Priority Area 1), Gosford Council (excluding areas where residents have not contributed to a specific water/sewerage financing scheme) and Wyong Council.

The methodology specified in Determination 4.1 applies to backlog sewerage areas in which the provision of the backlog sewerage services delivers substantial environmental and public health benefits to both the local and the wider community. The backlog sewerage capital contribution charge (BSCCC) is calculated according to the following formula:

$$\text{BSCCC} = \frac{25\% \text{ of actual capital cost of sewerage infrastructure attributed to backlog properties}}{\text{Total number of existing properties in the backlog area}}$$

Determination 4.1 specifies that the backlog sewerage capital contribution charge for any property, as calculated by the above formula is to be capped at \$3,000 in nominal terms until otherwise determined by the Tribunal. In addition, the capital costs used in the calculation are to be net of funding from special environmental levies and if the capital works are undertaken to provide sewerage service to existing backlog properties, renewal of existing infrastructure or new development lots, the capital costs should be apportioned according to the best estimation of lot production.

The Determination requires that the backlog sewerage capital contribution charge be calculated on completion of the sewerage infrastructure and that the agency should submit the calculated charge to the Tribunal for review and gazettal.

To assist in managing customer impacts, Determination 4.1 provides that the following payment options will be available to affected land owners:

1. A special backlog sewerage annual charge. This special annual backlog sewerage charge will be calculated based on an amortisation method to recover the backlog

sewerage capital contribution charge due at the time of connection over a period of up to 20-years. The interest rate used in the amortisation calculation will be the interpolated secondary market NSW Treasury Corporation 10-year bond rate at the time of availability of sewerage services. At any time, the total of all outstanding special backlog sewerage annual capital charge instalments may be paid in a lump sum. The lump sum payable in this case may be calculated as the net present value of all outstanding special backlog sewerage annual charge instalments, calculated at the same interest rate used in the initial amortisation calculation.

2. A one off payment of the full backlog sewerage capital contribution charge at the time of sewerage connection.

The methodology for calculating the backlog sewerage capital contribution charge, and the pricing principles for backlog sewerage outlined in Determination 4.1 apply to:

- All unsewered areas identified by Sydney Water Corporation, and Hunter Water Corporation except areas specified in the Hunter Sewerage Project Priority Area 1.
- Gosford City Council, excluding areas where residents have not contributed to a specific water and/or sewerage financing scheme, and Wyong Shire Council.

4.1.2 Determination 4.2

Part 2 of the Tribunal’s 1997 determination covers specific communities not captured under Determination 4.1. Determination 4.2 sets maximum prices for the provision of water and/or sewerage services for existing properties in and around Gosford where property owners have not contributed to a specific water and/or sewerage financing scheme.

Determination 4.2 specifies the backlog sewerage capital contribution charge payable by affected landowners prior to connection to Gosford City Council’s water and sewer mains. It specifies that a Net Present Value (NPV) methodology is to be used by Gosford City Council to calculate the maximum water and/or sewerage contribution charge and that this methodology is to be the same as the NPV methodology decided by the Tribunal in its 1996 determination of developer charges (Determination No 3.1, 1996).

The formula used to calculate the backlog sewerage capital contribution charge is specified as follows:

$$\text{BSCCC}^1 = \frac{\text{NPV}_k - \text{NPV}(r-c)}{\text{NPVI}}$$

Where:

- NPV_k = NPV of the costs of the assets used to service the Backlog area
- NPV_r = NPV of the future periodic revenues
- NPV_c = NPV of the future annual operating costs
- NPV_I = NPV of the number of Lots in the Backlog area

¹ The backlog sewerage capital contribution charge for a scheme is calculated upon connection to the system and this charge applies for the duration of the scheme. A new backlog sewerage capital contribution charge is not calculated on an ongoing basis.

The water and/or sewerage contribution charge is to be calculated on completion of the sewerage infrastructure and requires that Gosford City Council submit the calculated charge to the Tribunal for review and gazettal.

