

Yarra Valley Water final decision

2023 Water Price Review

23 June 2023

Acknowledgement

We acknowledge the Traditional Owners of the lands and waterways on which we work and live.

We acknowledge all Aboriginal and Torres Strait Islander communities, and pay our respects to Elders past and present.

As the First Peoples of this land, belonging to the world's oldest living cultures, we recognise and value their knowledge, and ongoing role in shaping and enriching the story of Victoria.

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Summary

We have made our final decision on Yarra Valley Water's prices for the next 5 years

In December 2022, we released our draft decision on the price submission Yarra Valley Water submitted to us in September 2022.¹ The draft decision set out our preliminary views on Yarra Valley Water's proposals and invited interested parties to make further submissions. We also held a public forum in February 2023. In addition to responses by Yarra Valley Water, we received three written submissions on our draft decision, which is available on our website (see Appendix A of this final decision for details).

After considering that feedback and Yarra Valley Water's response, we have made a price determination for Yarra Valley Water.² The price determination sets out the maximum prices Yarra Valley Water may charge for prescribed services (or the manner in which its prices are to be calculated, determined, or otherwise regulated) for the 5-year period from 1 July 2023 (2023–28). This final decision sets out our supporting reasons and analysis for the price determination.



Where our final decision on a particular aspect is unchanged from our draft decision, we have not detailed the supporting reasons in our final decision. Rather, we have noted that our final decision confirms the reasons and position we reached in the draft decision.

Where we have reached a different decision to that proposed in our draft decision, or where new information required our consideration, we have set out our reasons in full in this final decision. This final decision should be read in conjunction with our draft decision.

¹ Our draft decision for Yarra Valley Water is available at www.esc.vic.gov.au/waterpricereview.

² Before the commencement of a regulatory period, clause 10 of the Water Industry Regulatory Order 2014 requires us to make a price determination which determines the maximum prices a water business may charge, or the manner in which its prices are to be calculated, determined or otherwise regulated during the regulatory period. See Essential Services Commission, *Yarra Valley Water Determination: 1 July 2023 – 30 June 2028*, 23 June 2023.

We have approved a revenue requirement of \$4,947.5 million over 5 years

Our final decision approves a revenue requirement of \$4,947.5 million over the 5-year period starting 1 July 2023 (see Chapter 4).³ This is \$56.5 million or 1.2 per cent higher than our draft decision, which mainly reflects our updates to the cost of debt.

This revenue requirement will allow Yarra Valley Water to deliver on its customer service commitments, government policy, statements of obligations, and obligations monitored by the Environment Protection Authority Victoria and the Department of Health.

Typical water and sewerage bills will rise from 1 July 2023

A summary of approved maximum prices for major services delivered by Yarra Valley Water is set out in Section 5.3.2. Table A shows the estimated typical bills for different customer groups under our final decision, for 2022-23 (the current year) and 2023-24. For a typical residential owner occupier, estimated annual water and sewerage bills (including inflation) will rise from around \$1,028 currently to \$1,049 in 2023-24, an increase of around 2.1 per cent. For a typical residential tenant, bills (including inflation) will rise from around \$498 currently to \$508 in 2023-24. The bill paid by each customer will vary depending on water use, prices for fixed and variable tariffs, and other charges.

As noted below, most of Yarra Valley Water's tariffs are regulated under a revenue cap. This means the revenue Yarra Valley Water can earn is fixed at the start of the regulatory period, but customer prices may vary annually – within pre-defined limits – so the business can meet its revenue requirement. The prices determined for 2023-24 are fixed, noting later prices can vary within the constraints of its revenue cap. As noted below, this includes a nominal cap on water and sewerage prices in 2024-25.

Subject to its revenue cap, water and sewerage prices for residential and non-residential customers will generally fall by around 1.6 per cent in 2024-25, excluding inflation, before moving in line with inflation in the following 3 years.

³ Along with forecast demand, the revenue requirement is an input to calculating the prices to be charged by a water business.

Table A Estimated typical annual water and sewerage bills

Customer group	Average consumption (kL p.a.)	2022-23 (current)	2023-24
		\$2022-23	\$2023-24
Residential – owner occupier	150	\$1,028	\$1,049
Residential – tenant	150	\$498	\$508
Non-residential (small)	150	\$1,569	\$1,601
Non-residential (medium)	1,000	\$5,604	\$5,720
Non-residential (large)	10,000	\$48,332	\$49,330

Note: The table shows the average bills for 2023-24 expressed in \$2023-24 terms (which means 7 per cent inflation has been included). Our draft decision included bill estimates based on our draft decision revenue requirement, expressed in \$2022-23 terms as the inflation figure was not available at this time. Our determination for Yarra Valley Water sets prices in \$2023-24 terms, with provision for inflation to be added in each of the remaining years of the regulatory period based on the latest inflation data. Dollar amounts have been rounded. Non-residential prices have been calculated based on volumes provided by Yarra Valley Water.

Yarra Valley Water has evolved its outcomes to reflect customer priorities, including a focus on Caring for Country

Yarra Valley Water plans to deliver the following outcomes for customers:

- Safe and pleasant drinking water
- Reliable water and sewerage services
- Timely response and repair
- Service that meets everyone’s needs
- Saving water for the future
- Looking after our natural environment.⁴

These have been refined by Yarra Valley Water since its 2018 review, informed by its engagement. It will embed Caring for Country in all decisions, including its approach to delivering on its outcome commitments and targets. Service improvements are focused in areas such as investing in climate resilience including reducing carbon emissions (targeting a net zero position by 2025) and enhancing asset security, and water quality. This is in addition to investments to respond to growth in its region and maintaining best practice in customer support programs.

⁴ Yarra Valley Water, 2023 price submission, September 2022, pp. 37–56.

Tariff structures will generally remain the same, noting Yarra Valley Water will simplify charges for residential customers

Our final decision approves Yarra Valley Water's proposed tariff structures.

Our final decision approves Yarra Valley Water's proposal to combine its residential sewage disposal charge and its residential variable water charge. This was justified by Yarra Valley Water based on simplicity, and that it is supported by customers. We agree with its justification.

Our final decision is to approve other water and sewerage tariff structures proposed by Yarra Valley Water. We note they remain unchanged and generally supported by customers, and otherwise meet the requirements of our guidance.

Our final decision is to accept Yarra Valley Water's proposed revenue cap form of price control (Section 5.2). This means its revenue is capped subject to annual updates for demand, the cost of debt, changes in bulk charges, and any other price adjustments we approve in our price determination (Section 5.5). Its proposal included a nominal cap on changes in prices for 2023-24 and 2024-25 of 5 per cent.

We have rated Yarra Valley Water's price submission as 'Advanced' under the PREMO framework

Consistent with our draft decision, our final decision is to rate Yarra Valley Water's price submission as 'Advanced' under the PREMO framework (Table B). This is the same as Yarra Valley Water's self-rating. Factors in support of Yarra Valley Water's PREMO rating include, that it implemented a strong engagement program which indicates that its proposals are informed by deep insights into customer priorities and concerns, and it proposed a relatively high operating cost efficiency target contributing to real price reductions for customers and improved value consistent with an 'Advanced' price submission. Yarra Valley Water also provided a price submission and supporting model that were of a high quality.

See Section 1.4 for an explanation of the PREMO framework and Chapter 7 for more detail on our assessment of Yarra Valley Water's price submission.



Our PREMO rating is an assessment of the water business's price submission and its ambition to deliver outcomes valued by its customers. It is not an assessment of the water business itself.

Table B **PREMO rating**

	Overall PREMO rating	Performance	Risk	Engagement	Management	Outcomes
Yarra Valley Water's self-rating	Advanced	Advanced	Advanced	Leading	Advanced	Advanced
Commission's rating	Advanced	Advanced	Advanced	Leading	Advanced	Advanced

1. Our role and approach to water pricing

1.1 We are Victoria's independent economic regulator

Our role in the water industry is based on the Water Industry Regulatory Order 2014 (WIRO), which is made under the *Water Industry Act 1994* (WI Act) and sits within the broader context of the *Essential Services Commission Act 2001* (ESC Act). Our role under the WIRO includes regulating the prices and monitoring service standards of the 18 water businesses operating in Victoria.

1.2 We are reviewing the proposed prices of 14 water businesses

Our review is of the prices that the 14 water businesses propose to charge customers for prescribed services from 1 July 2023.⁵ The prescribed services include retail water and sewerage services, and bulk water and sewerage services delivered by the water businesses.⁶

Yarra Valley Water provided a submission to us proposing prices for a 5-year period starting 1 July 2023. Our task is to assess the price submission using the legal framework and make a price determination that takes effect from 1 July 2023. We make a price determination after issuing a draft decision and considering feedback from interested parties, including any response to the draft decision from the water business.

The price determination specifies the maximum prices a water business may charge for prescribed services, or the manner in which prices are to be calculated, determined or otherwise regulated. We also issue a final decision that sets out our supporting reasons for our price determination.

1.3 We assess prices against the WIRO and other legal requirements

Clause 11 of the WIRO specifies the mandatory matters we must have regard to when making a price determination, including matters set out in the WIRO, the WI Act and the ESC Act, and clause 8 of the WIRO requires that we place particular emphasis on the promotion of efficiency related matters. In making a price determination, we have had regard to each of the matters required by clause 11 of the WIRO, including:

- the objectives and matters specified in clause 8 of the WIRO, which include economic efficiency and viability matters, industry specific matters, customer matters, health, safety, environmental

⁵ The review excludes Melbourne Water, Goulburn-Murray Water, North East Water and Greater Western Water. In 2021 we approved prices for Melbourne Water to 30 June 2026 and in 2020 we approved prices for Goulburn-Murray Water to 30 June 2024. In 2018, we approved prices for North East Water to 30 June 2026. We have approved an extension to the regulatory period for Greater Western Water to 30 June 2024.

⁶ The prescribed services are listed at clause 7(b) of the WIRO.

and social matters, and other matters which are specified in sections 8 and 8A of the ESC Act and section 4C of the WI Act

- the matters set out in section 33(3) of the ESC Act, which include the return on assets, relevant benchmarking and any other matters that the ESC considers relevant
- the matters specified in our guidance⁷
- the principle that prices should be easily understood by customers and provide signals about the efficient costs of providing services, while avoiding price shocks where possible
- the principle that prices should take into account the interests of customers of the regulated entity, including low income and vulnerable customers.

Appendix B lists the specific objectives and the various matters we must have regard to when making a price determination and provides a guide to where we have done so for our final decision for Yarra Valley Water. Table 1.1 summarises the matters we must have regard to and groups them into themes.

