



Australian  
Competition &  
Consumer  
Commission

## **Water Charge (Infrastructure) Rules**

**Application by Essential Service Commission of Victoria for  
accreditation**

**Final Decision**

17 February 2012



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# Summary

The ACCC is responsible under the Water Charge (Infrastructure) Rules 2010 (Cth) (WCIR) for approving or determining the regulated charges of Part 6 and Part 7 water operators in the Murray–Darling Basin.

Part 9 of the WCIR allows for the accreditation of arrangements whereby a State agency would be responsible for approving or determining the regulated charges of Part 6 and Part 7 operators under the WCIR instead of the ACCC.

On 23 November 2011, the ACCC received an application from the Essential Services Commission of Victoria (ESCV) for the accreditation of arrangements that would allow the ESCV to determine regulated charges for Part 6 and Part 7 operators in Victoria.

This paper outlines the ACCC's final decision to approve the ESCV's application. The period of accreditation is for ten years from 17 February 2012

In making this decision to approve the ESCV's accreditation application, the ACCC is satisfied that the application meets the criteria set out in Schedule 5 of the WCIR and includes the information required by rule 60 and Schedule 4 of the WCIR.

Two terms and conditions apply to the accredited arrangements:

**a) The ESCV must apply pricing principles for price approvals and determinations under the Water Charge (Infrastructure) Rules published by the ACCC**

In approving or determining regulated charges of a Part 6 operator under arrangements accredited under Part 9 of the WCIR, the ESCV must apply the pricing principles for Part 6 approvals or determinations published by the ACCC from time to time.

**b) Upon request, the ESCV must provide to the ACCC information relevant to the ESCV carrying out its functions under accredited arrangements.**

Upon request by a relevant ACCC officer, information obtained or produced by the ESCV in carrying out its functions under arrangements accredited under Part 9 of the WCIR must be provided to the ACCC.

The relevant ACCC officer may nominate the information that is requested, the form in which the information is to be provided and the date by which it is to be provided.

The first requirement ensures one set of pricing principles will be applied to price determinations for rural water providers across the Basin, which will contribute to consistency in pricing where there are multiple regulators.

The second requirement will contribute to achieving the Basin water charging objectives and principles. This is because the ACCC's functions and responsibilities under the *Water Act 2007* (Cth), which includes monitoring and enforcement, directly support the achievement of the Basin water charging objectives and principles, and the ACCC may require access to certain information to undertake its functions and meet its responsibilities.

# 1. Introduction

The *Water Act 2007* (Cth) (the Water Act) created new institutional and governance arrangements to address the sustainability and management of water resources in the Murray–Darling Basin (MDB). Among other things, Part 4 of the Water Act gives the responsible Minister (the Minister) the role of making water charge rules in relation to fees and charges for rural water in the MDB.

The Water Charge (Infrastructure) Rules 2010 (WCIR) were made by the Minister for Sustainability, Environment, Water, Population and Communities on 21 December 2010. The WCIR apply new regulatory arrangements to fees and charges levied by infrastructure operators for rural water infrastructure services in the MDB including access to infrastructure, storage and delivery. The WCIR address the various issues that arise from rural water infrastructure operators having market power as natural monopoly service providers, and introduce a more consistent approach to rural water pricing across Basin jurisdictions.

Price approvals and determinations apply to charges levied by two different types of infrastructure operators regulated under the WCIR – Part 6 operators and Part 7 operators.

Part 6 operators are non–member owned operators that provide services in relation to more than 250 GL of managed water resources<sup>1</sup>.

Part 7 operators are member-owned operators that:

- provide services in relation to over 10 GL of entitlement within the MDB<sup>2</sup>, and
- make a distribution to all member customers.

Price approvals and determinations of Part 6 and Part 7 operators may be made by the ACCC under the WCIR or a State agency operating under arrangements accredited by the ACCC.