To assist in managing customer impacts, Determination 4.2 provides two payment options for affected land owners as follows:

1. A special annual water and/or sewerage rate over a 20-year period. This special annual water and/or sewerage rate will be calculated based on an amortisation method to recover the water and/or sewerage contribution charge due at the time of connection. The interest rate used in the amortisation will be the interpolated secondary market NSW Treasury Corporation 10-year bond rate at the time of availability of water or sewerage services.
2. A one off payment of the full water and/or sewerage contribution charge at the time of water and/or sewerage connection.

This determination has applied since July 1997 and has not been reviewed since it was introduced. The Tribunal is aware that the circumstances of some communities and subsidies payable by the NSW Government may have changed sufficiently to warrant a review of the above pricing arrangements.

4.2 Government Priority Sewerage Program (PSP) program

In response to the Tribunal's 1997 determination of backlog sewerage services, the EPA identified a number of communities which it considered a high priority for the provision of sewerage services.

This classification identified areas where the provision of backlog sewerage services would deliver a substantial environmental and public health benefit to both the local and wider community and forms the basis of the Government's Priority Sewerage Program (PSP).

The EPA classification not only covered communities within the Gosford sewerage financing scheme area but also covered communities outside this area such as Mooney Mooney and Cheero Point and SWC communities such as Brooklyn and Dangar Island.

These communities were all classified as Category A (high priority) indicating that substantial environmental and public health benefits would be realised through providing these communities with similar sewerage services to those already provided in the greater metropolitan area of Gosford City.

Council subsequently included Mooney Mooney and Cheero Point on its future program of works with the intention being that these communities would eventually be provided with access to the Gosford sewerage system.

4.3 Country Towns Water Supply and Sewerage (CTWSS) Program

The provision of water supply and sewerage services to country towns in NSW is the responsibility of Local Government under the *Local Government Act (1993)*. The NSW State Government provides technical, management and financial support to Local Government through the Country Towns Water Supply and Sewerage (CTWSS) Program administered by the Department of Energy and Utilities (DEUS) formerly the Department Land and Water Conservation (DLWC).

Under the Program, Local Government Councils and DEUS effectively become partners to deliver appropriate affordable and well managed water supply and sewerage services in urban areas of country New South Wales. These services are necessary to meet community needs, protect public health and achieve sustainable environmental outcomes whilst making best use of regional resources.

In New South Wales, the partnership between State and Local Governments in the provision of water supply and sewerage infrastructure is necessary to protect public health in rural areas. From time to time changes are made to the CTWSS Program to reflect changes in the emphasis of Government policy and the financial capacity of Government relative to the demands on the CTWSS Program. The overall objectives of the CTWSS Program remain to help councils achieve a broad range of objectives such as:

- **Planning and management.** Achieve and maintain best practice in community consultation, strategic planning, financial planning, environmental management, demand management and total asset management.
- **Operation and maintenance.** Achieve and maintain best practice in operation and maintenance of water services, and in the management of emergencies, to provide agreed levels of customer service and environmental protection.
- **Provision of capital works.** Provide physical infrastructure to cost-effectively meet community needs in urban areas in a timely manner whilst protecting environmental values and making best use of regional resources.

Under the CTWSS Program, the NSW Government has committed to increasing the emphasis given to initiatives aimed at helping councils improve their planning and operational management.

The Government also aims to encourage councils to implement sound management practices (such as appropriate demand management and asset management practices, pay for use tariffs and developer charges) and it also provides direct financial assistance for capital works towards “backlog” works including the provision of initial services to unserved towns.

4.4 Sewer management at Fishermans Parade

In the mid to late 1990s more stringent public health and environmental controls for on-site wastewater systems meant that for many residents in the remote community of Fishermans Parade on the outskirts of the Gosford area of operations, building approvals were becoming increasingly difficult to obtain. In response to these difficulties, many residents requested that Council provide access to the sewerage system.

Given that the residents of Fishermans Parade had not contributed to the Gosford sewerage financing scheme, there was a need to treat these customers separately from other backlog sewerage customers. To deal with this situation the Tribunal created Determination 4.2.

Under Determination 4.2, these customers were required to pay a maximum water and/or sewerage contribution charge calculated using the Net Present Value (NPV) methodology similar to that used in the determination of developer charges.

Given that some of the residents in Fishermans Parade had an adequate on-site sewerage system, a decision to force all residents to connect to the Gosford sewerage system was likely to result in some debate.