In October 2021, we issued guidance to water businesses, including Yarra Valley Water to inform their price submissions. The guidance set out how we would assess Yarra Valley Water's submission against the matters we must consider under clause 11 of the WIRO. It also outlined our expectation that Yarra Valley Water would comply with certain requirements and specified information that Yarra Valley Water must provide to us when submitting its price submission.⁸

If we consider the price submission has adequate regard for the matters in clause 11 of the WIRO and complies with our guidance, we must approve Yarra Valley Water's maximum proposed prices it can charge for the prescribed services it provides.⁹

If we consider the submission does not have adequate regard for the matters specified in clause 11 of the WIRO or does not comply with our guidance, we may specify maximum prices, or the manner in which prices are to be calculated, determined or otherwise regulated.¹⁰



The power for water businesses to charge fees for services they provide is set out in the *Water Act 1989*.¹¹ These provisions in the Water Act also govern the processes and manner in which water businesses may set and impose fees. Each water business must ensure that it complies with these legislative requirements.

⁷ Essential Services Commission, *2023 water price review: Guidance paper*, 26 October 2021.

⁸ Among these expectations are matters that progress our 'Getting to fair' strategy relating to the water industry. See Essential Services Commission, *Getting to fair: Breaking down barriers to essential services*, August 2021.

⁹ This is a requirement of the WIRO, clause 14(a).

¹⁰ This is provided for under the WIRO, clause 14(b)(i).

¹¹ See Part 13, Division 5 and 6 of the Water Act 1989.

Table 1.1 Matters businesses and the commission must have regard to

Economic efficiency and viability matters	Industry/business specific matters	Customer matters
<ul style="list-style-type: none"> • promotion of efficient use of prescribed services by customers [cl 8(b)(i), WIRO] • promotion of efficiency in regulated entities as well as efficiency in, and the financial viability of, the regulated water industry [cl 8(b)(ii), WIRO] • provision to regulated entities of incentives to pursue efficiency improvements [cl 8(b)(iii), WIRO] • efficiency in the industry and incentives for long term investment [s. 8A(1)(a), ESC Act] • efficient costs of producing or supplying regulated goods or services and of complying with relevant legislation and relevant health, safety, environmental and social legislation applying to the regulated industry [s. 33(3)(b), ESC Act] • financial viability of the industry [s. 8A(b)(1), ESC Act] 	<ul style="list-style-type: none"> • particular circumstances of the regulated industry and the prescribed goods and services for which the determination is being made [s. 33(3)(a), ESC Act] • return on assets in the regulated industry [s. 33(3)(c), ESC Act] • ensure that regulatory decision making and regulatory processes have regard to any differences between the operating environments of regulated entities [s. 4C(b), WI Act] 	<ul style="list-style-type: none"> • in performing its functions and exercising its powers, the objective of the Commission is to promote the long-term interests of Victorian consumers [s. 8(1), ESC Act] without derogating from that objective. The Commission must in seeking to achieve the objective have regard to the price, quality and reliability of essential services [s. 8(2), ESC Act] • 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 [cl 11(d)(i), WIRO] • 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 [cl 11(d)(ii), WIRO] • take into account the interests of customers of the regulated entity, including low income and vulnerable customers [cl 11(d)(iii), WIRO]

Continued next page

Table 1.1 (continued)

Benchmarking	Health, safety, environmental and social obligations	Other
<ul style="list-style-type: none"> any relevant interstate and international benchmarks for prices, costs and return on assets in comparable industries [s. 33(3)(d), ESC Act] 	<ul style="list-style-type: none"> the relevant health, safety, environmental and social legislation applying to the industry [s 8A(1)(d), ESC Act] to ensure that regulatory decision making has regard to the health, safety, environmental sustainability (including water conservation) and social obligations of regulated entities [s. 4C(c), WI Act] 	<ul style="list-style-type: none"> the degree of, and scope for, competition within the industry, including countervailing market power and information asymmetries [s. 8A(1)(c), ESC Act] consistency in regulation between States and on a national basis [s. 8A(1)(f), ESC Act] the benefits and costs of regulation (including externalities and the gains from competition and efficiency) for—(i) consumers and users of products or services (including low income and vulnerable consumers) (ii) regulated entities [s. 8A(1)(e), ESC Act] wherever possible, to ensure that the costs of regulation do not exceed the benefits [s. 4C(a), WI Act]

Note: References in the table are to the Water Industry Regulatory Order 2014 (WIRO), the Essential Services Commission Act 2001 (ESC Act), and the Water Industry Act 1994 (WI Act).

1.4 PREMO

PREMO stands for Performance, Risk, Engagement, Management, and Outcomes. Each element of PREMO is summarised in Box 1.1.

Box 1.1 PREMO

Water businesses must demonstrate their level of ambition in delivering value for money for customers in their price submissions across the five PREMO elements:

- Performance — have the performance outcomes to which the business committed in the previous regulatory period been met or exceeded?
- Risk — has the business sought to allocate risk to the party best positioned to manage that risk? To what extent has the business accepted risk on behalf of its customers?
- Engagement — how effective was the business's customer engagement to inform its price submission?
- Management — is there a strong focus on efficiency? Are controllable costs increasing, staying the same, or decreasing? Is the price submission succinct and free of material errors?
- Outcomes — do proposed service outcomes represent an improvement, the status quo, or a reduction of service standards?

First introduced at our 2018 water price review, the purpose of PREMO is to provide incentives for water businesses to deliver outcomes most valued by customers. PREMO includes reputation incentives, via the rating of price submissions as Leading (the highest available rating), Advanced, Standard or Basic, depending on the level of ambition expressed by a water business in its price submission. Financial incentives are provided by linking the return on equity to the PREMO rating.

A key priority under PREMO is to provide incentives for a water business to engage with customers to understand their priorities and concerns and to take these into account in forming the proposals outlined in its price submission. This should be evidenced in price submissions by linking the outcomes proposed with findings from a business's engagement.

Our guidance specifies the way in which we expect water businesses to assess themselves by reference to the PREMO elements.

Our PREMO framework rewards stronger customer value propositions in price submissions, and an early draft decision is available for price submissions we can assess in a short timeframe.¹²

¹² In December 2022, we issued early draft decisions for Yarra Valley Water and Westernport Water.

For the 2023 water price review, a water business’s ambition in terms of delivering customer value is being assessed against all five elements of PREMO — Performance, Risk, Engagement, Management and Outcomes. This is the first water price review where we are assessing the Performance element of the PREMO framework. The Performance element assesses businesses against their Outcomes and proposals from the previous price review (for our 2023 review, this means proposals at the 2018 water price review). We did not assess the Performance element in 2018 because it was the first time that we had applied the PREMO framework and so we did not have a set of approved Outcomes to inform our assessment.

Taking into account all five elements of PREMO, a water business must self-assess and propose a rating for its price submission as ‘Leading’, ‘Advanced’, ‘Standard’ or ‘Basic’. Its proposed return on equity will then reflect its proposed PREMO rating. A ‘Leading’ submission has the highest return on equity, and a ‘Basic’ submission the lowest. We assess the self-rating and also assess the price submission more broadly, including the water business’s justification for the proposed PREMO rating, and form our own view of the appropriate rating. This process determines the PREMO rating adopted and the return on equity reflected in the revenue requirement.¹³

¹³ Essential Services Commission, *2023 water price review: Guidance paper*, pp. 41–46.

2. Our assessment of Yarra Valley Water's price submission

We have made our final decision on Yarra Valley Water's price submission after considering:

- Yarra Valley Water's price submission
- Yarra Valley Water's presentation made directly to commissioners
- Yarra Valley Water's responses to our queries and our draft decision
- our consultants' reports
- the views of participants in our public forum held on 23 February 2023¹⁴
- written submissions from interested parties (a list of submissions responding to our draft decision is provided in Appendix A).

Any reports, submissions or correspondence provided to us that are material to our consideration of Yarra Valley Water's price submission are available on our website (to the extent the material is not confidential).

Our guidance included matters water businesses must address in their price submissions. Yarra Valley Water's price submission addressed each of these matters, and our initial assessment of those matters is set out in our draft decision.

We consulted on our draft decision, receiving submissions between 20 December 2022 and 10 March 2023 and holding an online public forum on 23 February 2023. Questions raised and answered by Yarra Valley Water during the forum included questions relating to environmental water flows and the link between prices and water use.

In terms of environmental water flows, it is the responsibility of Yarra Valley Water to manage water flows and sources – we do not have powers related to water management. Our guidance required that water businesses must propose a revenue requirement that provides them with sufficient revenue to efficiently meet its legislative, regulatory and policy obligations.¹⁵ We are limited to assessing the expenditure proposed by a water business in its price submission. Further, the expenditure benchmarks that we adopt to determine prices do not represent the amount that the water business is required to spend or allocate to particular projects or activities. Rather, it represents assumptions about the overall level of expenditure (to be recovered through prices) that we consider sufficient to operate the business and to maintain or improve services over the

¹⁴ A recording of this forum is available on our website.

¹⁵ The Statements of Obligations (General) issued by the Minister for Water includes obligations on water businesses relating to management of water resources, minimising environmental impacts, and compliance with any Sustainable Water Strategy.

regulatory period. Yarra Valley Water will determine how to best manage the allocation of its revenue and priority of its expenditure within a regulatory period.

Yarra Valley Water provided a response to our draft decision, including a revised financial model that reflected the updated cost of debt and inflation figures we provided to businesses in May 2023.¹⁶ In arriving at our final decision, we have considered Yarra Valley Water's responses to our draft decision.

This paper sets out our final decision.

2.1 Final decision paper outline

This final decision paper is structured around the steps we have taken to arrive at our price determination. In summary, these steps were:

- Determine the regulatory period (Section 2.2).
- Confirm the customer outcomes and service levels that Yarra Valley Water has committed to over the regulatory period (Chapter 3).
- Establish Yarra Valley Water's revenue requirement using a building block methodology (Chapter 4).
- Use demand forecasts and the form of price control to convert the revenue requirement to tariffs and prices (Chapter 5).

Chapter 6 outlines our consideration of Yarra Valley Water's financial position, which we have also had regard to.

Chapter 7 outlines our assessment of Yarra Valley Water's price submission under the PREMO framework.

Unless otherwise noted, all financial values referred to in this final decision paper are in \$2022-23, which means inflation is excluded.

¹⁶ All references to Yarra Valley Water's price submission in this document refer to Yarra Valley Water's original price submission that it provided to us in September 2022 rather than its response to our draft decision.

2.2 Regulatory period

Our final decision is to approve a regulatory period of 5 years from 1 July 2023.

We are required to set the term of the regulatory period over which a water business's price determination will apply.¹⁷ Our guidance proposed that we set a 5-year regulatory period, but also noted we were open to justified alternatives proposed in a price submission.¹⁸

Yarra Valley Water proposed, and our draft decision approved, a regulatory period of 5 years.

In a submission on our draft decisions, the Consumer Action Law Centre supported our proposed 5-year regulatory period. It noted that a 5-year period provided customers with predictability around billing and services and that having a uniform period across all businesses included in our current review meant it would be easier to generate public awareness and engagement.¹⁹

Accordingly, consistent the reasons outlined in our guidance, and as proposed in our draft decision, our final decision is to set a regulatory period of 5 years.

