

6th Screening Workshop

Environmental objectives and exemptions

17 – 19 October 2015

ECRAN 60743

Cost recovery as a non-structural measure within the PoM



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Structure of the presentation

Definitions

Best practice in full cost recovery

WFD Cost recovery

Cost categories

Financial cost



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Definitions (1)

Cost recovery means the generation of sufficient revenues to pay the cost of water and sewage services.

It includes user fees and charges for services that allocate costs to users in an equitable manner and are affordable.

Full cost recovery supports a business plan and funding approach that suits local conditions, sustains water and sewage systems in perpetuity and maintains acceptable service levels for the users of the systems.

Full cost recovery includes concepts of both costs and cost recovery.



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Definitions (2)

Costs include all water and sewage system costs that must be incurred to provide services at sustainable service delivery levels and reflect customer, industry and government service standards.

Costs include operating, maintenance and administration (OM&A) expenditures, land, financial and capital investments to repair, rehabilitate, replace, expand and upgrade facilities; and, in some cases, decommissioning and disposing of infrastructure.

These costs must be recognized and reported.



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Best practice in full cost recovery

The following steps represent :

1. Set goals for what you want to include in a rate setting plan for achieving full cost recovery.
2. Identify components of full costs.
3. Estimate full costs (i.e., over the life of the assets to quantify long-term needs).
4. Conduct gap analysis (i.e., the financial gap between what is being spent and what should be spent).
5. Identify revenue sources and prioritize.
6. Review financing methods and prioritize sources of revenue.
7. Develop a financial plan.
8. Set the rates and charges.
9. Review full costs and the cost recovery plan annually.



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Economic elements of the WFD

- **Cost recovery** is about the amount of money that is being paid for water services, i.e. it answers the question **how much is paid for water**;
- The **polluter-pays-principle** addresses the adequacy of contributions from different water uses to the total cost, based on their role in causing these costs, i.e. it answers the question **who pays for water**;
- **Incentive pricing** deals with the way water users pay for their use, and whether the right price signals are transmitted, i.e. it answers the question **how is water being paid for, and which effects the water price has on the behaviour of water users**.



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WFD – cost recovery

Asses current levels of recovery of costs in accordance to Article 9 of the Water Framework Directive

Objective:

Definition of cost-benefit by sector.



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Tasks

1. Estimates costs of water services, including financial, environmental and resource costs;
2. Estimate the price/tariff currently paid by the users;
3. Assess the extent of cost recovery by water service and sector;
4. Assess the contribution to cost recovery from key water uses;
5. If felt necessary, initiate review of incentive pricing properties of existing tariffs.



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Information base

1. Estimation of financial costs (broken down in operating maintenance and capital costs);
2. Tax transfers, administrative costs and any other costs. (to be evaluated);
3. Environmental and resource costs as required. (to be evaluated);
4. Extent of financial and environmental cost-recovery;
5. If activities initiated for reviewing incentive pricing: current pricing structure and price elasticity, affordability criteria.



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Cost recovery, WFD

„Member States shall take account of the principle of recovery of the costs of water services, **including environmental and resource costs** [.....] and in accordance in particular with the polluter pays principle..

Member States shall ensure by 2010:

an **adequate contribution** of the different water uses, disaggregated into a least industry, households and agriculture,, to the recovery of the costs of water services“ (Art.. 9 (1))..

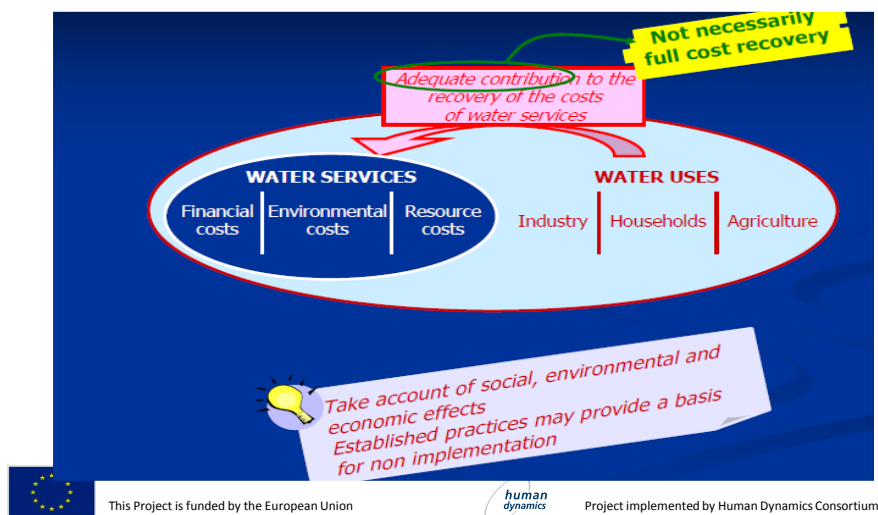


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Cost categories

In order to achieve full cost recovery 3 main categories of cost should be taken into account:

- Financial Cost : operation and maintenance cost
- Resource Cost : Opportunity cost
- Environmental Cost: The cost is created either from the deterioration of water quality from pollution or deprivation of quantity of water from the different uses.



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Financial costs

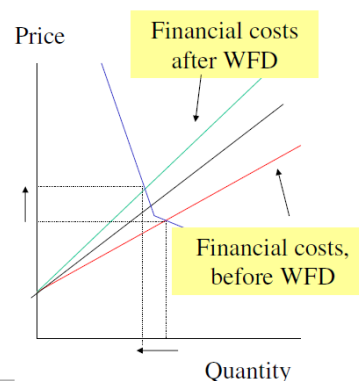
Cost Recovery

What costs:

- Operating costs
- Return of capital
- Return on capital
- Environmental costs
- Resource costs

WFD should internalise these external costs

Long average costs or marginal costs?



What are these costs?



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Ecosystem Services Approach

WFD Article 9 on cost recovery for water services:

The ESA can be used as support for environmental and resource costs assessments, or at least for the identification and characterization of these costs.

Since the consideration of cost recovery is restricted to water services, this excludes some of the activities that strongly impact ecosystem services provision (if, however, the definition of water services is widened, the concept of ecosystem services could be of more significance to this article).

Besides, the ESA can help demonstrate the advantages of the Programme of Measure and encourage local operators and stakeholders to implement it.



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Programmes of measures (Art.11 WFD)

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Under Article 11 of the WFD, EU Member States will need to develop a Program of Measures (POM) for each River Basin District (RBD) taking into consideration the results of characterisation of the particular river basin.

A POM may include actions such as:

- measures to manage specific pressures arising from: forestry, agriculture, industry, etc;
- control regimes or environmental permitting systems;
- water demand management measures;
- **economic instruments such as incentives**, taxes on fertilisers, etc;
- river restoration strategies, etc.
- Any measure or policy instrument that is targeted at changing water prices (both for water supply / abstraction and for water pollution) would need to be included in the programme of measures.



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Thank you!



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