Council consulted with the residents of Fishermans Parade extensively and determined that a majority of residents were in favour of connecting to the sewerage system. It therefore decided to build the necessary infrastructure and all customers were required to connect to the system and pay the full developer charge (less any Government subsidy) set by the Tribunal.

In the past, Gosford Council has received financial assistance under the CTWSS Program for capital works associated with the provision of backlog sewerage services to communities not initially included in the Gosford sewerage financing scheme.

While residents in Fishermans Parade were provided with access to both the water and sewerage system, funding received under the CTWSS Program was limited to sewerage only up to a maximum of \$210,000 or 50 per cent of the total project cost (whichever was the lower).

As a measure to minimise the customer impacts associated with the large capital contributions required by residents of Fishermans Parade and to maintain equity across the remainder of the Gosford area of operations, the Tribunal's determination allowed residents to pay the full cost of connection in instalments over a period of 20 years.

Given that the communities of Mooney Mooney and Cheero Point are directly comparable with that of Fishermans Parade and that many of the residents of Fishermans Parade are still paying (and will be for many years to come) the full cost of connection as instalments, any decision to change Determination 4.2 would need to be made only after careful consideration of the equity implications within the Gosford area of operations.

5 RECENT DEVELOPMENTS

Since the mid 1970s the Gosford area of operations has continually been expanded. Many residents who are now included within its regional boundary were at the time not intended to be connected to the water and sewerage system and have therefore not contributed to the funding of the system through sewerage loan charges.

While there are a number of remote communities in and around Gosford for which the provision of water and sewerage services is planned, the most advanced of these schemes is the sewer augmentation works currently being undertaken in the Hawkesbury Villages of Mooney Mooney and Cheero Point.

Council have recently advised that they also intend to provide sewerage services to Little Wobby. Little Wobby will not form part of the joint scheme due to its relative isolation. However, it is anticipated that it will be serviced in conjunction with contracts for Mooney Mooney and Cheero Point.

Council advise that funding under the CTWSS Program for Mooney Mooney and Cheero Point has been approved by the Minister for Energy and Utilities but at this stage, no approval for funding under the CTWSS Program has been obtained for any other backlog project.

5.1 Hawkesbury Villages Gosford/SWC joint works

Gosford Council is currently investigating/undertaking a joint scheme with SWC to build a sewerage treatment plant which will service communities in both the Gosford area of operations (eg, Mooney Mooney and Cheero Point) and also communities within the SWC area of operations (eg, Brooklyn-Dangar Island).

The proposed treatment plant is intended to allow high quality effluent discharge to the Hawkesbury River at the F3 road bridge.

This scheme currently covers 151 lots in Mooney Mooney and 71 lots in Cheero Point. The estimated number of future lots is 185 and 83 for Mooney Mooney and Cheero Point respectively. Gosford Council estimates that the total cost of the scheme (Council's share) will be in the order of \$6.1m.

5.2 Government funding to apply under PSP and CTWSS Program

Currently, Mooney Mooney and Cheero Point which lie on the Central Coast side of the Hawkesbury River qualify for a subsidy under the Government's Priority Sewerage Program (PSP) and also under the NSW Government's Country Towns Water Supply and Sewerage (CTWSS) Program.

After the Tribunal made its determination in 1997, the Government made available under its Priority Sewerage Program a subsidy of approximately \$3,000 per property for communities in which the provision of backlog sewerage services would deliver substantial environmental and public health benefits to both the local and the wider community.

The funding available to Gosford City Council under the Priority Sewerage Program is summarised in Table 1 below:

Table 1 Priority Sewerage Program Funding

Location	Number of lots	Funding
Bar Point	≤ 138	\$414,000
Bensville, Empire Bay, South Kincumber	≤ 79	\$237,000
Little Wobby Beach	≤ 82	\$246,000
Mooney Mooney, Cheero Point	≤ 249	\$747,000
Patonga Creek	≤ 59	\$177,000
TOTAL	≤ 607	\$1.821m

In addition, for similar communities in the Gosford area of operations the Government also committed to pay a subsidy under the NSW Government's Country Towns Water Supply and Sewerage Program of up to two thirds of the required capital contribution for each property connecting to the sewerage system.