¹⁷ This is a requirement of the WIRO, clause 9.

¹⁸ For detail on the reasons for using 5 years as the default regulatory period, see: Essential Services Commission, *2023 water price review: Guidance paper*, p. 18.

¹⁹ Consumer Action Law Centre, *Feedback on standard draft decisions: 2023 Water Price Review*, 5 May 2023, p. 4.

3. Customer outcomes

The customer outcomes Yarra Valley Water plans to deliver over the regulatory period is a key component of its price submission – confirming its commitments to customers, underpinning its revenue requirement, and feeding in to its PREMO assessment.

This chapter outlines our views on:

- Yarra Valley Water’s engagement with its customers in preparing its price submission (Section 3.1)
- whether Yarra Valley Water has delivered on the outcomes it committed to for the current regulatory period (2018–23) and the customer outcomes Yarra Valley Water is committing to for the next regulatory period (Section 3.2)
- Yarra Valley Water’s service standards for the regulatory period (Section 3.3)
- Yarra Valley Water’s proposed guaranteed service level scheme for the regulatory period (Section 3.4).

3.1 Customer and community engagement

Our guidance required Yarra Valley Water to engage with customers to inform its price submission. Our guidance also identified principles to guide Yarra Valley Water’s engagement.²⁰

As outlined in our draft decision, we consider Yarra Valley Water’s engagement with customers and community aligned with these principles in a number of ways. Yarra Valley Water’s engagement was:

- wide reaching and involved over 39,000 customer and community interactions since the previous price review in 2018
- inclusive and used a range of engagement methods including co-design to set the context and direction of engagement, a citizens’ jury, willingness to pay studies, workshops and panels
- tailored to the circumstances of its customers and community, including targeted engagement with First Nations customers and Traditional Owners and people more likely to experience vulnerability.

Our draft decision outlined several ways in which Yarra Valley Water demonstrated that its engagement influenced its proposals. These included:

²⁰ Essential Services Commission, *2023 water price review: Guidance paper*, p. 20. This guidance includes a focus on engagement by businesses with First Nations people and people experiencing vulnerability which are actions identified in our ‘Getting to fair’ strategy. See Essential Services Commission, *Getting to fair: Breaking down barriers to essential services*, August 2021.

- engaging on water quality and reliability of services, bills and affordability, customer support and communications, and water conservation and the environment
- the development of a formal partnership agreement with Wurundjeri Woi Wurrung Cultural Heritage Aboriginal Corporation as the Traditional Custodian/Owner of its service area, and developing ongoing relationships and an advisory forum with Aboriginal communities
- adapting its approach to digital meters and its stewarding water conservation initiatives.

Our preliminary view was to accept Yarra Valley Water's 'Leading' self-rating for the Engagement element of PREMO on the basis it had designed and delivered a high-quality engagement program and achieved strong customer and stakeholder influence on the proposals in its submission.

Examples outlined in our draft decision included:

- the role of stakeholders in shaping the context and direction of the engagement through co-design on key aspects of its citizens' jury
- the Aboriginal Community Working Group self-determining their role and scope for their involvement in the citizens' jury process
- its extensive effort to elevate diverse voices into its decision-making process, including by providing translation services such as Auslan interpreters and arranging methods to support inclusive participation to gain insights from people experiencing vulnerability.

We have considered all submissions received in response to our draft decision. Our final decision is the same as our draft decision, which is to accept Yarra Valley Water's self-rating of 'Leading' for its price submission engagement.

See Chapter 7 for more detail on our PREMO assessment of Yarra Valley Water's price submission.

3.2 Outcomes

Yarra Valley Water's proposed set of outcomes indicates the value its customers can expect to receive during the next regulatory period. Actual performance against output measures and targets is monitored during the regulatory period to demonstrate whether customers are receiving the value they paid for. It also informs the rating for the 'Performance' element of PREMO at the next price review.

Yarra Valley Water proposed to deliver the following outcomes over the regulatory period starting 1 July 2023:

- Safe and pleasant drinking water
- Reliable water and sewerage services
- Timely response and repair
- Service that meets everyone's needs
- Saving water for the future

Customer outcomes

- Looking after our natural environment.

Yarra Valley Water's proposed measures and targets that it will use to report on the performance for each outcome are detailed on pages 42 to 56 of its price submission.

In our draft decision, we agreed with Yarra Valley Water's self-assessment that it has, overall, met its outcome commitments for the 2018–23 period to date, and that its reporting to customers during this period met our requirements.

We considered its proposed set of outcomes for 2023–28 demonstrated an overall improvement in customer value and was consistent with the requirements of an 'Advanced' rating for the Outcomes element of PREMO. In response to our draft decision, we received one anonymous submission, which supported our view on Yarra Valley Water's proposed outcomes.²¹

In our draft decision, we noted that some of Yarra Valley Water's proposed outcome measures and targets were not presented in a manner consistent with our guidance requirements. We have worked with Yarra Valley Water to ensure its final set of measures and targets meets the requirements set out in our guidance. In response to our draft decision, Yarra Valley Water amended its outcome measures and targets.

Following the release of this final decision, we will publish the 2023–28 outcomes reporting template for all water businesses participating in this price review, and we expect water businesses to publish them prominently on their own websites.

Our assessment of Yarra Valley Water's outcomes, measures and targets has informed our final decision rating of its price submission for the Outcomes element of PREMO, which is discussed in Chapter 7.

3.3 Service standards related to service reliability and faults

Yarra Valley Water provided a list of service standards relating to reliability and attending faults that it will include in its customer charter. Service standards are a common set of services applicable to all Victorian consumers as required by clause 18.2 of the Water Industry Standard – Urban Customer Service (Urban Water Industry Standard). Each water business must specify its own targets against each of these service standards. These service standards and corresponding target service levels are the minimum level of service customers can expect to receive.

Yarra Valley Water's proposed service standards relating to reliability and faults can be found on page 60 of its price submission, with the exception of the minimum flow rates which can be found on the outcomes tab of its price review model.

²¹ Anonymous, *submission to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 14 February 2023.

The service standards proposed by Yarra Valley Water are the same as those for the current 2018-23 regulatory period (with some wording changes required by the updated Urban Water Industry Standard). The target service levels proposed are, in general, an improvement on the target service levels for the current regulatory period. Yarra Valley Water has also specified the minimum flow rates as required by the Urban Water Industry Standard.

On the basis of the above, our assessment is that the service standards relating to reliability and faults proposed by Yarra Valley Water comply with the requirements of the Urban Water Industry Standard.

These service standards and Yarra Valley Water's targets until 2028 are set out in Appendix C.

Service standards are set out in our Urban Water Industry Standard. Accordingly, in early 2023-24, we will update the Urban Water Industry Standard to reflect targets set by the water business.

3.4 Guaranteed service levels

Our final decision is to adopt the amended guaranteed service levels as set out in Appendix D.

Guaranteed service levels define a water business's commitment to deliver a specified level of service. For each guaranteed service level, typically a water business commits to a payment or a rebate on bills to those who have received a level of service below the guaranteed level.

Yarra Valley Water's proposed guaranteed service levels are set out on pages 61 and 62 of its price submission, and in a letter submitted to us on 30 November 2022 which is available on our website.²²

Our draft decision summarised Yarra Valley Water's proposed changes to its guaranteed service levels in its scheme from July 2023, which included proposed new guaranteed service level for water quality events and a bottled water refund process for water quality events. We stated that final guaranteed service levels and rebates would be subject to any feedback on our draft decision, and further information on Yarra Valley Water's proposal for a new guaranteed service level focussed on water quality and protocols for when rebates would apply.

In its response to our draft decision, Yarra Valley Water provided further information on its proposed new guaranteed service level for water quality events.²³ This information included details of when a community rebate would apply, the rebate value and the protocols for applying this

²² Yarra Valley Water, Additional information on 2023 water price submission: Water quality GSL, 30 November 2022.

²³ Yarra Valley Water, *submission in response to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 10 March 2023, pp. 1-2.

rebate. It also provided information about a refund scheme for bottled water purchased during a water quality event and how the claim process would operate.

The information contains sufficient detail on the protocol for when and how the community rebate will be applied which has satisfied us that it meets the criteria outlined in our guidance.²⁴

After considering all submissions received following our draft decision, on the basis of the above, our final decision is to adopt the amended guaranteed service levels outlined in Appendix D. Guaranteed service levels are approved in our Urban Water Industry Standard. Accordingly, in early 2023-24, we will update the Urban Water Industry Standard to reflect the guaranteed service levels set out in Appendix D.

²⁴ Essential Services Commission, 2023 water price review: Guidance paper, 26 October 2021, pp. 25 and 26

4. Revenue requirement

The revenue requirement is the forecast amount a water business needs to deliver on customer outcomes, government policy, statements of obligations, and obligations monitored by technical regulators including the Environment Protection Authority Victoria and the Department of Health.²⁵ Along with forecast demand, it is an input to calculating prices.

We have used a building block methodology to establish the revenue requirement. This chapter outlines our assessment of Yarra Valley Water's revenue requirement based on the following steps:

- establish an efficient benchmark level of forecast operating expenditure for the next regulatory period (Section 4.1)
- establish an efficient benchmark level of forecast capital expenditure for the next regulatory period (Section 4.2)
- roll-forward the regulatory asset base (Section 4.3)
- apply a rate of return to the regulatory asset base, calculated using:
 - a benchmark cost of debt estimated using a 10-year trailing average approach (Section 4.4.1)
 - a benchmark return on equity value determined by Yarra Valley Water's PREMO rating (Section 4.4.2)
- establish a return of capital through a regulatory depreciation allowance (Section 4.5)
- establish a benchmark tax allowance (Section 4.6).

Our final decision is to approve a revenue requirement of \$4,947.5 million.

Yarra Valley Water proposed a revenue requirement of \$4,894.9 million over a 5-year period starting 1 July 2023. Our draft decision approved a slightly lower revenue requirement of \$4,891.0 million, subject to our ongoing review of Yarra Valley Water's proposed new customer contributions and revenue from customer contributions. Our final decision approves a revenue requirement of \$4,947.5 million (Table 4.1), which reflects our assessment of each element of the revenue requirement, including forecast operating and capital expenditure.

²⁵ We met with officers of the Department of Energy, Environment and Climate Action, the Department of Health, and the Environment Protection Authority Victoria, to discuss their expectations of Yarra Valley Water in the regulatory period from 1 July 2023. We had regard to their views in arriving at our final decision.

Table 4.1 Final decision on Yarra Valley Water’s revenue requirement

\$ million 2022-23

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Operating expenditure	707.4	702.2	702.4	689.6	687.5	3,489.0
Return on assets	135.5	136.0	146.9	159.0	171.0	748.3
Regulatory depreciation	135.7	127.3	126.3	133.3	137.4	660.0
Adjustments from last period ^a	-1.7	-	-	-	-	-1.7
Tax allowance	11.0	9.4	9.4	10.6	11.4	51.7
Final decision – revenue requirement	987.9	974.9	985.0	992.4	1,007.3	4,947.5

Note: Numbers have been rounded. ^a This adjustment relates to the return of money to customers due to the non-achievement of one performance target.