To achieve consistency in approaches to rural water infrastructure price determinations across the MDB, an accredited State agency would be required to apply relevant provisions of the WCIR (as incorporated into State law) that also apply to the ACCC where it is the responsible regulator. Terms and conditions or obligations for accreditation may also be imposed by the ACCC if the terms, conditions or obligations contribute to achieving the Basin water charging objectives and principles set out in Schedule 2 of the Water Act (**Appendix A**). Accreditation arrangements continue for a period of ten years unless revoked by the ACCC (rule 67).

On 23 November 2011, the ACCC received an application from the Essential Services Commission of Victoria (ESCV) for the accreditation of arrangements that would allow it to determine regulated charges of Part 6 and Part 7 operators in Victoria. In Victoria,

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<sup>1</sup> Managed water resources include entitlements within the MDB and within a State where that State has referred power to the Water Act in respect of all of non-urban water in its State.

<sup>2</sup> Or within a State where that State has referred power to the Water Act in respect of all of non-urban water in its State.

Goulburn-Murray Water and Lower Murray Water are currently Part 6 operators. There are no Part 7 operators in Victoria.<sup>3</sup>

On 16 December the ACCC published its draft decision to approve the ESCV's application for accreditation. Two terms, conditions or obligations of accreditation were proposed.

The ACCC received submissions on its draft decision from the Victorian Farmers Federation, Goulburn-Murray Water and Victorian Government Minister for Water.

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<sup>3</sup> Available at [www.accc.gov.au/water](http://www.accc.gov.au/water)

## 2. Accreditation of arrangements under the WCIR

The ESCV may make an accreditation application under rule 60 of the WCIR. An application must be in writing and include the information outlined under rule 60 and Schedule 4 of the WCIR. The application must be made within a certain timeframe and must be accompanied by evidence in writing that the application is supported by the Minister, or the Head of a Department, of the State Agency responsible for that agency.

Under rule 63 the ACCC

- (a) must not approve an application under this Part for the accreditation of arrangements unless the ACCC is satisfied that the arrangements are in accordance with the criteria set out in Schedule 5; and
- (b) must not refuse to approve an application under this Part for the accreditation of arrangements unless the ACCC is satisfied that the arrangements are not in accordance with the criteria set out in Schedule 5.

Schedule 5 of the WCIR includes the following:

- (1) There must be a law of the State:
  - (a) under which the applied provisions are a law of the State; and
  - (b) that includes provision to the effect that the applied provisions operate only during such period or periods as an accreditation of arrangements under Part 9 has effect
- (2) The functions of the State Agency must include the functions conferred on a Regular under the applied provisions
- (3) The State Agency must not be subject to the direction of a Minister of the State in carrying out its functions under the applied provisions
- (4) The State Agency must not be, or have a relevant interest in a Part 6 operator or a Part 7 operator.

Under rule 59(2) applied provisions means the following provisions of the WCIR:

- (a) Divisions 2,3 and 4 of Part 6
- (b) Division 2 of Part 7
- (c) Division 1 of Part 8
- (d) Schedules 1 ,2 and 3
- (e) Part 1, so far is relevant to the interpretation of the provisions referred to in paragraphs (a), (b), (c) and (d).

### **3. Assessment of ESCV application**

The ACCC is satisfied that the accreditation application meets the criteria set out in Schedule 5 of the WCIR and includes the information required by rule 60 and Schedule 4 of the WCIR.<sup>4</sup>

Table 1 outlines the reasons why the ACCC considers that the ESCV's application meets the criteria set out in Schedule 5 of the WCIR.

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<sup>4</sup> The application is supported in writing by the Secretary of the Victorian Department of Treasury and Finance, and the Victorian Minister for Water.