This meant that upon connection to the Gosford sewerage system, communities on the Gosford side of the Hawkesbury River would receive a \$3000 subsidy under the PSP program as well as a subsidy up to two thirds of the required capital contribution under the CTWSS Program.

Recently, the NSW Government reviewed the arrangements for the CTWSS Program. For Communities within the Gosford area of operations (such as Mooney Mooney and Cheero Point) connecting to the water and sewerage system, this meant that the subsidy payable under this scheme would be reduced from approximately two thirds of the required capital contribution to one half.

Council estimate that the reduction in the Country Towns subsidy is likely to translate to an increase of approximately \$3,000 per property such that the required backlog sewerage capital contribution (calculated using the developer charge methodology) payable (the unsubsidised amount) by the residents of communities such as Mooney Mooney, Cheero Point will increase from about \$8,000 to \$10,000 per property to \$11,000 to \$13,000 per property².

Council has not yet obtained approval for funding under the CTWSS Program for the provision of sewerage services to Little Wobby.

² GCC submission to 2005 IPART Metropolitan Water Price Review - October 2004.

5.3 Variation in capital contribution payable by Hawkesbury Villages residents

Given that Mooney Mooney and Cheero Point lie within the Gosford area of operations and residents have not paid sewerage loan charges in the past, these communities are currently covered by the Tribunal's determination 4.2.

Communities on the SWC side of the Hawkesbury River such as Brooklyn and Dangar Island are covered by Determination 4.1. This means that while these communities are located physically close to each other (ie, across the Hawkesbury River), the capital contribution charge payable by residents in each of these communities is calculated very differently.

As outlined above, Determination 4.1 requires that residents on the SWC side of the Hawkesbury River will be required to pay a backlog sewerage capital contribution charge up to a maximum of \$3,000 per property and the NSW Government has committed to pay this charge under the PSP Program on behalf of residents.

Determination 4.2 requires that residents on the Central Coast side of the Hawkesbury River meet the cost of connection to the sewerage system by paying a capital contribution charge which is calculated using the developer charges methodology as outlined in section 4.1.2 above.

Currently under determination 4.2, residents on the Central Coast side of the Hawkesbury River have the option of paying a one off payment of the full water and sewerage contribution charge at the time of water and/or sewerage connection or a special annual water and/or sewerage rate over a 20 year period. This special annual water and/or sewerage rate is calculated based on the amortisation method to recover the water and/or sewerage contribution charge due at the time of connection.

While this situation is in line with the Tribunal's current determination of backlog sewerage services and maintains equity within the Gosford area of operations, the Minister for Energy and Utilities is concerned about the potential inequality in charges payable by SWC and Gosford residents and also that the additional costs associated with the reduction in the Country Towns subsidy represent a significant impost for Hawkesbury Villages residents.

This is particularly evident where in some cases, properties located within sight of each other will be required to make substantially different capital contributions upon connection to the same system.

6 OPTIONS FOR PRICING OF BACKLOG SEWERAGE SERVICES FOR GOSFORD COUNCIL

In late 2004, Gosford Council identified that changes to the CTWSS Program would likely mean substantial increases in the capital contribution charges payable by backlog residents in communities such as Mooney Mooney and Cheero Point. On 29 October 2004, Gosford Council wrote to the Tribunal seeking its view on a proposal to spread costs associated with the reduced CTWSS Program subsidy and new EPA requirements for higher quality effluent over its customer base in the form of higher sewerage charges generally.

Council note that this would generate a cross subsidy of at least \$2.57m³ as customers within the Gosford area of operations who have previously paid sewerage loan charges would be required to pay some of the costs associated with connecting customers who have not. While the communities of Mooney Mooney and Cheero Point have been the focus of attention to date, this is primarily due to the fact that pre-construction works are most advanced in these areas.

The communities of Little Wobby, Bar Point, Bensville, Empire Bay, South Kincumber and Patonga Creek are also included under the Priority Sewerage Program and any decision by the Tribunal could potentially be applied to these communities as well.

The Minister for Energy and Utilities has since requested that the Tribunal re-open its 1997 determination of backlog sewerage services in order to examine spreading additional backlog sewerage costs associated with the reduced CTWSS subsidy over the entire Gosford Council customer base.