Since our draft decision, we have updated our estimates for the cost of debt, inflation, licence fees and environmental contribution to reflect the latest available information. We required Yarra Valley Water to update its revenue requirement and prices to reflect updates to inflation and the cost of debt and we updated the licence fee and environmental contribution estimates.

Yarra Valley Water also updated its bulk water charges to reflect the latest information and, in response to our draft decision, also updated its forecast energy costs. These updates are discussed in Section 4.1.

Yarra Valley Water also updated its forecast operating expenditure to reflect changes announced in the 2023-24 Victorian State Budget (see Section 4.1).

The main reason for the increase in our final decision revenue requirement compared to our draft decision is the updated estimate for the cost of debt which reflects the rise in borrowing costs since Yarra Valley Water prepared its price submission.

The adjustments to Yarra Valley Water’s revenue requirement that we have made in our draft and final decisions are set out in Table 4.2, with the reasons outlined in the following sections.

Table 4.2 Adjustments to revenue requirement – our draft and final decisions

\$ million 2022-23

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
A. Yarra Valley Water's proposed revenue requirement	1,002.4	973.6	973.7	970.7	974.5	4,894.9
B. Total adjustments proposed in our draft decision	-3.9	-	-	-	-	-3.9
Adjustments from last period ^a	-3.3	-	-	-	-	-3.3
Tax allowance	-0.6	-	-	-	-	-0.6
C. Draft decision – revenue requirement (C = A+B)	998.5	973.6	973.7	970.7	974.5	4,891.0
D. Total adjustments in our final decision	-10.7	1.4	11.2	21.7	32.8	56.5
Operating expenditure	-1.7	1.4	1.1	0.5	0.6	1.9
Return on assets	-6.3	2.6	12.7	23.7	34.6	67.4
Regulatory depreciation ^b	-0.0	-0.0	-0.0	-0.0	-0.0	-0.0
Tax allowance	-2.7	-2.7	-2.6	-2.5	-2.4	-12.8
E. Final decision – revenue requirement (E = C + D)	987.9	974.9	985.0	992.4	1,007.3	4,947.5

Note: Row A shows the total revenue requirement proposed by Yarra Valley Water in its price submission. Row B shows the total difference between our draft decision and what Yarra Valley Water proposed in its price submission. Row C shows the total revenue requirement we adopted in our draft decision. Row D shows the total difference between our final decision (row E) and our draft decision. ^a This adjustment relates to the return of money to customers due to the non-achievement of one performance target. ^b An update to revenue from customer contributions led to a minor adjustment to regulatory depreciation.

4.1 Operating expenditure

Our final decision is to adopt a forecast operating expenditure of \$3,489.0 million for Yarra Valley Water for the 2023–28 regulatory period.

Operating expenditure – comprising both controllable and non-controllable expenditure – is a component of the revenue requirement. Our draft decision proposed to adopt a forecast operating expenditure of \$3,487.1 million for the 5-year period, as proposed by Yarra Valley Water.

Table 4.3 sets out our final decision on Yarra Valley Water’s forecast operating expenditure, for the purpose of establishing the revenue requirement outlined in Table 4.1.

Table 4.3 Final decision – operating expenditure

\$ million 2022-23

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
Controllable operating expenditure	162.34	162.27	162.97	162.53	164.71	814.82
Non-controllable operating expenditure	545.03	539.91	539.40	527.07	522.80	2,674.22
Bulk services ^a	497.96	494.42	495.43	484.57	481.73	2,454.11
Environmental contribution ^b	45.83	44.28	42.78	41.33	39.93	214.15
Licence fees – Essential Services Commission ^c	0.85	0.82	0.79	0.76	0.74	3.96
Licence fees – Department of Health ^c	0.30	0.30	0.30	0.30	0.30	1.49
Licence fees – Environment Protection Authority ^c	0.10	0.10	0.10	0.10	0.10	0.51
Final decision – operating expenditure	707.37	702.18	702.38	689.60	687.51	3,489.04

Notes: Numbers have been rounded. ^a Bulk services covers the supply of bulk water and sewerage services.

^b Environmental contributions are funds collected from water businesses under the *Water Industry Act 1994*. ^c Licence fees are paid to cover costs incurred by the Department of Health, the Environment Protection Authority Victoria, and the Essential Services Commission in their regulatory activities related to the water business.

Table 4.4 sets out the adjustments we have made to controllable and non-controllable operating expenditure for our draft decision, and since our draft decision. Details of our assessment and the reasons for our adjustments are included in Section 4.1.1 (controllable operating expenditure) and Section 4.1.2 (non-controllable operating expenditure).

The operating expenditure that we have adopted for Yarra Valley Water does not represent the amount that Yarra Valley Water is required to spend or allocate to particular operational,

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maintenance and administrative activities. Rather, it is a benchmark that represents assumptions about the overall level of operating expenditure (to be recovered through prices) that we consider sufficient to operate the business efficiently, meet its legislative and policy objectives, and to maintain services over the regulatory period.

Table 4.4 Our adjustments to Yarra Valley Water’s operating expenditure for our draft and final decisions
\$ million 2022-23

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
A. Yarra Valley Water’s proposed total operating expenditure	709.08	700.78	701.27	689.09	686.88	3,487.10
A1 – Our draft decision adjustments to controllable operating costs	-	-	-	-	-	-
A2 – Our draft decision adjustments to non-controllable operating costs	-	-	-	-	-	-
B. Draft decision – total operating expenditure	709.08	700.78	701.27	689.09	686.88	3,487.10
C. Final adjustments to controllable operating costs (C1 + C2 + C3)	0.76	1.89	1.70	1.23	1.80	7.38
C1 – Updated growth costs	0.43	0.47	0.53	0.58	0.62	2.63
C2 – Electricity prices adjustment	-0.08	0.99	0.72	0.20	0.73	2.57
C3 – 2023-24 State Budget updates	0.40	0.44	0.45	0.45	0.45	2.18

Continued next page

Table 4.4 (continued)

	2023-24	2024-25	2025-26	2026-27	2027-28	Total
D. Final adjustments to non-controllable operating costs (D1 + D2 + D3 + D4 +D5)	-2.47	-0.49	-0.60	-0.72	-1.16	-5.44
D1 – Environmental contribution	-0.22	-0.43	-0.63	-0.81	-0.98	-3.07
D2 – Licence fees – Essential Services Commission	-0.03	-0.06	-0.09	-0.12	-0.44	-0.74
D3 – Licence fees – Department of Health	-0.01	-0.01	-0.01	-0.01	-0.01	-0.06
D4 – Licence fees – Environment Protection Authority	0.00	0.00	0.00	0.00	0.00	0.01
D5 – External bulk water charges – Melbourne Water	-2.21	0.01	0.13	0.21	0.27	-1.58
E. Final decision – total operating expenditure (E = B + C + D)	707.37	702.18	702.38	689.60	687.51	3,489.04

Note: The adjustments shown in rows C and D (and disaggregated in rows C1 to C3 and rows D1 to D5) are the differences between our draft decision and our final decision and are outlined in Section 4.1.1 (controllable operating expenditure) and Section 4.1.2 (non-controllable operating expenditure) of this final decision. Numbers have been rounded.

4.1.1 Controllable operating expenditure

In relation to controllable operating expenditure, our preliminary findings (outlined in Section 4.1.1 of our draft decision) were that:

- We considered Yarra Valley Water’s proposal reflects an efficient baseline cost to forecast annual operating expenditure.
- Yarra Valley Water had proposed a relatively high efficiency improvement rate of 1.7 per cent per year, of which it planned to absorb approximately \$38.4 million in costs over the next regulatory period compared to the proposed cost adjustments of \$31.9 million to account for growth related costs.
- This approach effectively delivers a net efficiency rate of 0.26 per cent per year and a small decrease to Yarra Valley Water’s controllable annual baseline operating cost in each year of the regulatory period.

- There is evidence that Yarra Valley Water has significantly tested its controllable expenditure requirements and that forecast cost adjustment additions were prudent and efficient.

In response to our draft decision, Yarra Valley Water has updated its demand forecast based on recently updated Victorian Government population and dwelling growth estimates, which resulted in adjustments to Yarra Valley Water's operating expenditure growth forecast for 2022-23, and its growth costs step change for the next regulatory period.²⁶

Yarra Valley Water's revised forecast produces a \$2.6 million increase in controllable operating expenditure for the next regulatory period and a reduction of 0.5 per cent in customer prices for 2023-24, as discussed in Section 5.3. We consider that this adjustment is appropriate because it reflects our requirement to consider the latest updated Victorian Government growth estimates.

In a further response to our draft decision, Yarra Valley Water updated its proposed forecast energy costs to reflect the latest electricity price forecasts, which result in an additional \$2.57 million of operating expenditure across the next regulatory period.²⁷ Yarra Valley Water provided information substantiating its exposure to movements in electricity prices later in the next regulatory period, its current contract positions for electricity across the next regulatory period, in which its forecast electricity demand for 2024-25, 2026-27 and 2027-28 are uncontracted.

While this is a relatively minor cost adjustment for Yarra Valley Water, we recognise that because Yarra Valley Water's approach is to tightly forecast its growth costs, rather than using a growth factor, it has little scope to absorb this change in the revenue requirement that we approved in our draft decision. For these reasons, and because the increase will have no material impact on customer prices, we have accepted the increase requested by Yarra Valley Water.

Following release of the 2023-24 Victorian State Budget on 23 May, we wrote to water businesses to provide them with an opportunity to update their cost forecasts, should they seek to claim any additional costs and reflect these in customer prices.²⁸

Yarra Valley Water responded with updated cost forecasts to reflect higher payments relating to payroll tax, land tax and WorkCover premiums. We have accepted these additional amounts as they are unavoidable costs that the business faces in delivering prescribed services to its customers.

²⁶ Yarra Valley Water, *submission in response to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 10 March 2023, p. 5.

²⁷ Yarra Valley Water, *further information and revised proposal in response to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 10 May 2023, pp. 2–3.

²⁸ Victorian Government, *Budget papers '2023/24 State Budget papers'*, 23 May 2023.

Accordingly, our final decision is to accept Yarra Valley Water's revised forecast controllable operating expenditure of \$814.82 million on the basis that it is consistent with our guidance.

4.1.2 Non-controllable operating expenditure

In relation to non-controllable operating expenditure, our preliminary findings (outlined in Section 4.1.2 of our draft decision) were:

- Yarra Valley Water had followed the approach set out in our guidance paper to forecast its non-controllable operating costs in its price submission.
- Yarra Valley Water's forecast bulk charges were consistent with Melbourne Water's 2021 price determination.

