



ACCC Decision

On the exemption of the Lower Murray Water Urban and Rural Water Authority (LMW) from the operation of divisions 2, 3 and 4 of Part 6 of the Water Charge Rules 2010

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1. Decision

The ACCC has decided to grant the Lower Murray Water Urban and Rural Water Authority (LMW) an exemption from the operation of the requirements of divisions 2, 3 and 4 of Part 6 of the *Water Charge Rules 2010* (WCR).

This is because the ACCC has considered the matters under subrule 23C(5) and is satisfied that the application of the requirements in divisions 2, 3 and 4 of Part 6 to LMW would not materially contribute to the achievement of the Murray-Darling Basin (the Basin) water charging objectives and principles set out in Schedule 2 of the *Water Act 2007 (Cth)* (the Water Act) (see **Attachment A**).

2. Introduction

On 1 July 2020, rule changes came into effect, consolidating three existing sets of water charge rules into the WCR and changing the regulation of infrastructure operators under Part 6 of the WCR (see section 3 below). The amended rules give effect to the policy intent that the approval or determination of the infrastructure charges of infrastructure operators is largely achieved by Basin States under Basin State law, where Basin State regulatory approaches ensure that relevant infrastructure operators' costs are prudent and efficient and infrastructure charges are set at levels that would not allow the operator to earn monopoly returns.

On 8 September 2021, LMW notified the ACCC of its belief that it was a Part 6 operator and, at the same time, applied for an exemption from the operation of the requirements of divisions 2, 3 and 4 of Part 6 of the WCR.

In a separate decision, the ACCC has formed the view that LMW will be a Part 6 operator under rule 23 of the WCR after 30 June 2023 (see the ACCC's decision on the classification of LMW under Part 6 of the WCR, available on the ACCC's website, for more information).

As LMW is a Part 6 operator, if the ACCC does not grant LMW an exemption under Part 6 of the WCR, the ACCC will be responsible for approving or determining all of the infrastructure charges levied by LMW for the regulatory period commencing 1 July 2023 unless LMW ceases to be a Part 6 operator before that date.¹

The ACCC may grant an exemption from the operation of the requirements of divisions 2, 3 and 4 of Part 6 only if the ACCC is satisfied that the application of those requirements would not materially contribute to the achievement of the Basin water charging objectives and principles. The ACCC is satisfied of this and has decided to grant LMW's application for an exemption, on the basis of the assessment outlined in section 5.

3. Legal framework

The *Water Charge Amendment Rules 2019*² (the amending rules) amended and combined the *Water Charge (Infrastructure) Rules 2010* (WCIR), *Water Charge (Termination Fees) Rules 2009* and *Water Charge (Planning and Management Information) Rules 2010* into a single set of rules—the WCR.

¹ The infrastructure charges are limited to regulated water charges within the meaning of section 91 of the *Water Act 2007* (Cth) and therefore exclude LMW's charges for urban water supply activities.

² Available at: <https://www.legislation.gov.au/Details/F2019L00521>.

These rules are made under section 92 of the Water Act and apply to all infrastructure operators (operators) in the Basin.

Section 91 of the Water Act limits the scope of charges regulated by the WCR. Subsections 91(2) and (3) of the Water Act mean that the WCR:

- only relate to Basin water resources³
- do not apply to urban water supply activities beyond the point at which the water has been removed from a Basin water resource.

3.1. LMW has been regulated in accordance with accreditation arrangements under the Water Charge (Infrastructure) Rules 2010

Under the former WCIR:

- LMW was a Part 6 operator because it was a non-member owned operator which provided services in relation to more than 250 GL of water access entitlements held by LMW, its customers or the owner of water service infrastructure operated by LMW.⁴
- In the absence of accreditation arrangements under which charges were approved or determined by a State agency, the ACCC was responsible for approving or determining the infrastructure charges⁵ of Part 6 operators (such as LMW).
- In February 2012, the ACCC accredited arrangements to allow the Victorian Essential Services Commission (ESCV) to determine and approve the infrastructure charges of infrastructure operators in Victoria (including LMW) under Part 9 of the WCIR.⁶ These arrangements, which were implemented in Victorian State law through Part 1B of the *Water Industry Act 1994 (Vic)* (the WI Act) required that the

³ Section 4 of the Water Act defines **Basin water resources** means all water resources within, or beneath, the Murray-Darling Basin, but does not include: (a) water resources within, or beneath, the Murray-Darling Basin that are prescribed by the regulations for the purposes of this paragraph; or (b) ground water that forms part of the Great Artesian Basin.

⁴ Subrule 23(1) of the WCIR stated that Part 6 of those Rules applied to an infrastructure operator that is not a member owned operator if the sum of the maximum volume of water from managed water resources in respect of which the operator provides infrastructure services in relation to: (a) water access entitlements held by the operator (otherwise than for the purpose of providing infrastructure services to customers who hold water access entitlements to that water); and (b) water access entitlements held by its customers; and (c) water access entitlements held by the owner (not being the operator) of the water service infrastructure operated by the operator: is more than 250 GL.

⁵ The WCIR and the accreditation arrangements refer to 'regulated charges' rather than 'infrastructure charges'. However, the definition of 'regulated charges' under the previous WCIR is the same as the definition of 'infrastructure charges' under the new WCR. That is, a charge of a kind referred to in paragraph 91(1)(a), (b) or (d) of the Act other than: (a) a fee to which rule 13 of the *Water Market Rules 2009* applies [a transformation application fee]; or (b) a termination fee.

⁶ Part 9 of the WCIR allowed for accreditation arrangements whereby a State agency (such as the ESC) would be responsible for approving or determining the charges of Part 6 operators under the WCIR instead of the ACCC.

ESCV make determinations or approvals under the water charge rules and apply the *Pricing principles for Part 6 approvals or determinations* published by the ACCC.⁷

The ESCV is a statutory authority established under the *Essential Services Commission Act 2001 (Vic)* (the ESC Act). It is Victoria's independent economic regulator⁸ of prescribed essential services.

3.2. LMW's current regulatory period started on 1 July 2018 and expires on 30 June 2023

On 19 June 2018, the ESCV made a determination under section 33 of the ESC Act, pursuant to rule 29 of the WCIR and clauses 10 and 14 of the *Water Industry Regulatory Order 2014 (WIRO)*,⁹ which determined the infrastructure charges¹⁰ which LMW could levy or charge during the regulatory period. This determination took effect on 1 July 2018 and will have effect until 30 June 2023.