**Table 1 – Assessment of ESCV’s accreditation application**

Criteria	Assessment
<p>There must be a law of the State under which the applied provisions are a law of the State; and that includes provision to the effect that the applied provisions operate only during such period or periods as an accreditation of arrangements under Part 9 has effect</p>	<p>As set out below, the <i>Water Legislation Amendment (Water Infrastructure Charges) Act 2011</i> (Vic), No 63 of 2011 amended the <i>Water Industry Act 1994</i> (Vic) and the <i>Essential Services Commission Act 2001</i>(Vic) so as to give effect to the applied provisions of the WCIR under Victorian law.<sup>5</sup></p> <p>The ACCC is satisfied that the applied provisions are a law of Victoria under s. 4K of the <i>Water Industry Act 1994</i> (Vic.)</p> <p><b>4K Application of Commonwealth provisions</b></p> <p>In respect of Basin water charges, the Commonwealth provisions apply as a law of the State.<sup>6</sup></p> <p>The ACCC is satisfied that s. 4K will not apply unless the ESCV obtains accreditation for arrangements under Part 9 of the WCIR.</p> <p>Section 4N of the <i>Water Industry Act 1994</i> (Vic.) limits the operation of the applied provisions in Victoria to the period for which the accreditation of arrangements under Part 9 of the WCIR has effect</p> <p><b>4N Cessation of effect of provisions</b></p> <p>Sections 4K, 4L and 4M do not have effect if this Part is not accredited arrangements.</p> <p>Further, s. 10(m) of the <i>Essential Services Commission Act</i> provides that the Commission’s functions under the applied provisions apply only where accredited arrangements have effect.</p>
<p>The functions of the State Agency must include the functions conferred on a Regulator under the applied provisions</p>	<p>The ACCC is satisfied that under s.10 of the <i>Essential Services Commission Act 2001</i> (Vic.) and s.4M of the <i>Water Industry Act 1994</i> (Vic.), as set out below, the ESCV has the functions conferred on a Regulator under the applied provisions.</p> <p>The <i>Water Industry Act 1994</i> (Vic.) s. 4M:</p> <p><b>4M Powers of Commission</b></p> <p>The Commission has all the powers that are necessary to perform its functions as a State Agency under the</p>

<sup>5</sup> The *Water Legislation Amendment (Water Infrastructure Charges) Act 2011* (Vic) commenced on 16 November 2011.

<sup>6</sup> s. 4J of the *Water Industry Act 1994* (Vic.) defines Basin water charge and Commonwealth provisions. The former is defined as a regulated charge for a service in relation to Basin water resources provided by a Part 6 operator or Part 7 operator that is an Authority. The latter has the same meaning as applied provisions in rule 59(2) of the Commonwealth Water Charge WCIR.

	<p>applied Victorian provisions.</p> <p><i>The Essential Services Commission Act 2001 (Vic.) s. 10</i></p> <p>The functions of the Commission are...</p> <p>(m) if, under Part 1B of the Water Industry Act 1994, the Commonwealth provisions (within the meaning of that Part) are applied as a law of the State, to perform the functions conferred under those applied provisions on the Commission as the State Agency (within the meaning of that Part).</p>
<p>The State Agency must not be subject to the direction of a Minister of the State in carrying out its functions under the applied provisions</p>	<p><i>The Essential Services Commission of Victoria Act 2001 (Vic.) s. 12</i> applies when the ESCV is carrying out its functions under the applied provisions</p> <p><b>12 Commission not subject to direction or control</b></p> <p>Except as provided by or under this Act or any other Act, the Commission is not subject to the direction or control of the Minister.</p> <p>In its application to the ACCC, the ESCV has stated ‘there is not a provision under any of the Acts relevant to the ESC’s powers and functions to approve or determine Basin water charges that would make the ESC subject to the direction or control of a Minister in carrying out its functions under the "applied provisions"’. The ACCC is satisfied that this is correct.</p>
<p>The State Agency must not be, or have a relevant interest in a Part 6 operator or a Part 7 operator.</p>	<p>There are currently two Part 6 operators in Victoria – Goulburn-Murray Water and Lower Murray Water. The ACCC is satisfied that the ESCV does not have a relevant interest in either of these operators.</p> <p>There are no Part 7 operators in Victoria.</p>

## 4. Terms and conditions of accreditation

Under rule 65(1) of the WCIR, the ACCC may, if it determines that it is necessary to do so, impose terms, conditions or obligations on the accreditation if the terms, conditions or obligations contribute to achieving the Basin water charging objectives and principles set out in Schedule 2 of the Water Act.