We noted in our draft decision that we would update the forecast non-controllable operating expenditure for our final decision, and also adjust for the latest inflation and external bulk charges data.²⁹

For the environmental contribution, we have used the 2022-23 value provided by the Department of Energy, Environment and Climate Action and assumed that this will remain flat in nominal terms (decline in real terms) across the 2023–28 regulatory period.

We have assumed the licence fees for the Department of Health and the Environment Protection Authority Victoria remain flat in real terms across the period.³⁰

For our Essential Services Commission licence fee, we have taken our forecast fee estimate schedule, which is based on the expected work program across the 2023–28 regulatory period (which is in nominal dollars) and deflated it into 2022-23 dollars to express the fee in real terms.³¹

In May 2023, we advised Yarra Valley Water of our approved bulk water charges for Melbourne Water for 2023-24. In response, Yarra Valley Water updated its forecasts for bulk water charges.

We have reduced Yarra Valley Water's forecast non-controllable operating expenditure by \$5.44 million across the 2023–28 period, resulting from the following adjustments:

- \$0.79 million decrease for licence fees after considering the latest information received from the relevant regulatory authorities.

²⁹ Non-controllable costs are those that cannot be directly or indirectly influenced by a water business's decisions.

³⁰ For the Safe Drinking Water Administration levy, we have used the 2021-22 value provided by the Department of Health and indexed it by the annual rate for fees in 2022-23 (1.75 per cent), as set out by the Department of Treasury and Finance's cost recovery guidelines (<https://www.dtf.vic.gov.au/financial-management-government/indexation-fees-and-penalties>). We have applied the same approach to the 2021-22 licence fee provided by the Environment Protection Authority Victoria.

³¹ These fees are yet to be determined by the Minister for Water.

- \$3.07 million decrease for the environmental contribution to account for the latest data on inflation.
- \$1.58 million increase for external bulk water charges reflecting a slightly higher volume demand proposed by Yarra Valley Water to reflect the latest Victorian Government population and dwelling growth estimates; and to reflect the Melbourne Water Bulk Charges for 2023-24.

Accordingly, consistent with the reasoning in our guidance paper, our final decision is to adopt a revised non-controllable operating expenditure of \$2,674.22 million (Table 4.3) over the next regulatory period.

4.2 Capital expenditure

Our final decision is to adopt a forecast capital expenditure of \$1,962.0.

Capital expenditure is an input to estimating the regulatory asset base, which is an input to the revenue requirement. Our draft decision proposed to adopt a forecast capital expenditure of \$1,962.0 million for the 5-year period, as proposed by Yarra Valley Water.

The reasons for our draft decision were:

- Yarra Valley Water demonstrated it has adopted a reasonable approach to developing its capital program, and that its capital expenditure forecasts are prudent and efficient.
- We considered the planned capital expenditure program is achievable, given Yarra Valley Water's past track record delivering its capital expenditure program.
- Yarra Valley Water has an appropriate approach for managing expenditure associated with uncertain projects, excluding an estimated \$347.3 million of project costs from its price submission where there is uncertainty in timing, cost, scope and benefits of capital expenditure. We reiterate that Yarra Valley Water will need to demonstrate the prudence and efficiency of these costs if they are incurred during the 2023–28 regulatory period, if seeking to include them in the regulatory asset base for the 2028–33 price review.
- We considered Yarra Valley Water's approach to forecasting its capital expenditure was consistent with the requirements of our guidance.

We have considered all submissions in response to our draft decision. Our final decision is to adopt a forecast capital expenditure of \$1962.0 million for the 5-year period (Table 4.6), as proposed in our draft decision and for the same reasons proposed in our draft decision. We consider this benchmark is consistent with our guidance and the principles in the Water Industry Regulatory Order (2014). Our final decisions on Yarra Valley Water's forecast regulatory asset base (Table 4.6) and revenue requirement (Table 4.1) reflect this benchmark.

The benchmark that we propose to adopt for Yarra Valley Water does not represent the amount that Yarra Valley Water is required to spend or allocate to particular projects. Rather, it represents assumptions about the overall level of expenditure (to be recovered through prices) that we consider sufficient to operate the business and to maintain or improve services over the regulatory period. Where we have made an adjustment to exclude a project's capital expenditure from Yarra Valley Water's revenue requirement, we are not requiring the business to remove that project. Yarra Valley Water determines how to best manage the allocation of its revenue and priority of its expenditure within a regulatory period.

4.3 Regulatory asset base

A water business's regulatory asset base is the value of the business's assets for regulatory purposes.³² The regulatory asset base is used to estimate the return on assets (discussed in Section 4.4) and regulatory depreciation (discussed in Section 4.5). Both the return on assets and regulatory depreciation are components of the revenue requirement.

Our guidance required Yarra Valley Water to propose:

- the closing value of its regulatory asset base at 30 June 2022 (using actual data)
- the opening value of its regulatory asset base at 1 July 2023 (calculated according to the criteria outlined in the guidance)
- the forecast value of its regulatory asset base for each year of the regulatory period (2023-24 to 2027-28), in accordance with the prudence criteria outlined in the guidance.

4.3.1 Closing regulatory asset base

Our final decision is to approve a closing regulatory asset base at 30 June 2022 of \$5,266.0 million.

We update the regulatory asset base to reflect actual gross capital expenditure, less government and customer contributions, and asset disposals for the period from 2017-18 to 2021-22.³³ This helps to ensure prices reflect the actual net expenditure of a water business.³⁴

Our draft decision accepted Yarra Valley Water's closing regulatory asset base because it was calculated in accordance with the requirements of our guidance. After considering all submissions

³² These values were set initially for the water businesses by the Minister for Water and are adjusted on an ongoing basis to account for new investments, asset disposals, depreciation and inflation.

³³ See Section 4.2 for a discussion of Yarra Valley Water's capital expenditure.

³⁴ Net capital expenditure is calculated by deducting government and customer contributions from gross capital expenditure. Customer contributions reflect revenue earned from new connections made to the water business's water, sewerage or recycled water networks.

received in response to our draft decision, our final decision is the same as our draft decision. Therefore, our final decision is to approve a closing regulatory asset base at 30 June 2022 of \$5,266.0 million (Table 4.5).

Table 4.5 Final decision – closing regulatory asset base (RAB)
\$ million 2022-23

	2017-18	2018-19	2019-20	2020-21	2021-22
Opening RAB 1 July	4,416.0	4,583.7	4,766.5	4,946.5	5,132.4
Plus gross capital expenditure	315.3	343.8	348.5	348.0	290.9
Less government contributions	-	-	-	-	-
Less customer contributions	51.1	52.3	55.9	54.2	45.2
Less proceeds from disposals	1.2	1.1	0.9	0.5	3.4
Less regulatory depreciation	95.2	107.7	111.7	107.4	108.7
Closing RAB 30 June	4,583.7	4,766.5	4,946.5	5,132.4	5,266.0

Note: Numbers have been rounded.

4.3.2 Forecast regulatory asset base

Our final decision is to accept a forecast regulatory asset base as set out in Table 4.6.

The forecast regulatory asset base is calculated having regard to the closing regulatory asset base, and forecasts for capital expenditure, government and customer contributions, and asset disposals.

Our draft decision was to accept Yarra Valley Water's forecast regulatory asset base. In response to our draft decision, Yarra Valley Water updated its forecast regulatory asset base to reflect an update to its forecast revenue from customer contributions (see Section 4.3.2.1).

Table 4.5 sets out our final decision on Yarra Valley Water's forecast regulatory asset base from 1 July 2023.³⁵

³⁵ Our guidance required water businesses to provide an estimate of the components of their regulatory asset base for 2022-23. This was so we could assess the opening asset base for 1 July 2023. Our guidance noted that where the 2022-23 forecasts for net capital expenditure (gross capital expenditure less government and customer contributions) is lower than the forecast benchmark for that year in its 2018 price determination, the lower amount must be used.

Our final decision on Yarra Valley Water’s forecast regulatory asset base reflects our final decisions on its closing regulatory asset base and the components of the forecast regulatory asset base, which are outlined in the following sections of this final decision paper:

- Section 4.2 (capital expenditure)
- Section 4.3.2.1 (customer contributions)
- Section 4.5 (regulatory depreciation).

Table 4.6 Final decision – forecast regulatory asset base (RAB)

\$ million 2022-23

	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28
Opening RAB 1 July	5,266.0	5,281.6	5,182.3	5,401.9	5,682.3	5,920.4
Plus gross capital expenditure	217.9	329.9	394.5	458.2	428.4	351.0
Less government contributions	-	-	-	-	-	-
Less customer contributions	40.1	46.2	46.0	50.0	55.0	54.6
Less proceeds from disposals	50.9	247.3	1.6	1.5	2.0	1.1
Less regulatory depreciation	111.3	135.7	127.3	126.3	133.3	137.4
Closing RAB 30 June	5,281.6	5,182.3	5,401.9	5,682.3	5,920.4	6,078.4

Note: Numbers have been rounded.

4.3.2.1 Customer contributions

Our final decision adopts a forecast for new customer contributions as set out in Table 4.6.

Revenue from customer contributions is deducted from gross capital expenditure so it is not included in the regulatory asset base.³⁶

Our draft decision adopted Yarra Valley Water’s forecast revenue from customer contributions appeared reasonable, having regard to past trends and growth forecasts. On that basis, we

The estimates for 2022-23 will be confirmed at the price review following the 2023 water price review. Essential Services Commission, *2023 water price review: Guidance paper*, p. 38.

³⁶ Revenue from new customer contributions reflects revenue earned from new connections made to the water business’s water, sewerage or recycled water networks.

accepted Yarra Valley Water's forecast in our draft decision, subject to our further review of its proposed new customer contributions prior to our final decision.

In response to our draft decision, Yarra Valley Water outlined a revised approach to its new customer contributions and updated its forecasts for revenue from customer contributions. Yarra Valley Water has adjusted the forecast revenue from customer contributions accordingly.

We compared Yarra Valley Water's updated forecasts for customer contributions with past outcomes. We consider Yarra Valley Water's forecast contributions are reasonable, having regard to past trends and its growth forecasts.

After considering all submissions received in response to our draft decision, for the reasons set out above, our final decision is to accept the benchmark revenue from customer contributions set out in Table 4.6.

4.4 Rate of return

In establishing the return on assets component of Yarra Valley Water's revenue requirement, we have applied a rate of return to Yarra Valley Water's regulatory asset base. The rate of return is calculated using a benchmark cost of debt (discussed in Section 4.4.1) and a benchmark return on equity value (discussed in Section 4.4.2).

4.4.1 Cost of debt

Our final decision is to accept the updated cost of debt figures used by Yarra Valley Water to calculate its revenue requirement.

In our draft decision we proposed to approve the cost of debt proposed by Yarra Valley Water as it used the cost of debt values we specified in our guidance to calculate its revenue requirement. We also noted that our estimate of 3.75 per cent for the cost of debt in 2022-23 would be updated to reflect the latest available data.

