

Water and Waste Regulatory Office

Waste Collection Tariff Policy

December 2007

Water and Waste Regulatory Office

Mission

“Water and solid waste utilities delivering a consistent, good quality and efficient service to all customers throughout Kosovo.”

Vision

“To regulate the water and solid waste sectors in a transparent and equitable manner in accordance with good European practice which ensures that the water and solid waste utilities deliver a qualitative, sustainable, reliable and affordable service throughout Kosovo, with respect for both the environment and for public health.”

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1. INTRODUCTION

1.1 Rate setting provisions of the WWRO Regulation (UNMIK Regulation No. 2004/49)

This policy, issued by the Water and Waste Regulatory Office (WWRO), presents the WWRO's interpretation and elaboration of its statutory obligations with respect to regulated tariffs for waste collection services.

In particular, Section 38 of the WWRO Regulation (*Rules Issued by the Regulator*) requires the WWRO to create rules for the setting and approving of tariffs. This policy is the foundation upon which such detailed rules can be developed.

Section 10 of the WWRO Regulation prescribes certain tariff obligations including:

- Consultation process (10.2)
- Expectations of efficiency (10.3 b), and
- Sufficiency to meet capital and recurrent costs (10.3 d)

The statutory obligations as set out in the WWRO Regulation permit a degree of regulatory discretion based upon professional judgement, understanding of the regulated entities (and their specific circumstances) and other socio-economic criteria.

Following an initial consultation process in May 2007 and subsequent representations from stakeholders this draft policy statement has been prepared.

1.2 Objectives

The interests of the various stakeholders do not necessarily coincide; for example consumer interest in low tariffs is in conflict with investor interest in financial sustainability. It is the function of the WWRO to ensure that the tariffs provide an optimum balance between these interests and ensure the best possible value, including tariff and improved quality of service for society. This Tariff Policy is designed to deliver this best overall balance.

2. JURISDICTION

2.1 Public owned enterprises (POEs)

This policy document is based upon the current institutional environment whereby the seven regional POEs are the sole

licensed providers of waste collection services. Although there are several unlicensed (private) waste collection service providers operating within Kosovo their activities are generally confined to the collection of waste from non-domestic (commercial, industrial and institutional) customers, such activities are operating in and tariffs are set by an openly competitive market and as such a regulatory Tariff Policy does not apply to them. The POEs, however, are responsible for the collection of waste from domestic households and those non-domestic customers not served by the private sector. These POEs operate in a monopoly environment and as such the tariffs for services are regulated by the WWRO in accordance with Regulation 2004/49. This Tariff Policy is therefore confined to the activities of the POEs. A principal feature of this Tariff Policy is, however, to promote competition in the sector. The proposals herein are therefore designed to remove, where possible, market distortions thereby opening up the sector to wider competition. It is recognised that the institutional framework for waste (collection and disposal) is under review and any changes therein may require subsequent changes to this Tariff Policy.

WCPS 1: Jurisdiction

This Tariff Policy applies to the activities of POEs only and does not apply to the activities of private service providers operating in a competitive market.

3. PRINCIPAL TARIFF POLICY OPTIONS

3.1 Social fairness and tariff structures

3.1.1 POEs' role with respect to social responsibility

Regulation 2004/49 (Section 10.3 (f)) states that tariffs shall be determined with regard to 'the responsibility of the Provisional Institutions of Self-Government, not the service providers, to help low-income Customers pay their invoices'. Consequently, the POEs should be allowed to operate on a fully commercial basis.

WCPS 2: Social responsibility

The Government (local and central) is the agency responsible for meeting the needs of disadvantaged including helping them to meet the costs of public services.

3.1.2 Uniformity of tariffs

It is recognised that the costs of waste collection may vary between POEs owing to utilisation of available resources, economies of scale and other factors. It is however, inequitable to vary tariffs for the same service within a POE's defined area regardless of the costs of service. Therefore it is appropriate for a uniform tariff structure to be applied throughout each POE's service area.

WCPS 3: Uniformity of tariffs

Tariffs shall be uniform throughout each POE's service area for similar services.

3.1.3 Levels of service

The domestic (and in some cases non-domestic) waste collection services fall into two basic categories: those that enjoy an individual service, e.g. individual houses, and those that employ communal services, e.g. apartment dwellers. It is therefore appropriate to apply two different tariffs to reflect these two different levels of service, the tariff for the individual service higher than that of the communal service to reflect the differences in costs. This Tariff Policy therefore supports, but does not obligate, the POEs to apply different tariffs for these two clearly identifiable levels of service.

WCPS 4: Levels of service

Each POE may elect to adopt a two tier tariff structure to reflect the costs of individual and communal waste collection services.