Accredited arrangements in Victoria under Part 9 of the WCIR are to be subject to two terms, conditions or obligations.

**a. The ESCV must apply pricing principles for Part 6 approvals and determinations published by the ACCC**

In approving or determining regulated charges of a Part 6 operator under arrangements accredited under Part 9 of the WCIR, the ESCV must apply the pricing principles for Part 6 approvals or determinations published by the ACCC from time to time.

This will contribute to achieving the Basin water charging principle that ‘pricing policies should ensure consistency across sectors and jurisdictions where entitlements are able to be traded’.<sup>7</sup>

**b. Upon request the ESCV must provide to the ACCC information relevant to the ESCV carrying out its functions under accredited arrangements.**

Upon request by a relevant ACCC officer, information obtained or produced by the ESCV in carrying out its functions under arrangements accredited under Part 9 of the WCIR must be provided to the ACCC.

The relevant ACCC officer may nominate the information that is requested, the form in which the information is to be provided and the date by which it is to be provided.

This will contribute to achieving the Basin water charging objectives and principles because the ACCC’s functions and responsibilities under the *Water Act 2007* (Cth), which includes monitoring and enforcement, directly support the achievement of the Basin water charging objectives and principles, and the ACCC may require access to certain information to undertake its functions and meet its responsibilities

The reasons the ACCC has applied these terms and conditions or obligations are set out in further detail below.

### 4.1. Application of ACCC pricing principles for Part 6 approvals and determinations

The ACCC’s pricing principles for price approvals and determinations under the WCIR set out the methodology that the ACCC will apply when undertaking price approvals or determinations of either Part 6 or Part 7 operators under the WCIR. The current version of the pricing principles applying to Part 6 operators is provided at Appendix B.

The principles mainly relate to the determination of the costs on which regulated charges are to be based, as well as how revenue should be determined and, ultimately,

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<sup>7</sup> *Water Act 2007*, Schedule 2, Part 3, principle (d).

how charges are levied to recover this revenue. For instance, the principles relate to the determination of the rate of return to be applied to assets, and the approach used to assess operating and capital expenditure proposed by an operator.

The ACCC also wants to ensure that - as far as is practical - there is consistent implementation of price approvals and determinations where there are multiple regulators of Part 6 operators across the MDB. This will contribute to achieving the Basin water charging principle that 'pricing policies should ensure consistency across sectors and jurisdictions where entitlements are able to be traded'.<sup>8</sup>

## **4.2. Provision of information to the ACCC**

Access by the ACCC to information produced or obtained by the ESCV in carrying out its role under accredited arrangements will contribute to achieving the Basin water charging objectives and principles. This is because the ACCC's functions and responsibilities directly support the achievement of the Basin water charging objectives and principles, and as discussed below, the ACCC requires access to certain information to undertake its functions and meet its responsibilities.

Under s. 94 of the Water Act, the ACCC is responsible for monitoring compliance with water charge rules and monitoring regulated water charges and reporting the results of such monitoring in accordance with an agreement between the Minister and the ACCC.

Under s. 137(b) of the Water Act, the ACCC is also the appropriate enforcement agency responsible for regulating contraventions of the water charge rules. In this role, the ACCC is required to enforce approvals or determinations made by the ACCC or a State agency under accreditation arrangements.

Consequently, the ACCC may be required to access information obtained by an accredited State agency in order to fulfil its responsibilities.

Further, access to information produced by a State agency when carrying out its functions under accredited arrangements will assist the ACCC with future policy and regulatory obligations under the Water Act and the WCIR. For example, under the Water Act the Minister is required to ask the ACCC for advice about water charge rules the Minister proposes to make, or about proposed amendments or revocations of rules, and the ACCC must advise the Minister on these matters.<sup>9</sup> Access to information about how an accredited agency has determined the charges of Part 6 operators under the WCIR may be required by the ACCC if it is asked in the future to provide policy advice to the Minister on the operation of the rules in respect of Part 6 operators.