In May 2023, we provided Yarra Valley Water with an updated cost of debt value from 3.75 per cent to 6.76 per cent for 2022-23.³⁷ This reflects the rise in borrowing costs over the past 12 months. Yarra Valley Water used this updated value to recalculate its revenue requirement.

For the above reasons, our final decision adopts the updated figures for the benchmark cost of debt as set out in Table 4.6.

³⁷ These updated figures were based on data from Treasury Corporation Victoria on the actual trailing average cost of debt for 2022-23.

Table 4.7 Final decision – 10-year cost of debt

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Cost of debt (nominal)	7.05%	5.36%	5.27%	4.91%	4.53%	4.61%	3.31%	3.05%	3.75%	6.76%

Note: Numbers have been rounded.

4.4.2 Return on equity

Our final decision is to adopt a return on equity of 4.5 per cent in real terms, which reflects Yarra Valley Water's PREMO rating.

Under our PREMO incentive mechanism, which we have applied since 2018, the return on equity we adopt to calculate the revenue requirement is linked to a business's PREMO rating. See Chapter 7 for an explanation of PREMO and our assessment of Yarra Valley Water's PREMO rating. As outlined in our guidance, the return on equity we adopt depends on a water business's self-rating and whether we accept that rating.

Our guidance included a matrix proposing the return on equity we would adopt, based on the combination of the business's self-rating and our rating.³⁸

Yarra Valley Water rated its price submission as 'Advanced'. Based on this PREMO self-rating, Yarra Valley Water proposed a real return on equity of 4.5 per cent per year. This reflects the maximum return rate allowed in our guidance for a price submission rated as 'Advanced'.³⁹

Our draft decision adopted Yarra Valley Water's proposed return on equity, which reflected our preliminary overall PREMO rating of its price submission.

After considering all submissions received in response to our draft decision, our final decision on Yarra Valley Water's overall PREMO rating remains the same as our draft decision. Therefore, our final decision is to adopt Yarra Valley Water's proposed return on equity of 4.5 per cent per year, reflecting our final decision on the overall PREMO rating of its price submission (see Chapter 7).

³⁸ Essential Services Commission, *2023 water price review: Guidance paper*, pp. 42-43.

³⁹ Essential Services Commission, *2023 water price review: Guidance paper*, p. 42.

4.4.3 Long-term inflation forecast

A long-term inflation forecast is needed to convert the nominal cost of debt (outlined in Section 4.4.2 above) to real terms. A higher rate of inflation means a lower cost of debt in real terms, which would flow through to a lower revenue requirement and lower prices, all other things being equal. Conversely, a lower long-term inflation rate will flow through to increased prices, all other things being equal.

In addition to updating our estimate for the cost of debt, in May 2023 we also updated businesses on our long-term inflation forecast. We advised businesses that the long-term inflation rate we calculated was 3.5 per cent.⁴⁰ All businesses adopted this amount to calculate prices in their responses to our draft decision. We checked this estimate again for our final decision, based on the method below.

While we have estimated inflation based on the outcome of the two methods specified in our guidance – the ‘RBA geometric mean’ and the ‘bond breakeven’ methods – we have varied our approach given the relatively high near-term inflation environment. While our guidance indicated that our calculation of long-term inflation would cover a 10-year forecast period, we consider in the current high inflation environment, that this would lead to outcomes that underestimate inflation in the 2023–28 regulatory period, which would not be in the interests of customers. Accordingly, we have adopted an averaging period of 5 years. This is consistent with the time period adopted by other economic regulators, including the Australian Energy Regulator.

Estimates we have adopted for each year of the 2023–28 regulatory period under the ‘RBA geometric mean’ approach are set out in Appendix E. Using the ‘RBA geometric mean’ approach we estimate an inflation rate of 3.8 per cent.

For the ‘bond breakeven’ approach, we estimate a 5-year average rate of 3.3 per cent, with the estimates adopted for each year of the 2023–28 regulatory period also set out in Appendix E.

The average outcome under the two approaches is 3.5 per cent, which we have adopted for our final decision.

However, to manage the risk that inflation falls well below our forecast, our price determinations include a provision that allows for a reconsideration of the inflation forecast adopted, if inflation falls below 2.5 per cent by 2026-27. The updated inflation estimate, if needed, would be based on a 5-year averaging period.

⁴⁰ The inflation rate adopted in our draft decision was 3 per cent.

4.5 Regulatory depreciation

Our final decision is to adopt the benchmarks for regulatory depreciation as set out in Table 4.6.

Regulatory depreciation is a component of Yarra Valley Water's revenue requirement and is also an input to calculating the regulatory asset base.

As indicated in our draft decision, Yarra Valley Water's forecast regulatory depreciation was calculated using a straight-line depreciation profile, which is our preferred approach.⁴¹

In response to our draft decision, Yarra Valley Water provided updated forecasts for regulatory depreciation that reflected changes it made to its new customer contributions and revenue from customer contributions.⁴²

We received no submissions from other stakeholders on this issue.

On that basis, our final decision is to accept Yarra Valley Water's updated forecast regulatory depreciation, as set out in Table 4.6 in Section 4.3.2.

4.6 Tax allowance

Our final decision is to adopt Yarra Valley Water's forecast tax allowance of \$51.7 million for the 2023–28 regulatory period.

The tax allowance is a component of the revenue requirement. Yarra Valley Water has proposed a tax allowance of \$65.2 million in its revenue requirement for the 2023–28 regulatory period. Our draft decision was to accept a lower tax allowance of \$64.6 million reflecting the impact of changes to the revenue requirement and its treatment of rebate amounts for 2023-24.⁴³

In its response to our draft decision, Yarra Valley Water updated its estimates of forecast tax to \$51.7 million, mostly resulting from changes to its proposed new customer contributions. We consider Yarra Valley Water's updated estimates were calculated in a manner consistent with our guidance. The revisions lower the forecasts for tax payments by Yarra Valley Water by around \$12.8 million over the 5-year regulatory period from 1 July 2023, compared to our draft decision (Table 4.2).

⁴¹ Essential Services Commission, *2023 water price review: Guidance paper*, p. 39.

⁴² These adjustments were small and do not show as an adjustment in Table 4.2 due to rounding.

⁴³ Essential Services Commission, *2023 water price review: Guidance paper*, pp. 47–48.

No other new considerations were presented in submissions received following our draft decision which caused us to change our views on the tax allowance.

After considering all submissions received in response to our draft decision, for the reasons set out above, our final decision adopts a forecast tax allowance of \$51.7 million for the 5-year regulatory period, as set out in Table 4.1.

5. Demand, tariffs and prices

Once Yarra Valley Water's revenue requirement is established, demand forecasts and the form of price control are used to translate the revenue requirement into tariffs and prices.

5.1 Demand

Our final decision is to accept Yarra Valley Water's updated demand forecasts.

Along with the revenue requirement, demand forecasts are an input to calculating prices.

In our draft decision, we accepted Yarra Valley Water's proposed demand forecasts but required Yarra Valley Water in its response to our draft decision to demonstrate how it has considered the updated Victorian Government population and dwelling growth estimates that had been made available to water businesses.

In response to our draft decision, Yarra Valley Water adjusted its demand forecasts to reflect the updated higher Victorian Government growth estimates for its service area. This has resulted in a decrease in Yarra Valley Water's proposed prices. On the basis that Yarra Valley Water's update to its demand forecasts means that customers benefit from lower prices, and because it was estimated consistently with the requirements of our guidance, our final decision accepts Yarra Valley Water's updated demand forecasts.

5.2 Form of price control

Our final decision is to accept Yarra Valley Water's proposed revenue cap form of price control.

Yarra Valley Water proposed to retain a revenue cap form of price control. Under a revenue cap, annual revenue is capped subject to annual updates for demand, the cost of debt, changes in bulk charges, and any other price adjustments we approve in our price determination (Section 5.5).

Yarra Valley Water's proposal included a nominal cap on changes in water and sewerage prices for 2023-24 and 2024-25 of 5 per cent, noting the cap was not breached in 2023-24 (our final decision approves increases below the five per cent cap in nominal terms).

Our draft decision accepted Yarra Valley Water's proposal because it largely reflected a continuation of its current approach, would provide sufficient revenue to recover the efficient costs of providing services, and was consistent with the requirements of our guidance.

No new considerations were raised in response to our draft decision that caused us to change our views on the form of price control.

For the above reasons, our final decision confirms our draft decision and approves Yarra Valley Water's proposed revenue cap form of price control.

5.3 Tariff structures and prices

Our draft decision accepted Yarra Valley Water's proposed tariff structures but, like all our draft decisions in this review, did not approve prices for each tariff, because Yarra Valley Water needed to update its proposed prices to reflect our updates to inflation and cost of debt estimates.

Our final decision on tariff structures and prices is set out below.

5.3.1 Tariff structures

Our final decision is to approve Yarra Valley Water's proposed tariff structures.

As outlined in our guidance, we have provided the water businesses with a large degree of discretion to decide on individual tariff structures.⁴⁴ This recognises water businesses are often best placed to consider the interests of customers in designing tariffs, and that existing tariff structures have been developed over time to deal with a variety of local circumstances.

Yarra Valley Water proposed to retain its existing tariff structures, including:

- maintaining two-part tariffs for residential and non-residential water services
- removing the sewerage disposal charge and combining it with a water usage charge for residential customers

Our draft decision was to accept Yarra Valley Water's proposal because it is a continuation of its existing approach and because the tariff structures were generally supported by its customers. In our draft decision, we considered the two-part structure for water services will promote the efficient use of services. It also sends customers a signal about the costs of their water use and is an approach that is commonly applied in other states and territories.⁴⁵ We also considered two-part tariff structures were easy to understand. We also accepted Yarra Valley Water's proposal to continue its three-tier inclining block tariff for residential water use.

⁴⁴ Essential Services Commission, *2023 water price review: Guidance paper*, p. 51.

⁴⁵ Includes the tariffs of Icon Water, Sydney Water, Hunter Water, Central Coast Council, Power and Water Corp, Urban Utilities, Unity Water, SA Water and TasWater.

In our draft decision, in relation to sewerage services, we considered the proposed fixed charge for residential customers was easy to understand and that the two-part tariff for non-residential customers sent these customers signals about efficient costs.

Following our draft decision, we received one submission from a stakeholder supporting Yarra Valley Water's proposal to combine its residential sewage disposal charge and residential variable water usage tariff.⁴⁶

Another submission by the Consumer Action Law Centre noted water businesses' tariffs remained unchanged particularly the balance between fixed and variable charges and supported this outcome given the impact on tenants when more weight is assigned to variable charges.⁴⁷

A submission from the Registered Accommodation Association of Victoria asked us to consider multiple room rooming houses being charged based on the number of rooms.⁴⁸ This reflects the current inclining block pricing structure whereby a typical rooming house would generally always be paying at a higher inclining block rate, with little ability to respond to pricing signals. As noted above, businesses are often best placed to consider the interests of their customers in designing tariffs and that existing tariff structures have been developed over time to deal with a variety of local circumstances. We consider a different approach to charging rooming houses might be considered by the business in future periods. However, we note that any such approach may be administratively complex, given the variation in the number of rooms in rooming houses.