To provide a starting point for its review of backlog sewerage services, the Tribunal has presented two potential options for pricing of backlog sewerage services in Gosford. These options are provided to stimulate discussion only and do not represent the only options that the Tribunal will consider.

In considering each of these options the Tribunal will need to have regard for the following:

- The financial implications for the majority of the Gosford Council customer base.
- The financial implications for backlog sewerage customers (such as those living in the Hawkesbury Villages).
- Implications for land values of unsewered backlog properties upon connection to the sewerage system.
- The potential for creation of undesirable cross subsidies.
- Economic efficiency.
- Gosford Council's financial viability.
- The implications for the environment.

³ GCC letter to IPART, 29 October 2004.

6.1 Option1 – Maintain status quo

The first option for pricing of backlog sewerage services in Gosford which will be considered by the Tribunal represents no departure from the methodology outlined in the Tribunal’s 1997 determination of backlog sewerage services (Determination 4.2).

Under the current arrangements for the provision of backlog sewerage services, existing Gosford Council customers would not be required to make any additional contribution towards the provision of sewerage services for backlog communities such as the Hawkesbury Villages while existing Gosford Council customers who have made significant capital contributions to their water and sewerage system through the Gosford sewerage loan scheme will continue to be charged a standard sewerage service charge as determined by the Tribunal during its reviews of periodic charges.

Under this option, residents in communities such as Fishermans Parade would continue to be charged a standard sewerage service charge as well as a special annual water and/or sewerage rate over a 20 year period as per Determination 4.2 (unless the resident chose to pay a one off payment of the full water and sewerage contribution charge upon connection to the system).

Under Option 1, all existing customers would be no better or worse off and residents in backlog sewerage areas who wish to connect to the sewerage system would still be required to pay the capital contribution charge calculated under the current determination of backlog sewerage services (Determination 4.2).

The recent Government decision to reduce the subsidy payable under the CTWSS Program means that backlog customers connecting to the sewerage system are now required to pay significantly more than would otherwise have been the case.

The following table compares the indicative capital contribution charge for Mooney Mooney and Cheero Point residents prior to the Government’s changes to the CTWSS Program with the capital contribution required under the new arrangements.

Table 2 Comparison of capital contribution charge for Mooney Mooney, Cheero Point customers (\$2005/06)

	Once-off payment at time of sewerage connection (\$/property)	Annual instalment over 20 years (\$ per annum)
Required capital contribution (with two thirds CTWSS subsidy)	\$8,062	\$703
Required capital contribution (with one half CTWSS subsidy)	\$11,881	\$1,036

As can be seen above, changes to the Government’s CTWSS Program means that the total amount paid by residents of Mooney Mooney and Cheero Point upon connection to the sewerage system has increased significantly. Such an increase would significantly increase the disparity in capital contribution charges payable by Gosford and Sydney backlog customers.

While Option 1 does not address the variation in capital contribution required between Gosford and Sydney backlog customers, it would avoid the creation of undesirable cross subsidies between residents of Gosford City and Gosford backlog customers and ensure sufficient funds are available for Council by requiring backlog customers to make capital contributions which are cost reflective.

The Tribunal is also aware of the implications for land values of previously unsewered backlog properties upon connection to the sewerage system. Once a property is connected to the sewerage system, owners of backlog properties are likely to benefit from very large increases in property values, which in some cases could represent a substantial windfall gain to residents. The Tribunal would seek to avoid a situation where the backlog sewerage charges that it set considerably advantaged one group of customers while significantly disadvantaging another.

Pricing of backlog sewerage services below cost could potentially encourage unsustainable growth in backlog areas and promote undesirable environmental outcomes.

The Tribunal would welcome comments on Option 1 – maintaining the status quo.

6.2 Option 2 – Special rate for Mooney Mooney and Cheero Point

The second option to be considered by the Tribunal will examine the potential costs and benefits of offering the residents of Mooney Mooney and Cheero Point special treatment by reducing the capital contribution required upon connection to the sewerage system.

Such an option would assist in addressing the Minister's concerns in relation to the variation in capital contribution required by backlog residents in Gosford and SWC's area of operations when connecting to the Gosford or Sydney sewerage system. However, it should be noted that there may be additional backlog communities within the Gosford area which are in a similar situation to Mooney Mooney and Cheero Point (such as Little Wobby) but who will not be covered by these arrangements.

