

REVIEW OF MELBOURNE WATER PRICE SUBMISSION

In June 2016, the Commission released its final decision on Melbourne Water’s price submission. The final decision completes our review of the maximum prices that Melbourne Water may charge for its bulk water, sewage treatment, recycled water and waterways and drainage services for a five year regulatory period from 1 July 2016 to 30 June 2021.

Our final decision allows Melbourne Water to continue to provide its customers with high quality and reliable services and undertake historically high levels of investment to upgrade and renew water, sewerage and drainage infrastructure.

Furthermore, the maximum prices Melbourne Water may charge is, on average, lower than current levels. This partly reflects the cost savings identified by Melbourne Water in its price submission. Our review found additional savings. On average, household bills will remain steady or decline slightly in 2016-17.

We undertook our review in an open and consultative manner. This includes the release of our draft decision in March 2016, public meetings in February and April 2016 and review of 116 public submissions.

REVENUE REQUIREMENT – FINAL DECISION

We approve a revenue requirement of \$7 761 million for the period 2016-17 to 2020-21, \$94 million (or 1.2 per cent) lower than proposed by Melbourne Water (Table 1). This reflects our assessment of the efficient costs of delivering services. The revenue approved in our final decision will allow Melbourne Water to deliver safe and reliable wholesale water and sewage services, and meet service commitments in waterway health, flood protection and stormwater management.

The major areas of adjustment relative to Melbourne Water’s proposal include lower operating and capital expenditures.

Table 1. Revenue requirement – Melbourne Water final decision (\$m 2015-16)

	2016-17	2017-18	2018-19	2019-20	2020-21	Total
Proposed revenue	1 560	1 576	1 588	1 570	1 561	7 855
Final decision revenue	1 546	1 541	1 557	1 566	1 551	7 761

OPERATING EXPENDITURE – FINAL DECISION

We approve operating expenditure of \$4 529 million, which is 162 million (or 3.5 per cent) lower than the total proposed by Melbourne Water, reflecting our assessment of the efficient costs of operating the business and maintaining services over the regulatory period. The main reasons for the reduction is our assessment of energy costs.

The operating expenditure that we have adopted for Melbourne Water does not represent the amount that it is required to spend or allocate to particular operational, maintenance and administrative activities.

We approve Melbourne Water’s proposal to capitalise (that is, treat a proportion of operating costs as capital expenditure for pricing purposes) \$30 million per annum of its forecast annual desalination security payments over the 2016-17 to 2020-21 period. This has the effect of lowering prices for end-use customers.

CAPITAL EXPENDITURE – FINAL DECISION

We approve capital expenditure of \$2 456 million for the period 2016-17 to 2020-21 to allow Melbourne Water to maintain its existing assets and establish new assets in order to deliver its service commitments. Major projects include:

- upgrades to the Western Treatment Plant to increase treatment capacity and ensure safe, ongoing operation
- renewal of the Upper Hobsons Bay mains sewer to rehabilitate infrastructure built over 100 years ago
- renewal of a number of key water mains, pipelines and aqueducts to rehabilitate aging infrastructure built in the 1890s – 1930s and increase capacity to meet Melbourne’s growing population.

This is \$216 million (or 8.1 per cent) lower than proposed by Melbourne Water.

TARIFF STRUCTURE – FINAL DECISION

We approve a number of reforms to Melbourne Water’s bulk tariff structure and tariffs that will provide greater transparency and reflect cost-reflective pricing structures across its business.

Bulk Water and Sewerage Tariffs

We approve:

- a shift from a fixed and variable water headworks tariff to a fully fixed headworks tariff for each metropolitan water retailer and some regional water businesses to reflect the government’s bulk entitlement reform in 2014
- a shift in tariffs from a fixed and variable water transfer to a single variable tariff common across all retailers
- a variable bulk sewerage tariff structure for treatment and transfer and fixed monthly tariffs for sewerage
- a mechanism that allows Melbourne Water to adjust its prices upward to reflect the costs of desalination water orders. The current determinations for the metropolitan water retailers allow them to pass on the costs of water orders to end-use water customers.

Waterways and Drainage Tariffs

Melbourne Water’s residential waterways and drainage customers will continue to pay the existing flat charge of \$96 per annum indexed to inflation. Our final decision approves Melbourne Water’s proposed waterways and drainage tariffs for residential and rural customers and proposed flat minimum tariff for non-residential customers equal to 1.5 times the residential tariff.

FINANCING – FINAL DECISION

We have approved a trailing average approach to estimating Melbourne Water’s cost of debt. This new approach should reduce price volatility, aligns the regulatory allowance for financing costs with actual costs faced by Melbourne Water, and reduces refinancing risk.

FURTHER INFORMATION

More information, including material from past price reviews can be found on the Commission’s website www.esc.vic.gov.au.