3.3. LMW is subject to the transitional provisions for existing Part 6 operators

As:

- LMW was a Part 6 operator under the WCIR immediately before 1 July 2020, and
- the ACCC has formed the view that LMW will be a Part 6 operator under rule 23 of the WCR after 30 June 2023, and
- LMW did not make a transitional application before 1 July 2020¹¹

subrules 81(12) and (13) of the WCR mean that LMW's **transition period** began on 1 July 2020 and ends on the last day of LMW's current regulatory period (that is, the day on which the determination made by the ESCV on 19 June 2018 ends).¹² Therefore, LMW's transition period under the WCR ends on 30 June 2023.

Subrule 81(5) of the WCR means that as LMW's infrastructure charges were determined or approved before 1 July 2020 (on 19 June 2018) in relation to a period after 1 July 2020 (until 30 June 2023) by the ESCV under the accreditation arrangements established under the

⁷ ACCC, Water charge (Infrastructure) rules: accreditation arrangements. Available at: <https://www.accc.gov.au/regulated-infrastructure/water/water-charge-infrastructure-rules-accreditation-arrangements/accreditation-escv>

⁸ Section 12 of the ESC Act provides that the ESCV is not subject to the direction or control of any Minister.

⁹ ESCV 'Lower Murray Water Determination: 1 July 2018-30 June 2023'. Available at: <https://www.lmw.vic.gov.au/wp-content/uploads/2019/03/2018-water-price-review-lower-murray-water-determination-20180619.pdf>. Accessed 6 April 2021. The *Water Industry Regulatory Order 2014* was made under section 4D(1) of the WIA. It is available at: <http://www.gazette.vic.gov.au/gazette/Gazettes2014/GG2014G043.pdf> (starting at page 2485).

¹⁰ The WCIR, the accreditation arrangements and the ESC's determination refer to 'regulated charges' rather than 'infrastructure charges'. However, the definition of 'regulated charges' under the previous WCIR is the same as the definition of 'infrastructure charges' under the new WCR. That is, a charge of a kind referred to in paragraph 91(1)(a), (b) or (d) of the Act other than: (a) a fee to which rule 13 of the *Water Market Rules 2009* applies [a transformation application fee]; or (b) a termination fee.

¹¹ Under subrule 81(2), a **transitional application** is an application by the infrastructure operator for the determination or approval of charges under Part 6 before that was made before 1 July 2020 but where the charges to which the application related were not determined or approved before 1 July 2020.

¹² Subrule 81(3).

WCIR, the ESC's 2018 determination or approval is taken to have been made under Part 6 of the WCR after 1 July 2020.¹³

Because LMW's transition period ends on 30 June 2023, and the ACCC has formed the view that LMW is a Part 6 operator under rule 23 after 30 June 2023, the ACCC must now decide whether to grant LMW an exemption from the operation of divisions 2, 3 and 4 of Part 6.

3.4. The ACCC must decide whether to grant LMW an exemption from the operation of divisions 2, 3 and 4 of Part 6

Subrule 81(12) provides that the ACCC must:

- a) *form a view as to whether the [existing part 6] infrastructure operator is a Part 6 operator under rule 23 as amended by the amending rules, or is likely to cease to be one or to become one before the end of the transition period; and*
- b) *notify the operator of the ACCC's view, and*
- c) *if the ACCC is of the view that the operator is, or is likely to be, a Part 6 operator—advise the operator that the ACCC will decide whether the operator should be granted an exemption from the operation of Divisions 2, 3 and 4 of Part 6 after the end of the transition period.*¹⁴

Subrule 23C(2) provides that the ACCC may grant an infrastructure operator a written exemption from the requirements of divisions 2, 3 and 4 of Part 6 following:

- a) *an application made by the infrastructure operator, or*
- b) *if it has given the infrastructure operator a notice under rule 23B or paragraph 81(12)(b) that it is of the view that the operator is, or will be, a Part 6 operator.*

3.5. The exemption decision must consider objectives and principles and have regard to specified matters

Subrule 23C(4) specifies that the ACCC may only grant an exemption if it is satisfied that the application of the requirements in divisions 2, 3 and 4 of Part 6 of the WCR would not materially contribute to achieving the Basin water charging objectives and principles set out in schedule 2 of the Water Act.

Basin water charging objectives and principles

The water charges rules are intended to contribute to achieving the Basin water charging objectives and principles, contained in schedule 2 of the Water Act. Schedule 2 is based on clauses 64 to 77 of the National Water Initiative (NWI), an intergovernmental agreement between the Commonwealth and the states and territories which set the direction for national water policy.

¹³ Subrule 81(5) provides that: where infrastructure charges of the operator were determined or approved before 1 July 2020 in relation to a period after 1 July 2020 (that is. they were determined or approved under Part 6 as it then stood), the determination or approval is taken to have been made under Part 6 as amended by the amending rules on 1 July 2020

¹⁴ Subrule 81(13) provides that if paragraph (12)(c) applies, the ACCC must decide whether such an exemption should be granted by applying rule 23C as modified by subrule (15) of this rule. Under subrules 81(13) and (15), if the ACCC fails to make a decision within 3 months of receiving an exemption application or giving notice under 81(12)(b) that the ACCC considers that the operator is a Part 6 operator, the ACCC is taken to have decided to grant the operator an exemption from the operation of divisions 2, 3 and 4 of Part 6 for a period of 3 years that begins immediately after the end of the transition period for the operator. Under subrule 81(15)(d) the **regulatory start date** for the operator is taken to be i) for the purpose of the definition of '**regulatory period**' in subrule 3(1) – the date on which the operator's first regulatory period. Subrule 3(1) means the first regulatory period begins on the regulatory start date for the operator.

The water charging objectives are:

- to promote the economically efficient and sustainable use of:
 - a) water resources; and
 - b) water infrastructure assets; and
 - c) government resources devoted to the management of water resources; and
- to ensure sufficient revenue streams to allow efficient delivery of the required services; and
- to facilitate the efficient functioning of water markets (including inter-jurisdictional water markets, and in both rural and urban settings); and
- to give effect to the principles of user-pays and achieve pricing transparency in respect of water storage and delivery in irrigation systems and cost recovery for water planning and management; and
- to avoid perverse or unintended pricing outcomes.

There are 16 water charging principles, divided into four groupings, covering:

- water storage and delivery
- cost recovery for planning and management
- environmental externalities
- benchmarking and efficiency reviews.

The Basin water charging objectives and principles are set out in full at **Attachment A**.