On the basis of the above, our final decision is to approve Yarra Valley Water's proposed tariff structures.

5.3.2 Prices

Our final decision is to accept the revised prices proposed by Yarra Valley Water.

In our draft decision, we noted that Yarra Valley Water would need to propose updated prices to reflect our updates to inflation and cost of debt estimates and may also need to update prices depending on our further review of its new customer contributions and revenue from customer contributions.

Following our draft decision, Yarra Valley Water proposed revised prices that reflect the updates to our inflation and cost of debt of debt estimates, and to bulk water charges (see Section 4.1). Yarra

⁴⁶ Anonymous, *submission to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 14 February 2023.

⁴⁷ Consumer Action Law Centre, *Feedback on standard draft decisions: 2023 water price review*, 5 May 2013, p.2.

⁴⁸ Registered Accommodation Association of Victoria submission on water pricing for rooming houses in Victoria, 25 May 2023.

Valley Water's revised prices also reflect changes to its revenue requirement, including from changes to forecast operating expenditure reflecting revised energy costs and changes announced in the Victorian State Budget (See Section 4.1).

In response to our draft decision, we received a submission from a stakeholder supporting Yarra Valley Water's proposed reduction (before inflation) in sewerage service charges. However, they observed that high inflation may mean there is no real decrease in customer bills.⁴⁹ We confirm that in nominal terms, prices will generally increase for Yarra Valley Water customers in 2023-24. We consider its prices however, reflect forecast efficient costs and as discussed below, Yarra Valley Water has also considered the impacts on low income and vulnerable customers.

Our final decision is to approve the revised prices proposed by Yarra Valley Water because they have been calculated in a manner consistent with our guidance including that they reflect forecasts for prudent and efficient expenditure.

Our price determination for Yarra Valley Water sets out the maximum prices it may charge for the 5-year period from 1 July 2023 (or the manner in which its prices are to be calculated, determined, or otherwise regulated).

Approved maximum prices for water and sewerage services in 2023-24 applying to most residential and non-residential customers are set out in Tables 5.1 and 5.2. Note however, that prices after 2023-24 will move in accordance with Yarra Valley Water's revenue cap (Section 5.2). Subject to its revenue cap, water and sewerage prices for residential and non-residential customers will generally fall by around 1.6 per cent in 2024-25, excluding inflation, before moving in line with inflation in the following 3 years.

⁴⁹ Anonymous, *submission to the Essential Services Commission 'Yarra Valley Water draft decision: 2023 water price review'*, 14 February 2023.

Table 5.1 Final decision – water prices 2023-24
\$ 2023-24

	2023-24
Residential	
Variable (\$/kL) for water and sewerage customers	
Step one	3.3438
Step two	4.3873
Step three	5.0973
Fixed (\$/year)	80.59
Non-residential	
Variable (\$/kL)	2.9675
Fixed (\$/year)	299.02

Notes: These prices have been expressed in \$2023-24 terms, which means 7 per cent inflation has been factored into the prices for 2023-24. The figures in other tables of this report are expressed in \$2022-23, which means inflation has not been accounted for in 2023-24 or the remaining years of the 2023–28 regulatory period.

Table 5.2 Final decision – sewerage prices 2023-24
\$ 2023-24

	2023-24
Residential	
Fixed (\$/year)	460.37
Non-residential	
Variable (\$/kL)	2.0868
Fixed (\$/year)	575.12

Notes: These prices have been expressed in \$2023-24 terms, which means 7 per cent inflation has been factored into the prices for 2023-24. The figures in other tables of this report are expressed in \$2022-23, which means inflation has not been accounted for in 2023-24 or the remaining years of the 2023–28 regulatory period.

5.3.3 Addressing the interests of low income and vulnerable customers

In making our price determination, we must have regard to whether Yarra Valley Water’s prices take into account the interests of customers, including low income and vulnerable customers.⁵⁰

As outlined in our draft decision, we consider that Yarra Valley Water has done so in the following ways:

⁵⁰ Water Industry Regulatory Order 2014 clause 11(d)(iii).

- maintaining an efficiency improvement rate greater than the industry average, helping to minimise prices and bills
- a price path that focused price reductions in the first 2 years of the regulatory period in consideration of the near-term inflation outlook and cost of living pressures
- new expenditure items only where there was support among self-identified vulnerable customers
- piloting a combined water audit and showerhead replacement program with a particular focus on vulnerable and higher water use customers.

No new considerations were presented by Yarra Valley Water or in our consultation following our draft decision that caused us to change our views on how Yarra Valley Water has addressed the interests of low income and vulnerable customers.

5.3.4 Other services

As indicated in our draft decision, Yarra Valley Water has confirmed that its proposed tariffs for trade waste and miscellaneous services are calculated in accordance with the pricing principles referenced in our guidance.

After considering all submissions received in response to our draft decision, our final decision approves Yarra Valley Water's proposed prices for other services including trade waste and miscellaneous services because we consider that they are cost reflective and are calculated in accordance with the pricing principles in our guidance.

5.4 New customer contributions

Our final decision is to accept Yarra Valley Water's proposed new customer contributions.

Our final decision is to accept Yarra Valley Water's proposed negotiating framework for negotiated new customer contributions.

New customer contributions (or developer charges) are levied by water businesses when a new connection is made to its water, sewerage or recycled water networks in a given part of its service area. New customer contributions can be either standard or negotiated. Standard charges apply to new connections in areas where infrastructure requirements and growth rates are relatively well known and designated by the water business. The purpose of standard new customer contributions is to reduce the administrative burden as well as improve the timeliness and predictability of costs faced by developers.⁵¹ Negotiated charges allow water businesses and

⁵¹ Essential Services Commission, *New customer contributions: explanatory note*, December 2013, p. 3.

developers to negotiate a site-specific arrangement where standard charges are not fair and reasonable or where a new connection is outside the areas eligible for standard charges.⁵²

As outlined in our draft decision Yarra Valley Water proposed to:

- increase new customer contributions in the standard and special new urban growth boundary areas in real terms by 5 per cent per year (capped at 10 per cent per year in nominal terms by charging below the maximum price if inflation is higher than 5 per cent in any given year)
- integrate the Epping special charging area into its standard new customer contribution charge
- hold the Greenvale special charging area (negotiated) new customer contribution charge flat in nominal terms to allow its integration into the standard new customer contribution charge in a later regulatory period.

Our draft decision did not approve Yarra Valley Water's proposed new customer contributions because we did not consider Yarra Valley Water's proposal to be cost reflective as it was not based on its calculated new customer contributions, most of which were materially higher than what Yarra Valley Water proposed. We indicated in our draft decision that we needed to continue our review of the reasonableness of Yarra Valley Water's proposed inclusion of sunk costs, including for renewals, in its proposed new customer contributions and the length of its transition to cost reflective contributions. We also indicated that we would seek further information from Yarra Valley Water prior to our final decision and invited stakeholders to comment on its approach to transitioning to cost reflective charges.

In response to our draft decision and subsequent information requests, Yarra Valley Water provided a revised proposal to:

- increase new customer contributions in the special new urban growth boundary areas in nominal terms by 10 per cent for the first 2 years of the 2023–28 regulatory period and by 10 per cent in real terms for final 3 years of the 2023–28 regulatory period
- increase new customer contributions in the standard infill areas annually by 5 per cent in real terms
- maintain its separate Epping and Greenvale special charging areas until these reach parity with the standard infill contributions, which will occur in 2027-28 for Epping but will not align for Greenvale until 2045-46 assuming the 5 per cent real annual increase in standard new customer contributions is retained.

⁵² Essential Services Commission, *New customer contributions: explanatory note*, December 2013, p. 3.

Yarra Valley Water also provided:

- justification for including sunk costs in its new customer contributions based on its interpretation of section 268(1) of the *Water Act 1989* and its approaches outlined in its 2013 and 2018 price submissions
- explanation of the significant growth capital expenditure in the urban growth boundary in both the 2018 and 2023 pricing periods
- scenario analysis with and without the inclusion of sunk costs, showing that the calculated contributions remain well above those proposed by Yarra Valley Water
- updated forecasts to reflect updated Victorian Government population and dwelling growth estimates
- a letter from the Urban Development Institute of Australia calling for a 10 per cent nominal cap on annual new customer contribution increases for 24 months.

We have reviewed Yarra Valley Water's revised new customer contribution proposal against our guidance paper requirements.

In coming to our final decision, we have had regard to if and how Yarra Valley Water's proposal is consistent with the aims of the new customer contribution framework, which are to:

- send signals to developers about the costs of developing in different locations
- share the costs and benefits of growth between new and existing customers
- administer new customer contributions in a transparent way.⁵³

We have carefully considered the impact of the issues relating to cost reflectivity, avoidable cost and attribution of capital expenditure⁵⁴, the reasonableness and transparency⁵⁴ of the proposal and whether it is supported by customers and whether the proposal as a whole advances the aims of our new customer contributions framework.

The Consumer Action Law Centre made a submission on our draft decisions which reiterated its support for water businesses moving to higher more cost reflective new customer contributions. The Consumer Action Law Centre also supported our draft decision's call for clarity on the full proposed terms for transitioning to cost reflectivity.⁵⁵

⁵³ Essential Services Commission, *New Customer Contributions Explanatory Note Final*, December 2013, p.2.

⁵⁴ Informed by FTI Consulting, *Review of new customer contribution-related capital expenditure for Yarra Valley Water*, May 2023.

⁵⁵ Consumer Action Law Centre, *Feedback on standard draft decisions: 2023 Water Price Review*, 5 May 2023, p. 3.

We consider that Yarra Valley Water has had regard to a fair and reasonable allocation of incremental infrastructure and associated costs when determining its proposed new customer contributions.

Moreover, Yarra Valley Water's revised proposal (received after our draft decision) improves the pace at which cost reflectively will be achieved for the special new urban growth boundary areas, in comparison to the proposal set out in its price submission. Yarra Valley Water plans to transition to fully cost reflective new customer contributions for the special new urban growth boundary areas after three regulatory periods. Each pricing period Yarra Valley Water plans to continue to assess its new customer contributions prices to balance developer and new customer impacts with the transition to cost reflective prices.

We wish to highlight that, to the extent necessary, the new customer contribution framework allows water businesses and developers to negotiate new customer contribution in lieu of using the standard new customer contributions. This provides for flexibility where standard new customer contributions may not be appropriate.