While some information produced or obtained by the ESCV in carrying out its role under accredited arrangements will be publicly available, other information may not be. It is noted that the ACCC, or a State agency acting under accredited arrangements, is subject to confidentiality provisions when deciding whether to publish information submitted by a Part 6 or Part 7 operator (see rule 53 below).<sup>10</sup>

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<sup>8</sup> *Water Act 2007*, Schedule 2, Part 3, principle (d).

<sup>9</sup> *Water Act 2007*, s. 93.

<sup>10</sup> Notwithstanding these provisions, the ACCC may be required to disclose confidential information for other purposes, in accordance with its Information Policy as part of carrying out its responsibilities and functions under legislation.

### **53 Regulator not to publish applications and submissions if confidential**

(1) Except as provided in subrule (2), the Regulator must not publish an application or a submission under Part 6, 7 or 9, or include any information from an application or submission in its reasons for its decisions under Part 6, 7 or 9, if:

(a) the person who made the application or submission claimed, when making the application or submission, that it contains confidential information; and

(b) the Regulator decides that the application or submission contains confidential information.

(2) If a person claimed, when making an application or submission under Part 6, 7 or 9, that the application or submission contained confidential information and the Regulator considers that it does contain confidential information, the Regulator may publish the application or submission, and any information from an application or submission, if the confidential information is omitted but, before so doing, must cause a note to that effect to be included in the document at the place in the document from which the information is omitted.

(3) In this rule, **application** includes further information provided by the applicant at the request of the Regulator under rule 26, 35, 41, 47 or 61.

To ensure that the ACCC has access to all information necessary for the ACCC to carry out its responsibilities and functions under the Water Act, upon request by a relevant officer of the ACCC the ESCV is required to disclose to the ACCC information the ESCV receives or produces in carrying out its role under accredited arrangements. The relevant ACCC officer may nominate the information that is requested, the form in which the information is to be provided and the date by which it is to be provided.

The context in which the information is required will determine how exactly the information contributes to the Basin water charging objectives and principles. For example, if the ACCC does not have information on which to investigate a breach of a rule it may not be able to take compliance action which could lead to perverse pricing outcomes. This would be in conflict with objective (e) of the Basin water charging objectives and principles.

## 5. ACCC decision on accreditation

The ACCC's decision is to approve the ESCV's application for accreditation of arrangements under Part 9 of the Water Charge (Infrastructure) Rules.

In accordance with ss 92(g) and (h) of the *Water Act 2007* and rule 59(c) of the Water Charge (Infrastructure) Rules in carrying out its functions under accredited arrangements the ESCV must:

**a) Apply pricing principles for price approvals and determinations under the Water Charge (Infrastructure) Rules published by the ACCC**

In approving or determining regulated charges of a Part 6 operator under arrangements accredited under Part 9 of the WCIR, the ESCV must apply the pricing principles for Part 6 approvals or determinations published by the ACCC from time to time.

The current pricing principles for Part 6 approvals or determinations are provided in Appendix B to this final decision.

**b) Upon request, provide to the ACCC information relevant to the ESCV carrying out its functions under accredited arrangements.**

Upon request by a relevant ACCC officer, information obtained or produced by the ESCV in carrying out its functions under arrangements accredited under Part 9 of the WCIR must be provided to the ACCC.

The relevant ACCC officer may nominate the information that is requested, the form in which the information is to be provided and the date by which it is to be provided.

## **6. Issues relating to working arrangements under accreditation**

The ACCC received submissions on its draft decision from the Victorian Farmers' Federation, Goulburn-Murray Water and the Victorian Government Minister for Water. The submissions, which were broadly supportive of the draft decision, are available on the ACCC's website.

The submissions did not raise issues about the ACCC's draft decision to approve the ESCV's application, or the terms, conditions or obligations of accreditation proposed by the ACCC.

