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Enquiries to: Damian O'Doherty

26 August 2011

Mr. Andrew Chow  
Director, Water and Local Government  
Essential Services Commission  
Level 2, 35 Spring Street  
Melbourne VIC 3000

Dear Andrew

### WANNON WATER'S RESPONSE TO THE COMMISSION'S TARIFF ISSUES PAPER

Please find attached Wannon Water's contribution to the Commission's 2013 Water price Review-Tariff Issues Paper.

Yours sincerely



**Grant Green**  
Managing Director



26<sup>th</sup> August 2011  
Reference C2011/08205

Submission to 2013 Water Price Review – Tariff Issues Paper  
Essential Services Commission  
Level 2  
35 Spring Street  
Melbourne VIC 3000

Wannon Water provides the following response to the questions raised within the 2013 Water Price review – Tariff Issues Paper.

***Do the proposed principles adequately address the WIRO and other relevant requirements in relation to pricing matters?***

The proposed principles articulated by the Commission are considered to adequately address the WIRO.

Wannon Water notes that the 2013 Water Price review – Tariff Issues Paper (“Tariff Issues Paper”) states that the Commission has a preference for a two part water tariff structure comprising a fixed charge and a volumetric component to recover the business’s revenue requirement.

In the current regulatory period Wannon Water charges its residential customers an Inclining Block Tariff for water volume. The first tier quantum is based on a typical household’s essential water needs and the tariff charged is at a discount, the middle tier aligns with the water volume charge for business and other non-residential customers whilst the third tier is set as a surcharge for profligate use.

Wannon Water considers that the tiered volume concept may have contributed to the significant reduction in average household water consumption in the current regulatory period, down from 164 kilolitres in 2008/09 to 134 kilolitres per annum in 2010/11.

It is noted that the Essential Services Commission will accept either a one or two part tariff structure for sewerage services. Wannon Water’s past experience of volumetric sewerage tariffs was that estimating the sewerage volume discharged to the sewerage system was problematic, overly complex and was subject to many assumptions which were difficult to explain to customers. As a result, Wannon Water moved to a fixed sewerage service fee to provide the necessary revenue requirement

***What amendments – changes or additions – are needed to ensure the principles are clear, useful and applicable in the 2013 Water Price Review?***

The principles should include as a primary statement that Water Corporation tariffs must be in accordance with the Water Industry Regulatory Order. In the present Commission principles this is an unstated underlying assumption.

***Are there any other matters that we will need to consider in applying these proposed principles?***

A potential issue is that the Ministerial Advisory Council recommends that the State Government mandate that a minimum percentage of water billing being derived from the volumetric tariff. If so this would not be consistent with the Essential Services Commission’s preference for the volumetric water tariff price to be based on the Long Run Marginal Cost. In circumstances where major works have been completed in previous regulatory periods (and therefore treated as “sunk” costs) and there are no additional future major works planned, generally a very low value

volumetric price would be derived. Water Corporations will require a clear direction on how this potential conflict is to be managed in proposed pricing principles.

#### **Form of Price Control- Section 4**

##### ***What tariff innovations could be proposed for the 2013 Water Price Review period?***

There may be some merit in offering customers the opportunity to buy “green water” – i.e. providing customers with the option of including a surcharge on a customer’s bill to enable Wannon Water to purchase green power with which to supply water. Wannon Water’s water supply systems are relatively energy intensive.

##### ***What are the implications for the form of price control?***

Wannon Water is comfortable with current individual price cap methodology given the stability of its water supply. However, a significant proportion of supply is made to major commercial customers who are actively seeking alternative water supplies. Consequently Wannon Water would welcome the ability to move to a revenue cap during the next determination in the event of a significant change in demand due to the loss of major industrial customers.

##### ***How will equity implications of tariff changes be managed?***

Wannon Water is concerned that scarcity pricing has the potential to disadvantage the security of supply for customers who do not have the financial means to pay a higher tariff option to gain access to a more secure supply of water. Increasing the security of supply for one category of customers may disadvantage other customers connected to the same water system.

Consequently if a scarcity pricing tariff option was offered to customers, consideration should be given to a lower tariff option for customers receiving a Government pension entitlement.

##### ***Are there any significant cost forecasting uncertainties for water retailers, such as demand or variable bulk supply costs? If so, what are the appropriate mechanisms for managing these risks?***

Wannon Water’s principle concern relates to the bulk supply from GWMWater, which supplies from Rocklands to Hamilton and Balmoral, with a further small system supply to Glenthompson. The pricing for these GWMWater systems is regulated by the Essential Services Commission and changes in bulk supply charges will need to be accounted for in setting Wannon Water’s tariff charges for the Hamilton, Balmoral and Glenthompson water systems.

#### **Questions Retail tariffs Section 5.2**

##### **Comment**

This section discusses the variability of volumetric bulk water costs and the impact on retail tariffs. Management of the impact is generally either a pass through approach or some form of smoothing. Apart from the supply of water from Rocklands Reservoir to the Balmoral and Hamilton systems, the impact of variability in bulk supply prices is of minimal interest Wannon Water.

The Tariff Paper also considers postage stamp pricing, and questions whether this methodology reflects the true distribution costs, and whether proper investment decisions can be made when the retail price is distorted.

Wannon Water currently charges differential tariffs across its water and sewerage systems to better reflect the cost of operating and maintaining the separate systems. A social equity cap on

tariffs levied on customers in systems servicing smaller communities was applied as passing on the full cost of such systems would have delivered a severe price shock.