In addition, should the Tribunal decide to determine a special rate for Mooney Mooney and Cheero Point residents, Council would not generate sufficient revenue to cover the costs of this backlog program. This shortfall in revenue could be addressed through recovering the revenue shortfall from the remainder of the Gosford customer base.

This option was initially raised by Gosford Council in a letter to the Tribunal on 29 October 2004 and subsequently proposed by the Minister for Energy and Utilities on 14 March 2005.

Under option 2, it may be possible for the Tribunal to cap the backlog sewerage capital contribution payable by backlog sewerage customers at a predetermined amount and recover the remainder of the revenue required by Gosford Council for the construction of the backlog project through a small increase in the general sewerage service charge (currently \$363.99) payable by all Gosford Council customers.

While this option would address the Minister's concern, it has the potential to create a cross subsidy between existing Gosford sewerage customers and Gosford backlog sewerage customers. The Tribunal will need to consider the equity implications of requiring existing customers who have already paid for their own sewerage system to subsidise the costs of other (often more expensive) residents' sewerage systems.

Option 2 seeks to directly address the variation in backlog sewerage capital contribution required between backlog sewerage residents in Gosford and SWC's area of operations by reducing the capital contribution payable by Mooney Mooney and Cheero Point residents. Under this option, only those additional costs associated with the reduced CTWSS subsidy would be spread across the remainder of the Gosford Customer base.

However, in doing so, an undesirable cross subsidy between residents of Gosford City and the Gosford backlog customers may be created. Under this option, Gosford City customers would be required to pay for their own sewerage system and also subsidise the sewerage system of backlog customers through an increase in the general sewerage service charge.

Under Option 2, residents in backlog areas will enjoy the benefits of both a subsidised sewerage system and also the very large increases in property values which will result, while existing Gosford customers will be required to pay for their own sewerage system as well as part of the sewerage system in backlog areas.

The Tribunal would welcome comments on Option 2 - Special rate for Mooney Mooney and Cheero Point (ie, spreading of costs across remainder of Gosford customer base).

APPENDIX 1 SECTION 15 REQUIREMENTS

In making determinations the Tribunal is required by the IPART Act (1992) to have regard to the following matters (in addition to any other matters the Tribunal considers relevant):

1. the cost of providing the services concerned
2. the protection of consumers from abuses of monopoly power in terms of prices, pricing policies and standard of services
3. the appropriate rate of return on public sector assets, including appropriate payment of dividends to the Government for the benefit of the people of New South Wales
4. the effect on general price inflation over the medium term
5. the need for greater efficiency in the supply of services so as to reduce costs for the benefit of consumers and taxpayers
6. the need to maintain ecologically sustainable development (within the meaning of section 6 of the Protection of the Environment Administration Act 1991) by appropriate pricing policies that take account of all the feasible options available to protect the environment
7. the impact on pricing policies of borrowing, capital and dividend requirements of the government agency concerned and, in particular, the impact of any need to renew or increase relevant assets
8. the impact on pricing policies of any arrangements that the government agency concerned has entered into for the exercise of its functions by some other person or body
9. the need to promote competition in the supply of the services concerned
10. considerations of demand management (including levels of demand) and least cost planning
11. the social impact of the determinations and recommendations
12. standards of quality, reliability and safety of the services concerned (whether those standards are specified by legislation, agreement or otherwise).

APPENDIX 2 LETTER FROM MINISTER



NEW SOUTH WALES

MINISTER FOR ENERGY AND UTILITIES
MINISTER FOR SCIENCE AND MEDICAL RESEARCH
MINISTER ASSISTING THE MINISTER FOR HEALTH (CANCER)
MINISTER ASSISTING THE PREMIER ON THE ARTS



DEUS Ref: 05/517

Mr James Cox
Chief Executive Officer
Independent Pricing and Regulatory Tribunal
PO Box Q290
QVB POST OFFICE NSW 1230

14 MAR 2005

Dear Mr Cox

I refer to the Tribunal's letter of 8 December 2004 to Gosford City Council regarding capital contributions by residents for backlog sewerage in Gosford City. The properties concerned are all within the Government's Priority Sewerage Program (PSP) where substantial environmental and public health benefits accrue to both the local and the wider community.