Goulburn-Murray Water (GMW) raised issues related to how the accreditation arrangements would work in practice and the appeal arrangements in place under the regulatory framework. Specifically, GMW queried whether the ACCC and ESCV could work to streamline information requests from regulated operators in Victoria. GMW also submitted that there is currently no mechanism that allows GMW to have a decision by the ESCV reviewed by the ACCC, and that should an issue arise between the ACCC and ESCV, GMW could bear costs and administrative impacts.

Issues regarding the operational arrangements between the ACCC and ESCV under the accreditation arrangements, such as information collection by the regulators for their respective statutory roles, will be considered as part of the development of a Memorandum of Understanding (MOU) between the ACCC and ESCV following accreditation.

Regarding referral by GMW of the ESCV's decisions for the purposes of review by the ACCC, it is noted that the ACCC does not have the power to review the ESCV's decisions. Where the ESCV makes an approval or determination under the accreditation arrangements, the applicable appeal rights and appeal body will be those available under Victorian State law.

# **Appendix A – Basin water charging objectives and principles (Schedule 2 of the *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.

## Appendix B – Pricing principles for price approvals and determinations under the WCIR

This version of the pricing principles is current at February 2012. The pricing principles may be revised from time to time to reflect changes in market conditions or new regulatory approaches.

### Valuation of the opening Regulatory Asset Base (RAB)

- If a Part 6 operator has had its RAB set by an agency of a State under a law of the State in the regulatory period preceding the commencement of the initial regulatory period under Part 6, this value must form the opening RAB value for the purposes of the initial approval or determination process under Part 6.
- Where a RAB value has not been previously set by an agency of a State under a law of the State, the RAB must be determined by applying a recognised valuation methodology. The RAB may only include assets used to provide infrastructure services and may not include any assets:
  - gifted by government or another third party, with no expectation of a rate of return on those assets
  - funded by customers through charges, a renewals annuity or otherwise
  - funded through other customer contributions.
- The regulator must ensure that the initial RAB value does not result in price shocks.

### Roll forward of the RAB

- The RAB must be rolled forward as per Schedule 2 of the rules.

### Rate of return

- The cost of capital is to be calculated on the basis of a WACC determined in accordance with the following formula:

$$WACC = k_e \frac{E}{V} + k_d \frac{D}{V}$$

- The cost of equity is to be estimated using the domestic CAPM based on the Officer model.
- The cost of equity is to be calculated using a MRP of 6 per cent.
- The risk free rate is to be based on the yield of a 10 year CGS bond, using an averaging period of between 10-40 business day period

commencing as close as practically possible to the start of the regulatory period.

- The cost of equity is to be calculated using an equity beta of 0.7.
- The benchmark DRP is to be estimated on the basis of a benchmark gearing level of 60:40 debt to equity on the yields of BBB+ rated corporate bonds with 10 year maturity.

## **Assessment of operating expenditure**

- In making an assessment of the prudent and efficient operating expenditure for the next regulatory period, the regulator must assess:
  - the prudence and efficiency of operating expenditure in the previous regulatory period
  - the reasons and evidence supporting changes to service standards in the next regulatory period
  - the reasons and evidence supporting changes to operating expenditure in the next regulatory period
  - reasonable productivity improvements in providing services over the next regulatory period
- Where relevant, a regulator must compare and take into account operating expenditure of similar businesses.
- Forecasts must be based on reasonable assumptions of the efficient costs likely to be incurred in this period.

## **Assessment of capital expenditure**

- In making an assessment of the prudent and efficient capital expenditure for the next regulatory period, the regulator must assess:
  - the prudence and efficiency of capital expenditure in the previous regulatory period (where relevant to proposed capital expenditure in the next regulatory period)
  - the reasons and evidence supporting the commencement of new major capital expenditure projects in the next regulatory period, including whether such projects are consistent with efficient long term expenditure on infrastructure services.
  - the reasons and evidence supporting levels of capital expenditure in the next regulatory period
  - whether the timeframe for delivering the proposed capital expenditure program is reasonable, having regard to the operator's delivery of major projects in the past
  - whether the asset management and planning framework of the operator reflects best practice
- Forecasts must be based on reasonable assumptions of the efficient costs likely to be incurred in this period.