The Commission is seeking true innovation in tariff structures and promoting the concept of Water Corporations providing customers with choice in the tariff with particular emphasis on “scarcity pricing”. Again at this time, and for the next determination period, Wannon Water will not experience a shortage of water supply, and hence it is unlikely that any customer would “take-up” a higher price tariff option to guarantee supply in times of scarcity.

The concept of a customer paying for and then exercising the right to use water in excess of restrictions imposed on neighbours would take some considerable understanding by the community. It removes water as a commodity for the common good, to one of a luxury good for the moneyed and privileged. This would be a major philosophical shift in thinking not only for Water Corporations but the communities they serve.

***What are the implications of increased variability and uncertainty in bulk water costs for retail tariff structures and levels?***

In respect to Wannon Water the implications are minimal at the local level due to the small percentage of bulk supply taken from another Corporation provided those charges are fair and equitable.

***Are there net benefits in reflecting differences in distribution system costs by time or location in retail tariffs?***

There are costs in providing for peak demand and hence there maybe some benefit in both “locational” and timing tariffs to recognise this aspect. On the other hand systems are sized to meet peak demand, the cost of which is sunk. In addition there are few variable costs that would not be incurred if the water use was constant over a longer period (i.e. not subject to peaks). The complication in billing and the cost of same would need to substantially reduce to warrant the benefit of customers varying the time of their use.

***Are there any factors that would support a water business’s default retail water tariff not being a two-part tariff?***

Yes, the default tariff should be influenced by the historical tariff and by the outcomes of customer consultation.

***What approach should we take to innovations to default tariff offerings?***

If the Essential Services Commission is serious about encouraging innovation, then it can not set the tariff type in advance, but rather set the philosophy that the customer should not be disadvantaged, and nor should the remaining customers be disadvantaged by the necessity to cross –subsidise the innovation.

***Are businesses in a position to be able to offer choice to water customers?***

Subject to the outcome of customer consultation, Wannon Water does not intend to offer tariff choice to water customers. Scarcity pricing is not relevant to Wannon Water customers as more than 80% of Wannon Water customers have never been subjected to water restrictions beyond the Permanent Water Savings Measures.

Wannon Water does intend to consult with customers on options for choice regarding billing frequency.

***What constraints are there in offering a choice in water tariffs?***

The requirement to offer choice should not be imposed on customers or water corporations, rather customers should be consulted as to whether they want the option of having choice. Choice should not be offered to any customer where a choice of options may disadvantage any other customer's entitlements to security of water supply or maintaining their current levels of service.

However, if choice is to be provided, then the principle issues become:-

- a) the Water Corporation's tariff billing system and its ability to provide multiple options,
- b) customer understanding and their ability to select the most appropriate tariff for them, and
- c) the requirement that the Water Corporation's other customers should not cross subsidize the choice.

### **Sewerage and trade waste tariffs \_ Section 5.3**

#### **Comment**

Wannon Water concurs with the Productivity Commission's view that "... it is unlikely that the demand for domestic sewerage services can be influenced by price to the same degree as demand for water overall."

#### ***Are there any issues with regional urban water businesses' sewerage tariffs?***

Wannon Water has sixteen separate sewerage systems which are widely separated. These systems were built on the basis of historical subsidies provided for local solutions.

So an emerging issue for Wannon Water is the cost of localised sewerage systems servicing smaller communities and maintaining cross subsidies in order to mitigate price shocks.

#### ***Do trade waste disposal charges provide the right balance between efficiency, and the ability of customers to respond, simplicity, and equity?***

Yes, as the current principles allow for volume, content, strength and the plant costs associated with the treatment to be taken into account.

### **Recycled Water Charges – Section 5.4**

#### ***Are any changes required in the approach to determining recycled water prices having regard to the experience in the last Price Review period, the proposed pricing principles, the WIRO Regulatory Principles or the NWI pricing principles for recycled water and storm water?***

On the current information available, there does not appear to be any changes required. The future direction will be dependent upon the outcomes from the Ministerial Advisory Council and this position reviewed when the outcomes are available.

### **Melbourne Water Waterways and Drainage Charges - Section 5.5**

This section and its questions are not relevant to Wannon Water and consequently are not responded to.

However, there is the question of how urban storm water may be utilised as an alternate fit for purpose water resource across regional water corporations.

## **Tariffs and Customer Choice – Section 6**

### ***Should the Commission allow water businesses to offer customers choice in tariff offerings?***

In Wannon Water's view – yes the Commission should permit water businesses to offer customer choice in tariff offerings. It may be a new and innovative methodology becomes possible through new technology and the Commission should be prepared to consider new solutions not only for the 2013-18 determination but during that determination period. It would not be expected the revenue requirement would be altered during mid-term, but rather the techniques to allocate the requirement amongst customers might change.

### ***If so, is the Commission's proposal to regulate only default tariffs supported?***

The same level of regulation should be applicable regardless of the tariff option chosen.

### ***What role should the Commission play with respect to alternative tariffs offered by water businesses?***

The same level of regulation should be applicable regardless of the tariff option chosen.

### ***If tariff choice is introduced, what aspects of consumer protection would need to be introduced or enhanced?***

Given that it is a customer choice to opt for an alternative tariff, there shouldn't be special arrangements for additional customer protection because of that choice. The same level of regulation should be applicable regardless of the tariff option chosen.