The Basin water charging objectives and principles support achieving the overarching objectives of the Water Act, which include 'promot[ing] the use and management of the Basin water resources in a way that optimises economic, social and environmental outcomes;' and 'achiev[ing] efficient and cost-effective water management and administrative practices in relation to Basin water resources'.

The water charge rules contribute to achieving the Basin water charging objectives and principles by enhancing pricing transparency, providing for economic regulation that gives effect to the principles of cost recovery and user pays pricing, and prohibits key forms of discriminatory charging practices.

Matters to be considered before granting an exemption

In making the decision as to whether to grant an exemption under rule 23C, the ACCC must have regard to the matters specified in subrule 23C(5):

- a) *the total volume of water access rights in relation to which bulk water services are provided by the operator, if applicable;*
- b) *the total volume of water subject to water sharing arrangements in relation to which the operator provides infrastructure services, if applicable;*
- c) *the infrastructure services provided by the operator;*
- d) *any preferences expressed by the operator's customers to the ACCC;*
- e) *any views expressed by a State Agency to the ACCC;*

- f) *whether the relevant law of a State is being transitioned so that the operator's infrastructure charges will at a future date be determined or approved by a single State Agency in a way that is consistent with paragraph 29(2)(b);¹⁵*
- g) *the proportion of the infrastructure operator's revenue to be recovered from infrastructure charges;*
- h) *any other matters that the ACCC considers relevant.*

3.6. The exemption decision must be decided within 3 months

If the ACCC fails to make a decision within 3 months after it received the application, it is taken to have decided to grant the operator an exemption for 3 years from the end of the transition period (WCR rule 81(15)).

4. Consultation

The ACCC conducted public consultation on LMW's exemption application by publishing information on the ACCC website and emailing relevant stakeholders to invite submissions via the ACCC consultation hub. LMW notified its customers using social media and by including information about the ACCC consultation on its website. LMW also presented its application and information on the ACCC decision process, including the consultation, to its rural customer service advisory committees. The consultation ran from 13 September 2021 to 4 October 2021. The ACCC did not receive any submissions directly in response to its public consultation nor indirectly via LMW.

5. Reasons for decision and assessment of matters

In making its decision, the ACCC must have regard to the matters set out under subrule 23C(5) of the WCR and must be satisfied that the application of these requirements would not materially contribute to the achievement of Basin water charging objectives and principles. The remainder of this document sets out how these matters have been considered and gives more detail of the reasons for the decision to grant the exemption.

LMW is only captured as a Part 6 operator because it passes through a bulk water charge

At the outset the ACCC notes that LMW does not provide services of a kind specified in rule 23—that is, it does not provide services for bulk water or in relation to interstate water sharing arrangements. It is a Part 6 operator only because it levies a bulk water charge on its customers as a pass through on behalf of another infrastructure operator.

Although LMW *levies* an infrastructure charge in relation to a bulk water service in respect of water access rights (per subrule 23(b)(i) of the WCR), LMW does not itself *provide* a bulk water service to its customers. The relevant charges relate to services provided by Goulburn-Murray Water (GMW), which manages the Northern Victorian river storages and the infrastructure to convey bulk water to a point where LMW can extract the water for delivery to its customers.

LMW passes-through these GMW bulk water charges to its customers. LMW then remits the revenue back to GMW and money from these storage charges is excluded from LMW's

¹⁵ Subrule 23C(5) notes: For paragraph (f), once that is the case, paragraph 23(a) will cease to apply to the operator, and the operator will no longer be a Part 6 operator.

revenue cap.¹⁶ GMW's entitlement storage fees were approved by the ESCV in its 2018 determinations for LMW and GMW.¹⁷ These charges are based on the customer holding a water access right (a Victorian water share) and relate to the costs of operating and maintaining on-river water storages.¹⁸

LMW's other infrastructure fees do not relate to a bulk water service and would not of themselves result in LMW being a Part 6 operator pursuant to subrule 23(b)(i) of the WCR. However, once an entity is a Part 6 operator by reason of rule 23 of the WCR, each of its infrastructure charges is subject to determination or approval by the ACCC—whether or not that infrastructure charge meets the description in subrule 23(b) of the WCR.

The ACCC considers that the application of the requirements under Part 6 would not materially contribute to the achievement of the Basin water charging objectives and principles

The ACCC considers that regulating some of LMW's charges under Part 6 would not materially contribute to achieving the Basin water charging objectives and principles in comparison to granting an exemption to LMW (which would then be wholly regulated by the ESCV) because the regulatory arrangements that would result under Part 6 would be less efficient, would perpetuate unnecessary regulatory burden and may result in inconsistent or perverse pricing outcomes.

If divisions 2, 3 and 4 of Part 6 apply to LMW, LMW will face regulation by different regulators under two different frameworks, with all of LMW's infrastructure charges that fall within the scope of section 91 of the Water Act regulated by the ACCC, and all of its charges that relate to urban water supply activities regulated by the ESCV. In the ACCC's view this would fail to deliver the intended policy outcomes from the rule amendments, being for a single state regulator to determine a Part 6 operator's charges where State regulation ensures that relevant infrastructure operators' costs are prudent and efficient and infrastructure charges are set at levels that do not allow the operator to earn monopoly returns¹⁹. Further, it would perpetuate unnecessary regulatory burden and would not promote the economically efficient and sustainable use of government resources devoted to the management of water resources.

Victorian arrangements are being transitioned and are likely to meet the requirements of the WCR

The ACCC further notes the Victorian government has taken steps to implement legal and regulatory arrangements that are likely to meet the requirements of the WCR; that is, to require LMW to have all its infrastructure charges determined or approved by a single State

¹⁶ ESCV Lower Murray Water final decision – rural services, 19 June 2018. See: <https://www.esc.vic.gov.au/sites/default/files/documents/2018-water-price-review-lower-murray-water-rural-final-decision-20180619-v3.pdf>. Accessed 28 September 2021

¹⁷ ESCV Lower Murray Water Determination (1 July 2018 – 30 June 2023), 19 June 2018. See: <https://www.lmw.vic.gov.au/wp-content/uploads/2019/03/2018-water-price-review-lower-murray-water-determination-20180619.pdf>. Accessed 7 April 2021

ESCV Goulburn Murray Water Determination (1 July 2020 to 30 June 2024), 3 June 2020. See: <https://www.esc.vic.gov.au/sites/default/files/documents/goulburn-murray-water-price-review-2020-final-decision-20200605.pdf>

¹⁸ LMW. See: <https://www.lmw.vic.gov.au/wp-content/uploads/2020/08/2020-2021-Explanation-of-Tariffs-First-Mildura-Irrigation-District.pdf>. Accessed 7 April 2021

¹⁹ ACCC (2016) Review of the water charge rules – final advice, pp.146; 148. Available at: <https://www.accc.gov.au/regulated-infrastructure/water/water-projects/review-of-the-water-charge-rules-advice-development>

Agency (the ESCV) under a law of the State in a way that would be consistent with subrule 29(2)(b). The ACCC expects that these new arrangements, if the proposed amendments take effect, are likely to result in LMW ceasing to be a Part 6 operator before the start of the next regulatory period.