3.1.4 Fixed and variable charges

WCPS 5: Fixed and variable charges

Domestic households shall be subject to a fixed monthly charge for waste collection services whereas non-domestic customers shall be charged on the basis of either a fixed charge or a volumetric charge, the latter based upon a rate per container (variable depending upon the size of the container)

3.2 Cost recovery

3.2.1 Definition

The short-run nature of the waste collection business including short-life assets effectively makes the accounting definition of cost recovery the simplest and most viable definition.

WCPS 6: Definition of cost recovery

Cost recovery is defined in an accounting sense where revenues are balanced by all costs on an annualised basis. Costs include direct operational costs, depreciation, interest and other attributable costs in accordance with Kosovo or International Accounting Standards.

3.2.2 Time taken to achieve full cost recovery

Waste collection operates in a market where there is open competition and should therefore operate on a full cost recovery basis immediately. Postponing cost recovery is a market distortion and will discourage competition.

WCPS 7: Time frame for attainment of cost recovery

Cost recovery is an immediate objective

3.2.3 Efficiency expectations

As the POEs are operating in a competitive market the levels of efficiency should be comparable to their competitors. Tariffs should therefore be based upon realistic market levels of efficiency.

WCPS 8: Efficiency improvement expectations

The WWRO shall determine tariffs based upon efficiency improvement expectations in line with realistic private sector efficiency levels.

3.2.4 Recovery of capital investment costs

Due to the short run nature of waste collection assets (maximum of 10 years) and the low levels of expected inflation in a EURO currency environment simple historic cost depreciation is considered to be an appropriate vehicle for the return of capital.

WCPS 9: Recovery of capital investment costs

Capital investment shall be incorporated in tariffs by the passing through of full historic cost depreciation.

3.2.5 **Grants and gifted assets**

The POEs enjoy the position of owning gifted assets (or assets financed through grants). Such facilities give the POEs unfair advantage over their competitors. However, such distortions are short-term in nature as new replacement assets will need to be purchased through their own financial resources. It is therefore appropriate to allow depreciation on such gifted and/or grant financed assets to pass through to the tariff even if this gives the POEs cash flow revenues that are not enjoyed by their competitors. In the medium term such distortions will automatically fall away.

WCPS 10: Treatment of grants and gifted assets

The POEs shall be entitled to include depreciation on gifted and grant financed assets in their tariff structure.

3.3 **Capital structure, value and return**

3.3.1 **Capital structure**

Conventional economic theory rules that capital structure has no bearing on the performance of a business and as such the capital structure is a POE management issue rather than a regulatory concern. Consequently, the return on capital (once applicable) shall be based upon a return on total capital value irrespective of capital structure. In the very short term, prior to full cost recovery, the WWRO shall recognise the existing debt obligations of the POEs (interest and repayment of principal) in setting tariffs.

WCPS 11: Capital structure

In the very short term, prior to full cost recovery, the WWRO shall consider capital structure in setting tariffs in order to protect cash flow. Once full cost recovery is achieved the WWRO shall consider the capital structure of the POEs as a matter for their management and no longer considered as a regulatory concern

3.3.2 **Capital value and return on capital**

The competitive nature of the waste collection business does not demand the application of special regulatory capital valuation rules. The value of capital and the return on that capital should be based upon competitive market principles reflecting the value

of the investments and the risk related investor expectations of return.

WCPS 12: Capital value and return on capital

The capital value of the POEs shall be determined on the basis of their total capital (assets including working capital) and the return on capital shall be based upon market expectations of returns for similar risk investments.

3.3.3 Working capital

The working capital requirements of POEs will directly impact on the cash flow of the organisations and as such will need to be recognised in the tariff of services. Furthermore, once a return on capital is permitted to pass through to the tariff the value of capital upon which a return can be earned should include the working capital requirements of POEs.

WCPS 13: Working capital

The cash flow stream for POEs shall allow for any changes in working capital requirements. Once full cost recovery is attained and a return on capital is included in the tariff of services working capital shall be included in the total capital upon which a return can be earned.

3.3.4 Taxation

WCPS 14: Taxation

Non-recoverable taxes shall be included in tariffs. When a return on capital is included in tariffs it shall be determined on a 'post-tax' basis.

4. PROCESS

4.1 Major tariff reviews

WCPS 15: Major tariff reviews

For the year 2007/8 tariffs shall be determined on an annual basis in which time the Tariff Policy can be developed with a complete set of rules that can facilitate longer periods between reviews.

4.2 Interim reviews

In accordance with Regulation 2004/49 section 10.5 the WWRO shall review tariffs annually or 'at any other time the rules or an agreement with the Service Provider specify'. The WWRO shall set tariffs tri-annually with the intervening annual review required by the regulation limited to inflationary adjustments and extra-ordinary events.

WCPS 16: Interim reviews

The WWRO shall undertake periodic interim reviews of the tariffs taking into account inflation and any extraordinary changes in the operating environment.