- Subject to confidentiality, external review of an operator's proposed capital expenditure must be made public on the regulator's website.

## **Debt raising costs**

- The regulator must treat any forecast debt raising costs as operating expenditure.

## **Depreciation**

- Fixed assets should be depreciated using a straight line methodology. However, the regulator or the operator may adopt a different approach to depreciation where an operator can justify departure from this method or where it is appropriate for the regulator to do so. Where a different approach is used, the net present value to the business must be the same as under a straight line methodology.
- Depreciation for an asset must only be recovered once that asset is providing infrastructure services.

## **Taxation**

- In estimating the annual taxation building block, the regulator must estimate the annual actual corporate income taxation to be paid by the operator less the imputation credits that would be received by a hypothetical private investor in the operator.
- In estimating the value of imputation credits the regulator must multiply the annual estimated corporate income tax bill of the operator by an imputation factor ( $\gamma$ ).
- If required, the imputation factor will be determined by the ACCC.

## **Renewals annuities**

- Where a renewals annuity is used, the regulator must be satisfied that it:
  - provides sufficient revenue to fund all required expenditure
  - reflects prudent and efficient expenditure forecasts
  - the discount rate used to calculate the annuity is reasonable
  - is set across a long term planning horizon beyond the period to which the application applies and that the length of the annuity is determined by the capital expenditure program so that all material expenditure is captured.

## **Cost allocation principles**

- Charges are to be approved or determined on the basis of a cost allocation methodology that:
  - identifies which costs arise from providing infrastructure services (to which regulated charges apply) and which costs arise from other activities undertaken by the operator

- attributes direct costs to the service to which they relate and not more than once to any category of service
- uses an appropriate allocator when a causal allocator for shared costs can be identified
- only uses a non-causal allocator for shared costs where those costs are immaterial or no causal relationship could be established without undue cost and effort
- allocates shared costs such that the full amount of those costs, no more or no less, is allocated to the services to which it relates.
- The same cost must not be allocated more than once in any instance.

## **Form of price control**

- A regulator may apply any form of price control – subject to meeting the requirements of the Water Charge Infrastructure Rules 2010.

## **Tariff structures**

- Tariff structures should:
  - promote the economically efficient use of water infrastructure assets
  - ensure sufficient revenue streams to allow efficient delivery of the required services
  - give effect to the principles of user pays in respect of water storage and delivery in irrigation systems
  - achieve pricing transparency
  - facilitate efficient water use and trade in water entitlements.

## **Revenue from termination fees**

- The regulator must take into account the revenue already received by the operator from termination fees when determining the required revenue from regulated charges in the forthcoming regulatory period.
- The method for addressing revenue from termination fees must be transparent to customers and promote price stability.

## **Demand or consumption forecasts**

- An assessment of a Part 6 operator's demand or consumption forecasts is to involve an assessment of whether the demand or consumption forecasts:
  - are based on appropriate forecasting methodology
  - are based on reasonable assumptions about the key drivers of demand, including:
    - supply restrictions

- environmental conditions, including inflows and the availability of water
- commodities, including the treatment of water as a derived demand
- any elasticity assumptions
- demographic impacts, where appropriate.
- utilise the best available information, including historical data that can identify trends in demand
- take account of current demand and economic conditions.
- The regulator may engage an independent consultant to assist in determining the above. All reports from consultants should be made public, subject to confidentiality.

## **Customer consultation**

- The regulator must have regard to consultation undertaken by an operator in approving or determining regulated charges.

# Contacts

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Callers who are deaf or have a hearing or speech impairment can contact the ACCC through the National Relay Service, [www.relayservice.com.au](http://www.relayservice.com.au)

For other business information, go to [www.business.gov.au](http://www.business.gov.au)

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