Some of the amendments to enable the ESCV to determine LMW's infrastructure charges have already been introduced to the Victorian Parliament. The existing ESCV framework, while not identical to the arrangements in Part 6, includes benchmarking requirements and the consideration of efficient costs, which accords with the Basin water charging objectives and principles discussed below.

In summary, the ACCC considers that the regulation of LMW's infrastructure charges under Part 6 would impose unintended and unnecessary regulatory burden and would, accordingly, less materially contribute to achieving the Basin water charging objectives and principles than the granting of an exemption.

5.1. ACCC consideration of matter in subrule 23C(5) of the WCR

In making the decision to grant LMW an exemption from the operation of the requirements in divisions 2, 3 and 4 of Part 6 of the WCR, the ACCC has considered the matters specified in subrule 23C(5) of the WCR, as set out below.

a) the total volume of water access rights in relation to which bulk water services are provided by the operator, if applicable

The total volume of water access rights in relation to which bulk water services are provided by LMW is *zero*. LMW does not provide bulk water services, which are services for the storage and/or delivery of water that is primarily on-river. GMW, as the Northern Victorian Resource Manager, manages the northern Victorian river storages and the infrastructure to convey bulk water to a point where LMW can extract the water for delivery to its customers.

Consideration of this factor weighs strongly towards the view that the application of Part 6 requirements to LMW would not materially contribute to achieving the Basin water charging objectives and principles.

b) the total volume of water subject to water sharing arrangements in relation to which the operator provides infrastructure services, if applicable

The total volume of water subject to water sharing arrangements in relation to which the operator provides infrastructure services is *zero*.

LMW's exemption application states:

As an off-river infrastructure operator LMW does not have any responsibilities in water sharing arrangements.

The Northern Victoria Resource Manager (NVRM) makes seasonal determinations for all northern Victorian regulated river systems including the Goulburn, Broken, Campaspe, Loddon, Bullarook and Murray regulated river systems. The Minister for Water appointed GMW to undertake this role in accordance with Victorian water sharing rules.

Consideration of this factor weighs strongly towards the view that the application of Part 6 requirements to LMW would not materially contribute to achieving the Basin water charging objectives and principles.

c) the infrastructure services provided by the operator

The infrastructure services provided by LMW are the off-river delivery and drainage of water services to its customers in its irrigation districts (it also delivers water to environmental and recreational sites using its off-river infrastructure). That is, LMW extracts water from a natural watercourse (the River Murray) and delivers that water to its off-river customers through a network of channels and / or pipes (both gravity fed and pressurised) in its irrigation districts. LMW also provides drainage services to these customers.

LMW submits that it provides infrastructure services to:

- *2,666 irrigation and 2,240 stock and domestic customers in the four pumped irrigation districts of Mildura, Merbein, Red Cliffs and Robinvale*
- *309 Millewa rural district customers*
- *waterworks district of Yelta.*

LMW submits that it also manages:

- *the extraction of the region's rural bulk water entitlements;*
- *The collection and disposal of subsurface drainage water from the four pumped irrigation districts, as well as from private diverters in Nangiloc, Robinvale and Boundary Bend;*
- *Oversight of irrigation and drainage design in new agricultural developments ensuring conformity with salinity management plan development guidelines;*
- *Management of the private diversion licences of 1,313 water users along the Murray River in Victoria between Nyah and the South Australian border;*
- *The assessment and approval of licensing, water share and allocation trade applications; and*
- *Water supply delivery to important environmental and recreational sites.*

As mentioned above at 5.1(a), LMW does not provide bulk water services. Consideration of this factor weighs towards the view that the application of Part 6 requirements to LMW would not materially contribute to achieving the Basin water charging objectives and principles. The ACCC's final advice described the policy intent of the proposed Part 6 arrangements as being directed to the regulation of on-river operators where no Basin State mechanism for direct approval or determination of an operator's charges was in place, or where the infrastructure operator provided services across multiple jurisdictions.²⁰

d) any preferences expressed by the operator's customers to the ACCC

The ACCC did not receive any submissions from LMW customers in response to consultation. LMW submits that it has not obtained nor has an indication of preferences expressed from its customers.

During the development of the ACCC's advice on the water charge rules (upon which the WCR are based), the Victorian Farmers Federation (VFF) argued that it was important that the charges of the large, Victorian infrastructure operators (including LMW) be subject to regulatory approval/determination. The VFF argued that 'proper and appropriate' regulatory oversight is important and that it was important that the quality of the regulatory oversight not

²⁰ ACCC (2016) Review of the water charge rules – final advice, pages142-3 Available at <https://www.accc.gov.au/system/files/ACCC%20Review%20of%20the%20water%20charge%20rules%20-%20Final%20Advice.pdf>.

be diminished.²¹ The VFF was of the view that this was ensured through having Part 6 as a fall back in the absence of state regulation.

In relation to the VFF's previously expressed view the ACCC notes that LMW's infrastructure charges will continue to be regulated by the ESCV under the accreditation arrangements currently in place for the duration of the current regulatory period. Further, as stated in section 5, the ACCC expects that arrangements will likely be in place before 30 June 2023 for the ESCV to regulate all of LMW's charges in a manner that is likely to meet the test in rule 29(2)(b). As such, consideration of customer preferences – in particular, the views of the VFF – do not weigh against granting an exemption.

e) any views expressed by a State Agency to the ACCC

The Essential Services Commission of Victoria (ESCV) meets the definition of a 'State Agency'.²²

Throughout 2021, the ACCC has engaged with the ESCV about whether Victorian regulatory framework met the requirements of 29(2)(b) and whether the ESCV considered it appropriate for the ACCC to grant LMW an exemption from the operation of the requirements in divisions 2,3 and 4 of Part 6 of the WCR to LMW. On 24 June 2021, the ESCV wrote a letter to the ACCC (see **Attachment C**) in which the ESCV explained that:

- it considers that Victoria's state framework currently meets, and in some ways exceeds, the requirements of subrule 29(2)(b), and
- it supports LMW's application for an exemption from the operation of the operation of the requirements in divisions 2-4 of Part 6 of the WCR to LMW, with a transition to State Agency regulation

In explaining its reasons for supporting the LMW exemption application, ESCV submits that:

Regulating Lower Murray Water's basin charges under this same framework would meet the requirements of the rules and simplify regulatory processes. It will also make it easier for customers to understand the basis for setting prices, in that price regulation for all Lower Murray Water services would be under one framework.