The Tribunal's letter notes that in order for the Tribunal to assess whether Council may spread certain additional costs for backlog sewerage projects over its entire customer base, the Tribunal would need to re-open its 1997 Determination of Backlog Sewerage Services in Gosford City (Determination 4.2, 1997). It is understood that Gosford City Council has decided not to request re-opening of this Determination.

The additional backlog sewerage costs have been estimated by Council to be approximately \$6,000 per lot. This is a significant additional impost on those property owners within the backlog sewerage areas of Gosford City, and may be seen as inequitable, particularly when compared with residents in Brooklyn and Dangar Island in the Sydney Water area, as well as the other PSP areas in Sydney, Hunter and Wyong where residents are not now required to pay any up front capital contributions.

Accordingly, it is requested that the Tribunal re-open its 1997 determination in order to examine spreading of the additional backlog sewerage costs over Gosford Council's entire customer base. It would be appreciated if this investigation could be undertaken as part of the Tribunal's 2005 Urban Water Review.

It is understood that in order to provide for the cost of servicing the additional capital cost for all of the PSP backlog sewerage areas in Gosford City, an increase of under \$10/assessment would be required in the annual Gosford residential sewerage bills.

The Tribunal's early consideration of this matter would be appreciated.

Yours sincerely

Frank Sartor

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APPENDIX 3 COMPARISON OF CURRENT ARRANGMENTS FOR PRICING OF BACKLOG SEWERAGE SERVICES

Table A3.1 Comparison of pricing arrangements for backlog sewerage properties in NSW

Property type	SWC	HWC		GCC		WSC
	All unsewered areas	HWC Sewerage Project Priority Area ¹	Other unsewered properties in HWC area of operations	Contributed to GCC Sewerage Financing Scheme ²	Did not contribute to GCC Sewerage Financing Scheme	All unsewered areas
No strong environmental and health benefit would result from connection	Not covered by Det. 4.1 or 4.2. Resident to pay full developer charge upon connection.	Not covered by Det. 4.1 or 4.2. All HWC customers to pay annual Environmental Improvement Charge	Not covered by Det. 4.1 or 4.2. Resident to pay full developer charge upon connection.	Not covered by Det. 4.1 or 4.2. Resident to pay full developer charge upon connection.	Covered under Det. 4.2. Resident to pay full developer charge upon connection.	Not covered by Det. 4.1 or 4.2. Resident to pay full developer charge upon connection.
Strong environmental and health benefits would arise from connection (EPA classification - Category A)	Covered under Det. 4.1. Resident to pay capital contribution charge specified under Det. 4.1 up to max. of \$3000. NSW Government to meet capital costs up to max. of \$3000/lot.	Not covered by Det. 4.1 or 4.2. All HWC customers to pay annual Environmental Improvement Charge	Covered under Det. 4.1. Resident to pay capital contribution charge specified under Det. 4.1 up to max. of \$3000. NSW Government to meet capital costs up to max. of \$3000/lot.	Covered under Det. 4.1. Resident to pay capital contribution charge specified under Det. 4.1 up to max. of \$3000. NSW Government to meet capital costs up to max. of \$3000/lot	Covered under Det. 4.2. Resident to pay full developer charge upon connection.	Covered under Det. 4.1. Resident to pay capital contribution charge specified under Det. 4.1 up to max. of \$3000. NSW Government to meet capital costs up to max. of \$3000/lot

Notes:

1. The HWC Sewerage Project was initiated by the NSW Government and HWC in the late 1980s to address environmental problems arising from the sewerage backlog on the fringe of HWC's operational area. The NSW Government decided that a CSO would fund 50 per cent of the capital costs and the remaining 50 per cent would be funded by HWC. In June 1996, the Tribunal determined that HWC's share should be funded equally by an 'Annual Environmental Improvement' charge payable by residents.
2. GCC established a regional sewerage scheme in the mid-1970s. Properties serviced by the Sewerage Financing Scheme paid "loan charges" to fund the works for up to 20 years. Properties outside the sewerage financing scheme area were not intended to be connected to the sewerage system and therefore were not required to pay sewerage loan charges. Determination 4.2 is designed to deal with customers in this situation.