We must also have regard to the following pricing principles when making a price determination:

(i) enable customers or potential customers of the regulated entity to easily understand the prices charged by the regulated entity for prescribed services or the manner in which such prices are calculated, determined or otherwise regulated

²¹ Victorian Farmers' Federation, Draft Advice Submission 2016, pages 6-7. See: <https://www.accc.gov.au/system/files/Victorian%20Farmers%27%20Federation.pdf> and ACCC (2016) Review of the water charge rules – final advice, page 144. Available <https://www.accc.gov.au/regulation/infrastructure/water/water-projects/review-of-the-water-charge-rules-advice-development/final-advice#:~:text=Final%20advice%2017%20November%202016%20The%20ACCC%20provided,2010%2C%20consistent%20with%20the%20ACCC%E2%80%99s%20rule%20advice%205-L..>

²² Rule 3 of WCR defines a 'State Agency' as 'an agency of a State within the meaning of paragraph c) of the definition of agency of a State in [in section 4] of the [Water] Act. This is (c) a body (whether incorporated or not) established or appointed for a public purpose by or under a law of the State (including a local government body).

(ii) provide signals about the efficient costs of providing prescribed services to customers (either collectively or to an individual customer or class of customers) while avoiding price shocks where possible

(iii) take into account the interests of customers of the regulated entity, including low income and vulnerable customers.

We consider that these pricing principles meet rule 29(2)(b). This requires that the forecast revenue from Basin water charges are reasonably likely to meet, but not materially exceed, the prudent and efficient costs of providing infrastructure services.

The ESCV further states:

Our guidance to water corporations provided under the WIRO also sets out specifically that the forecast capital expenditure to be included for the purposes of determining the required revenue must be capital expenditure that would be incurred by a prudent service provider acting efficiently to achieve the lowest cost of delivering service outcomes, taking into account a long-term planning horizon (prudent and efficient forecast capital expenditure).

In addition, we have developed the PREMO - Performance, Risk, Engagement, Management and Outcomes - incentive mechanism to provide financial and reputational incentives for water corporations to deliver outcomes most valued by its customers. The main elements of PREMO are:

- a greater emphasis on the role of customer engagement to inform and influence proposals*
- an incentive mechanism linking the return on equity earned to the level of ambition to deliver customer value expressed in a price submission*
- flexibility mechanisms to allow a tailored and possibly fast-tracked assessment of proposals, consistent with the strength and clarity of a price submission.*

An independent review by consultants farrierswier found that PREMO was successful in providing incentives for water corporations to deliver better outcomes for their customers. This reflected extensive engagement by water corporations, so price submissions were better informed by customer priorities.

We are confident that the Victorian water industry price regulation framework meets, and in some ways exceeds, the requirements of rule 29(2)(b). This framework ensures regulated prices reflect efficient costs and outcomes reflect customers' interests.

The ESCV's view that LMW should be granted an exemption from Part 6 and that the current regulatory framework meets the requirements of the WCR and that price regulation for LMW's services should be under a single framework, supports the view that the application of Part 6 requirements to LMW would not materially contribute to achieving the Basin water charging objectives and principles.

f) whether the relevant law of a State is being transitioned so that the operator's infrastructure charges will at a future date be determined or approved by a single State Agency in a way that is consistent with paragraph 29(2)(b)

On 13 October 2021, amendments to Victorian regulatory framework were introduced to the Victorian Parliament. The changes will enable the ESCV to determine infrastructure charges

for infrastructure operators in the Murray-Darling Basin and remove the accreditation arrangements discussed in section 3.1.

If the proposed amendments take effect, LMW's infrastructure charges will be determined under the current Victorian framework, which the ACCC considers to be broadly consistent with the prudence and efficiency requirements under subrule 29(2)(b) of the WCR.

In forming this view, the ACCC has considered the ESCV's existing regulatory framework. This framework includes the ESCV's objectives and the matters the ESCV must have regard to in determining prices which include the efficient costs of producing or supplying regulated goods or services, the return on assets in the regulated industry, and any relevant interstate and international benchmarks for prices, costs and return on assets in comparable industries. While it is not identical to the requirements under Part 6, the existing Victorian framework is broadly consistent with the prudence and efficiency requirements in 29(2)(b).

The ACCC considers it likely that these new arrangements will be in place by the time LMW's transition period expires on 30 June 2023. As such, consideration of this factor weighs towards the view that the application of Part 6 requirements to LMW would not materially contribute to achieving the Basin water charging objectives and principles.

g) the proportion of the infrastructure operator's revenue to be recovered from infrastructure charges

LMW submitted in its exemption application that being an irrigation infrastructure operator, LMW's rural irrigation revenue predominantly consists of infrastructure charges. LMW's exemption application included audited revenue figures for 2020, which showed that revenue from infrastructure charges (\$25 325 933) was 79% of total revenue (\$32,066,170).²³

A significant percentage of LMW's revenue comes from infrastructure charges. However, as discussed above, the infrastructure services which LMW provides are not bulk water services. It should be noted that, in relation to the bulk water charges that it passes through, LMW remits this revenue back to GMW. As such, LMW does not receive significant revenue in relation to these services.²⁴

Consideration of this factor is not determinative in either direction in assessing whether the application of Part 6 requirements to LMW would not materially contribute to the achievement of the Basin water charging objectives and principles.

h) any other matters that the ACCC considers relevant

As discussed under section 5f, the ACCC considers it likely that new arrangements will be in place by the time LMW's transition period expires on 30 June 2023, and that these arrangements are likely to be consistent with subrule 29(2)(b).

If the proposed amendments take effect, this would also align with the policy intent of Part 6, to return regulatory responsibility for setting the infrastructure charges to a single State regulator, where Basin State regulation consistent with subrule 29(2)(b) was in place. The ACCC also considers that aspects of the current Victorian framework, highlighted above under section 5f, contribute to achieving the Basin water charging objectives and principles.

²³ Attachment B - LMW's exemption application – 8 September 2021, page 5.

²⁴ *LMW do charge a small bulk water component for the loss of water within its infrastructure via its infrastructure charges.* Attachment B - LMW's exemption application – 8 September 2021, page 3.

Therefore, the ACCC considers that this factor weighs towards the view that the application of Part 6 requirements to LMW would not materially contribute to the achievement of the Basin water charging objectives and principles.

6. Conclusion

For the reasons outlined above, the ACCC has decided to grant the Lower Murray Water Urban and Rural Water Authority an exemption from the operation of the requirements of Divisions 2, 3 and 4 of Part 6 of the WCR.

This is because ACCC has considered the matters under subrule 23C(5) and is satisfied that the application of the requirements in divisions 2, 3 and 4 of Part 6 to LMW would not materially contribute to the achievement of the Basin water charging objectives and principles set out in Schedule 2 of the Water Act.

Attachment A - Basin water charging objectives and principles (Schedule 2, *Water Act 2007*)

Part 1—Preliminary 1 Objectives and principles

This Schedule sets out:

- (a) the Basin water charging objectives; and
- (b) the Basin water charging principles.

Note 1: These objectives and principles are relevant to the formulation of water charge rules under section 92 of this Act.

Note 2: These objectives and principles are based on those set out in clauses 64 to 77 of the National Water Initiative when Part 2 of this Act commences.

Part 2—Water charging objectives

2 Water charging objectives

The water charging objectives are:

- (a) to promote the economically efficient and sustainable use of:
 - i) water resources; and
 - ii) water infrastructure assets; and
 - iii) government resources devoted to the management of water resources; and
- (b) to ensure sufficient revenue streams to allow efficient delivery of the required services; and
- (c) to facilitate the efficient functioning of water markets (including inter-jurisdictional water markets, and in both rural and urban settings); and
- (d) to give effect to the principles of user-pays and achieve pricing transparency in respect of water storage and delivery in irrigation systems and cost recovery for water planning and management; and
- (e) to avoid perverse or unintended pricing outcomes.

Part 3—Water charging principles

3 Water storage and delivery

- (1) Pricing policies for water storage and delivery in rural systems are to be developed to facilitate efficient water use and trade in water entitlements.
- (2) Water charges are to include a consumption-based component.
- (3) Water charges are to be based on full cost recovery for water services to ensure business viability and avoid monopoly rents, including recovery of environmental externalities where feasible and practical.
- (4) Water charges in the rural water sector are to continue to move towards upper bound pricing where practicable.
- (5) In subclause (4): upper bound pricing means the level at which, to avoid monopoly rents, a water business should not recover more than:

- (a) the operational, maintenance and administrative costs, externalities, taxes or tax equivalent regimes; and
 - (b) provision for the cost of asset consumption; and
 - (c) provision for the cost of capital (calculated using a weighted average cost of capital).
- (6) If full cost recovery is unlikely to be achieved and a Community Service Obligation is deemed necessary:
- (a) the size of the subsidy is to be reported publicly; and
 - (b) where practicable, subsidies or Community Service Obligations are to be reduced or eliminated.
- (7) Pricing policies should ensure consistency across sectors and jurisdictions where entitlements are able to be traded.

4 Cost recovery for planning and management

- (1) All costs associated with water planning and management must be identified, including the costs of underpinning water markets (such as the provision of registers, accounting and measurement frameworks and performance monitoring and benchmarking).
- (2) The proportion of costs that can be attributed to water access entitlement holders is to be identified consistently with the principles set out in subclauses (3) and (4).
- (3) Water planning and management charges are to be linked as closely as possible to the costs of activities or products.
- (4) Water planning and management charges are to exclude activities undertaken for the Government (such as policy development and Ministerial or Parliamentary services).
- (5) States and Territories are to report publicly on cost recovery for water planning and management annually. The reports are to include:
 - (a) the total cost of water planning and management; and
 - (b) the proportion of the total cost of water planning and management attributed to water access entitlement holders, and the basis upon which this proportion is determined.

5 Environmental externalities

- (1) Market-based mechanisms (such as pricing to account for positive and negative environmental externalities associated with water use) are to be pursued where feasible.
- (2) The cost of environmental externalities is to be included in water charges where found to be feasible.

6 Benchmarking and efficiency reviews

- (1) Independent and public benchmarking or efficiency reviews of pricing and service quality relevant to regulated water charges is or are to be undertaken based on a nationally consistent framework.
- (2) The costs of operating these benchmarking and efficiency review systems are to be met through recovery of regulated water charges

Lower Murray Corporation Application for Exemption - Water Charge Rules 2010

Purpose

To confirm Lower Murray Water (LMW) are a ‘Part 6 operator’ under the Water Charge Rules 2010 (WCR 2010) and to apply for an exemption in accordance with Rule 23C under the WCR 2010 to enable LMW to be regulated by the Victorian State Agency, being the Essential Services Commission (ESC).

Background

LMW confirms that it continues to be deemed as a Part 6 operator under the criteria of Division 1 Rule 23 of the Water Charge Rules 2010 (WCR 2010).

As LMW is deemed a Part 6 operator, all rural associated infrastructure charges are to be regulated and determined by the Australian Competition and Consumer Commission (ACCC) to ensure achievement of the Basin water charging objectives and principles set out in Schedule 2 to the Water Act 2007 (Cth). Under WCR 2010 Rule 29, the ACCC must determine or approve the infrastructure charges set out in a price application subject to Rule 29(2)(b) and (c).

The State of Victoria has a comprehensive regulation regime with encompassing legislation in place for all LMW urban and associated services charges, which are regulated and determined by the ESC with charging objectives and principles that fundamentally align with the WCR 2010 Rule 29(2)(B).

For the Victorian water agencies that are deemed Part 6 operators, the rural associated charges have been regulated and determined by the ESC under approved accreditation arrangements within the Water Industry Act 1994 Part 1B Section 40, Power of Commission to apply for accreditation. These accreditation arrangements are to remain in place for the remainder of the current pricing determination period, however the next pricing submission determination and approval would be undertaken by the ACCC under current legislation.

The WCR 2010 has the provision under Rule 23C (1) to allow LMW to apply to the ACCC for an exemption. The ACCC may grant an infrastructure operator a written exemption from the operation of the requirements of Divisions 2, 3 and 4 of the WCR 2010.

In making the decision Rule 23C(5)(f) of the WCR 2010 states the ACCC must consider;

whether the relevant law of a State is being transitioned so that the operator’s infrastructure charges will at a future date be determined or approved by a single State Agency in a way that is consistent with paragraph 29(2)(b)

The Victorian government supports state-based regulation of Basin charges by the ESC and is proposing new arrangements that, once in effect, will ensure the state’s regulatory framework

meets the requirements set out in the Water Charge Rules 2010 and the Commonwealth's objectives for the economically efficient and sustainable use of Basin resources.

We understand that DELWP is in discussions with the ACCC to ensure that state-based regulation regime accords with the ACCC's expectations.

Application for Exemption

LMW are applying for an exemption under Rule 23C and provide the supporting information to assist the ACCC to make a decision having regard to matters contained in Rule 23C(5).

(a) the total volume of water access rights in relation to which bulk water services are provided by the operator, if applicable.

In Victoria, a water access right is the perpetual ongoing entitlement being a 'Water Share'.

LMW do not provide bulk water services. LMW do not incur costs for providing a service to be recouped via an (on-river) bulk water charge.

LMW is an off-river infrastructure operator whereby the storage, delivery and/or drainage of water diverted from a natural watercourse, through a network consisting of channels and/or pipes (which can be gravity fed or pressurised) to another person.

LMW does charge its customers a levy for bulk water, on a 'pass through' basis, whereby no additional margin is applied to the Goulburn Murray Water (GMW) bulk water charge. LMW has historically enabled GMW (the bulk water service provider) to levy their bulk water charge to recoup their costs of providing the service to their customers.

Prior to the Victorian Water Register 2007, there was no public register of all water-related entitlements in Victoria. GMW relied on LMW customer database and billing processes to enable the levying of the GMW bulk water charges on its behalf. This practice continues today, although it could technically be completed by GMW via the Victoria Water Register water share database.

The total volume of water share entitlements that LMW levied the bulk water charge on the 'pass through' basis 1 July 2020 was;

Entitlement Type	Bulk Water Charge Volume (ML)
Murray – High Reliability	296,315.09
Murray – Low Reliability	7,099.10
Goulburn – High Reliability	18,116.73
Goulburn – Low Reliability	6,290.94

Of the bulk water charges levied, 221,806.6 ML was for Private Diverter customers (operate their own infrastructure on-river) or Non-water Users.

The bulk water charges billed as a “pass through” depend on the volume of Water Shares that LMW customers hold as of 1 July of any given year. Based on the previous billing date of 1 July 2020, LMW billed \$2,545,471 (includes Private Diverters \$1,700,325) bulk water charges in FY2021 which represents 9.3% of LMW’s total rural revenue for FY2021 of \$27,282,447.

GMW manage the river storages and the infrastructure to convey bulk water down the river to a point where LMW can extract the water for delivery to our customers. LMW act as the infrastructure operator and on-charge as a pass-through the GMW bulk water fee to the individual end customer. LMW do charge a small bulk water component for the loss of water within its infrastructure via its infrastructure charges.

(b) the total volume of water subject to water sharing arrangements in relation to which the operator provides infrastructure services, if applicable.

Not applicable.

As an off-river infrastructure operator LMW does not have any responsibilities in water sharing arrangements.

The Northern Victoria Resource Manager (NVRM) makes seasonal determinations for all northern Victorian regulated river systems including the Goulburn, Broken, Campaspe, Loddon, Bullarook and Murray regulated river systems. The Minister for Water appointed GMW to undertake this role in accordance with Victorian water sharing rules.

The water necessary to give effect to inter-state water-sharing arrangements is stored, managed and operated by GMW as the NVRM.

(c) the infrastructure services provided by the operator;

LMW provides off-river infrastructure operator services.

LMW’s infrastructure service is mainly delivery and/or drainage of water diverted from a natural watercourse, through a network consisting of channels and/or pipes (which can be gravity fed or pressurised).

LMW provides infrastructure services to;

- Irrigation - river quality water services to:
 - 2,666 irrigation and 2,240 stock and domestic customers in the four pumped irrigation districts of Mildura, Merbein, Red Cliffs and Robinvale
 - 309 Millewa rural district customers
 - waterworks district of Yelta.
- Manage the extraction of the region’s rural bulk water entitlements;
- The collection and disposal of subsurface drainage water from the four pumped irrigation districts, as well as from private diverters in Nangiloc, Robinvale and Boundary Bend;

- Oversight of irrigation and drainage design in new agricultural developments ensuring conformity with salinity management plan development guidelines;
- Management of the private diversion licences of 1,313 water users along the Murray River in Victoria between Nyah and the South Australian border;
- The assessment and approval of licensing, water share and allocation trade applications; and
- Water supply delivery to important environmental and recreational sites.

(d) any preferences expressed by the operator's customers to the ACCC;

LMW has not obtained nor have any indication of preference expressed from our customers.

(e) any views expressed by a State Agency to the ACCC;

LMW has contacted the ESC (State Agency) informally, whereby the ESC has indicated support of the intent of LMW's application for exemption, with a transition to State Agency regulation. The ESC is confident that the Victorian regulatory framework provides a thorough and robust regime for the benefit of the Victorian customers.

For the ESC's formal view, the ACCC should contact the ESC directly.

(f) whether the relevant law of a State is being transitioned so that the operator's infrastructure charges will at a future date be determined or approved by a single State Agency in a way that is consistent with paragraph 29(2)(b);

We understand that DELWP is in discussions with the ACCC to ensure that state-based regulation accords with the ACCC's expectations.

The Victorian government supports state-based regulation of Basin charges by the ESC and is proposing new arrangements that, once in effect, will ensure the state's regulatory framework meets the requirements set out in the Water Charge Rules 2010 and the Commonwealth's objectives for the economically efficient and sustainable use of Basin resources.

(g) the proportion of the infrastructure operator's revenue to be recovered from infrastructure charges;

As LMW is an irrigation infrastructure operator, LMW's rural irrigation revenue predominantly consists of infrastructure charges.

Audited revenue received from irrigation services for 2020 is detailed below:

Rural Revenue	2019-20 \$
Infrastructure Charges	
Water Infrastructure	17,968,875
Drainage Infrastructure	1,479,512
Irrigation water delivery	5,877,546
Total Infrastructure Revenue	25,325,933
Other Income	
Termination Fees	52,208
Interest on Charges	68,280
Interest on Investments	45,786
Other Income	538,595
Proceeds Sale Assets	455,183
Fees	290,117
Abnormal Income	440,084
Rental/Lease Income	22,163
Assets rec'd by developers	157,780
Fees paid by developers	4,667,666
Govt Contributions (Noncapital)	2,375
Total Rural Income	32,066,170
Infrastructure Revenue % Total Rural Revenue	79%

(h) any other matters that the ACCC considers relevant.

LMW undertake to provide, where applicable, any further information the ACCC requests to assist them to make a decision on the exemption application.



24/06/2021

RM/21/17847

To: Mr Rod Simms
Chairperson
Australian Competition and Consumer Commission

And to: Mr Mick Keogh
Deputy Chairperson
Australian Competition and Consumer Commission

Per email: mlo@accc.gov.au

Dear Mr Sims/ Mr Keogh

Letter of support for Lower Murray Water application for exemption from price regulation under Water Charge Rules 2010 (Cth) from 1 July 2023

Lower Murray Water Urban and Rural Water Corporation (Lower Murray Water) charges for infrastructure services it provides in relation to Murray-Darling Basin water resources (Basin water charges) are currently regulated under a price determination made by the Essential Services Commission (commission). This determination is made under the Water Charge (Infrastructure) Rules 2010 (Cth) (the rules) and covers the regulatory period 1 July 2018 to 30 June 2023.

The rules were amended effective 1 July 2020 and envision that future regulation of Lower Murray Water's Basin water charges can occur under Victoria's state framework, provided it meets certain requirements under the rules. These are that the state framework should provide for regulation by a single state agency (such as the commission) (rule 23(1)) and cost reflective charging arrangements are in place, consistent with (not exceeding) the recovery of prudent and efficient costs (rule 29(2)(b)). The rules were also renamed at this time to the Water Charge Rules 2010.

If a qualifying state framework is not in place, Lower Murray Water's Basin water charges will be regulated under the rules by the Australian Competition and Consumer Commission (ACCC) for its next regulatory period commencing 1 July 2023.

The rules however provide for Lower Murray Water to apply for exemption from regulation of its Basin water charges by the ACCC if steps are being taken to transition Victoria's state framework

to an arrangement that is consistent with the rules. We understand that Lower Murray Water will shortly make an exemption application to the ACCC.

The Department of Environment, Land, Water & Planning (DELWP) has provided a letter to the commission confirming that the Victorian government is keen to continue with the commission undertaking price regulation of Basin water charges under a state framework that meets the requirements of the rules. It also supports Lower Murray Water making an exemption application.

DELWP has indicated in this letter that it will undertake the work required to implement a state framework that meets the requirement of the rules in 2021. DELWP has also asked that the commission support and undertake the necessary steps to aid the transition of Victoria's Basin infrastructure operators back to state regulation.

Noting the Victorian government's policy position, and the request from DELWP, the commission supports Lower Murray Water's proposed exemption application. The commission however notes that its ability to regulate Lower Murray Water's Basin water charges from 1 July 2023 depends on legislative changes being made to Victoria's state framework, to provide us with a clear legislative mandate to do this.

The commission considers that Victoria's state framework currently meets, and in some ways exceeds, the requirements of rules (in particular rule 29(2)(b)). Attachment 1 outlines the relevant areas of this framework that we consider meets, and exceeds, the rules.

The commission currently regulates Lower Murray Water's urban water charges under Victoria's state framework. Regulating Lower Murray Water's basin charges under this same framework would meet the requirements of the rules and simplify regulatory processes. It will also make it easier for customers to understand the basis for setting prices, in that price regulation for all Lower Murray Water services would be under one framework.

The key processes and indicative timelines for Lower Murray Water's next price review under Victoria's state framework for the regulatory period commencing 1 July 2023 are set out below:

- October/November 2021 – commission to issue guidance under clause 13 of the Water Industry Regulatory Order 2014
- October/November 2022 – Lower Murray Water to submit a price submission to the commission
- December to February 2023 – public consultation on price submission
- March 2023 – commission draft decision
- March-April 2023 – public consultation on commission draft decision
- June 2023 – commission final decision

This process could apply to both Lower Murray Water's urban and Basin water charges.

Some of these timelines can be shifted out to accommodate the time required to make the necessary changes to Victorian legislation.

If you have any queries or require further information, please contact Marcus Crudden, Executive Director, Price Monitoring & Regulation Division, at Marcus.Crudden@esc.vic.gov.au.

Yours sincerely



Kate Symons
Chairperson



Attachment 1: Victoria's water industry price regulation framework

The Victorian water industry price regulation framework is set out in the *Water Industry Act 1994* (Vic) (WI Act), the *Essential Services Commission Act 2001* (Vic) (ESC Act) and the Water Industry Regulatory Order 2014 (WIRO) made under the WI Act. Our role includes regulating the prices and monitoring service standards of water corporations operating in Victoria. There are currently 19 such water corporations.

The WIRO sets out the matters we must have regard to when making price determinations, and places particular emphasis on:

- (i) the promotion of efficient use of prescribed services by customers
- (ii) the promotion of efficiency in regulated entities as well as efficiency in, and the financial viability of, the regulated water industry
- (iii) the provision to regulated entities of incentives to pursue efficiency improvements.

We must also have regard to the following pricing principles when making a price determination:

- (i) enable customers or potential customers of the regulated entity to easily understand the prices charged by the regulated entity for prescribed services or the manner in which such prices are calculated, determined or otherwise regulated
- (ii) provide signals about the efficient costs of providing prescribed services to customers (either collectively or to an individual customer or class of customers) while avoiding price shocks where possible
- (iii) take into account the interests of customers of the regulated entity, including low income and vulnerable customers.

We consider that these pricing principles meet rule 29(2)(b). This requires that the forecast revenue from Basin water charges are reasonably likely to meet, but not materially exceed, the prudent and efficient costs of providing infrastructure services.

Our guidance to water corporations provided under the WIRO also sets out specifically that the forecast capital expenditure to be included for the purposes of determining the required revenue must be capital expenditure that would be incurred by a prudent service provider acting efficiently to achieve the lowest cost of delivering service outcomes, taking into account a long-term planning horizon (prudent and efficient forecast capital expenditure).

In addition, we have developed the PREMO - Performance, Risk, Engagement, Management and Outcomes - incentive mechanism to provide financial and reputational incentives for water corporations to deliver outcomes most valued by its customers. The main elements of PREMO are:

- a greater emphasis on the role of customer engagement to inform and influence proposals

- an incentive mechanism linking the return on equity earned to the level of ambition to deliver customer value expressed in a price submission
- flexibility mechanisms to allow a tailored and possibly fast-tracked assessment of proposals, consistent with the strength and clarity of a price submission.

An independent review by consultants farrierswier found that PREMO was successful in providing incentives for water corporations to deliver better outcomes for their customers. This reflected extensive engagement by water corporations, so price submissions were better informed by customer priorities.

We are confident that the Victorian water industry price regulation framework meets, and in some ways exceeds, the requirements of rule 29(2)(b). This framework ensures regulated prices reflect efficient costs and outcomes reflect customers' interests.