Regarding Yarra Valley Water's proposed negotiated new customer contribution framework, our draft decision proposed to accept the framework because it complied with the requirements of our new customer contribution pricing principles. No new considerations were presented by Yarra Valley Water or in submissions received following the draft decision which caused us to change our views on Yarra Valley Water's negotiated new customer contributions framework.

If there is a dispute between a developer and a water business (whether in relation to a standard or negotiated new customer contributions), developers may use the dispute resolution offered by a water business as part of its new customer contribution negotiating framework. In addition, developers may follow the *Water Act 1989* process to object and seek internal review by the water business, and to pursue unresolved matters through the Victorian Civil and Administrative Tribunal.⁵⁶

⁵⁶ *Water Act 1989*, section 271.

5.4.1 Review of the framework for new customer contributions

Our guideline for new customer contributions establishes our expectations for standard new customer contributions and bespoke negotiated new customer contributions. However, in light of issues we identified during our 2023 water price review, we believe that a review of the regulatory framework for new customer contributions is necessary. Our review will aim to identify and address key implementation issues for water businesses, establish consistency in setting new customer contributions across the sector, and define the purpose and content of the negotiating framework.

5.4.1.1 Current issues

Our experience reviewing the new customer contributions proposals of water businesses in the current price review has identified varied practices across businesses in terms of their approach and substantiation of proposed charges to meet our guidance and the objectives of the framework. This includes varied approaches to the inclusion of costs in new customer contributions, differentiated pricing, and use of negotiated new customer contributions.

A number of businesses in the current price review also based their new customer contributions on an average incremental cost methodology, rather than the net incremental cost approach adopted in the past. We want to explore the issues associated with having different underlying approaches and how this affects confidence and transparency in the way new customer contributions are arrived at.

Other issues we have identified in the current review – such as varied approaches to locational and incremental cost reflectivity – and the transparency of new customer contributions and the nature of engagement, may also be covered in the review.

5.4.1.2 Next steps

In 2023-24, we intend to initiate a review of the framework for new customer contributions by issuing a consultation paper. This paper will outline the proposed scope of the review and seek feedback from stakeholders. We encourage stakeholders to suggest any other important matters that they believe should be included in the review.

Throughout the review process, we will actively engage with industry and stakeholders to gather their input.

5.5 Adjusting prices

Our final decision is to accept Yarra Valley Water's proposed price adjustment mechanisms.

Yarra Valley Water's proposed price adjustment mechanism is similar to its existing mechanisms, including:

- A continuation of its existing uncertain and unforeseen events mechanism.
- Pass-through of several specific costs including:
 - sales and purchases of water allocations and bulk service charges, to account for differences between forecast and actual expenditure
 - annual cost of debt adjustment to reflect benchmark efficient cost of debt under a 10-year trailing average approach.
- Non-achievement of service outcomes
- Savings in financing costs arising from a deferral of top 10 projects
- Any unit rate efficiencies together with the financing costs to customers if the market reveals a reduction in the cost of the water reliability – reticulation main renewals program
- Savings due to any change in taxation status of either new customer contributions or developer gifted assets.

This proposal enables Yarra Valley Water to smooth nominal prices, by capping price increases in nominal terms to 5 per cent in 2024-25, to avoid price shocks and manage bill impacts that may arise from high inflation. Adjustment mechanisms to take into account shortfalls in performance relative to targets, and cost savings (relative to benchmarks) also demonstrate a commitment to ensuring customer prices are not higher than they need to be.

Our draft decision approved the proposed price adjustment mechanism because we considered that it satisfied the requirements of our guidance and the Water Industry Regulatory Order (2014).

After considering all submissions received following our draft decision, and for the above reasons, our final decision is to accept Yarra Valley Water's proposed price adjustment mechanisms.

6. Financial position

We have reviewed key indicators of Yarra Valley Water's financial performance and consider that Yarra Valley Water will generate sufficient cash flow to deliver on its service commitments.

In approving prices, we must have regard to the financial viability of the water industry.⁵⁷ We interpret the financial viability requirements under the *Essential Services Commission Act 2001* and the Water Industry Regulatory Order (2014) to mean that the prices we approve should provide a high level of certainty that each water business can generate sufficient cash flow to deliver on its service commitments, including financing costs arising from investments to meet service expectations.

Our guidance set out key indicators of forecast financial performance. We have reviewed forecasts for these key indicators based on our final decision on Yarra Valley Water's prices. We have assessed that under our final decision, Yarra Valley Water will generate sufficient cash flow to deliver on its service commitments, including financing costs arising from investments to meet service expectations.

⁵⁷ WIRO clause 8(b)(ii) and ESC Act s.8A(1)(b).

7. PREMO rating

PREMO is an incentive mechanism that links the return on equity used to calculate a water business's revenue requirement to that business's level of ambition expressed in its price submission. Our guidance required Yarra Valley Water to self-assess the level of ambition of its price submission for each element of the PREMO mechanism and arrive at an overall self-rating.⁵⁸ We required Yarra Valley Water to self-rate its price submission as either 'Leading', 'Advanced', 'Standard' or 'Basic', with 'Leading' being the most ambitious and 'Basic' the least.

The assessment tool included in our guidance directed Yarra Valley Water to consider its level of ambition in relation to matters covered in its price submission, such as proposals related to operating and capital expenditure, the form of price control, and tariffs.

We assessed and rated Yarra Valley Water's price submission. As outlined in our guidance, the combination of Yarra Valley Water's self-rating and our rating has determined the return on equity we have adopted to calculate Yarra Valley Water's revenue requirement in our final decision.

7.1 Our PREMO assessment of Yarra Valley Water's price submission

Our final decision is to rate Yarra Valley Water's price submission as 'Advanced' under PREMO, which is the same as Yarra Valley Water's self-rating.

Yarra Valley Water's self-rating for each of the PREMO elements and its overall self-rating are shown in Table 7.1. This table also includes our draft and final ratings of Yarra Valley Water's price submission. This rating is reflected in the return on equity we have approved for Yarra Valley Water (see Section 4.4.2).

Our PREMO assessment is set out in our draft decision.

No new considerations were presented by Yarra Valley Water or in submissions received following our draft decision, which caused us to change our assessment.

For that reason and for the reasons set out in our draft decision, our final decision is to agree with Yarra Valley Water's proposed overall PREMO self-rating of 'Advanced'.

⁵⁸ This is the first price review we have done where the rating has been based on all five elements of PREMO. In our 2018 price review, our PREMO assessment was against only four of the elements — Risk, Engagement, Management and Outcomes.

Table 7.1 **PREMO rating**

	Overall PREMO rating	Performance	Risk	Engagement	Management	Outcomes
Yarra Valley Water's self-rating	Advanced	Advanced	Advanced	Leading	Advanced	Advanced
Commission's draft decision rating	Advanced	Advanced	Advanced	Leading	Advanced	Advanced
Commission's final decision rating	Advanced	Advanced	Advanced	Leading	Advanced	Advanced

Our PREMO assessment is provided in our draft decision. In summary, the following matters support Yarra Valley Water's self-rating of its price submission as 'Advanced':

- sound performance against its outcome commitments in the current regulatory period, and a major project delivery record that compares favourably to other water businesses
- a strong engagement program which gives confidence that its proposals are informed by deep insights into customer priorities and concerns
- it demonstrated the ability for customers to influence its proposals, by clearly linking key proposals and initiatives such as Caring for Country, to recommendations of its Citizens' Juries
- its proposed expenditure aligned with its proposed key outcomes
- a relatively high operating cost efficiency target and commitment to absorbing future cost increases should they arise, such as above-inflation labour cost growth
- recognising the possible impacts of a high inflation outlook on prices in the near term, and proposing a price path (including limits on nominal price increases) that help to manage these impacts for its customers
- relatively strong outcomes on the commission's customer perception survey
- its commitment to return funds to customers or the community where service targets are not met, demonstrating a level of accountability for underperformance that stands out compared to the other water businesses
- it identified \$347 million of uncertain capital expenditure it had excluded from its prices – these project costs will be carried by the business and included at the end of the regulatory period if they are incurred
- the overall strength of the justification for the prudence and efficiency of its forecast expenditure.

Yarra Valley Water also provided a price submission and supporting model that were of a high quality.

Appendix A – Submissions received on draft decision

Name or organisation	Date received
Anonymous submission	14 February 2023
Yarra Valley Water	10 March 2023
Consumer Action Law Centre	5 May 2023
Yarra Valley Water	10 May 2023
Registered Accommodation Association of Victoria	26 May 2023

Appendix B – Commission’s consideration of legal requirements

Clause 11 of the Water Industry Regulatory Order 2014 (WIRO) specifies the mandatory factors we must have regard to when making a price determination. The WIRO covers matters that are included in the *Water Industry Act 1994* (WI Act) and the *Essential Services Commission Act 2001* (ESC Act).

Below, we describe how we apply the mandatory factors and where we have done so in our final decision for Yarra Valley Water.

The WIRO requires the Commission to place particular emphasis on the promotion of efficient use of prescribed services by customers, the promotion of efficiency in water businesses as well as efficiency in, and the financial viability of, the regulated water industry and the provision to regulated entities of incentives to pursue efficiency improvements.

In addition to the mandatory factors set out below, clause 11 of the WIRO requires the commission to have regard to the matters specified in the commission’s guidance.⁵⁹ Our draft and final decisions provide further information on where we have considered our guidance, and Yarra Valley Water’s compliance with our guidance, in making our price determination.⁶⁰

Note: all chapter and section numbers referenced below refer to our final decision for Yarra Valley Water.

Economic efficiency and viability matters

WIRO clause 8(b)(i) requires us to have regard to the ‘promotion of efficient use of prescribed services by customers’.

We consider that the efficient use of prescribed services by customers is promoted when a tariff is applied to customers benefiting from the service covered by the tariff, and tariffs send appropriate signals about efficient costs.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our assessment of the revenue requirement (Chapter 4).

⁵⁹ Essential Services Commission, *2023 water price review: Guidance paper*, 26 October 2021.

⁶⁰ Essential Services Commission, *Yarra Valley Water draft decision: 2023 water price review*, 20 December 2023; Essential Services Commission, *Yarra Valley Water Determination: 1 July 2023 – 30 June 2028*, 23 June 2023.

- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

WIRO clause 8(b)(ii) requires us to have regard to the ‘promotion of efficiency in regulated entities as well as efficiency in, and financial viability of, the regulated water industry’.

We consider that the delivery of outcomes which reflect customer service priorities at an efficient cost promotes efficiency in regulated entities and the water industry. Our final decision has therefore had regard to the extent that Yarra Valley Water has demonstrated its proposed outcomes reflect customer service priorities, and whether its tariffs and forecast costs reflect efficient levels of expenditure.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).
- Our assessment of financial viability (Chapter 6).

WIRO clause 8(b)(iii) requires us to have regard to the ‘provision to regulated entities of incentives to pursue efficiency improvements’.

We consider that the delivery of outcomes which reflect customer service priorities at an efficient cost provides regulated entities incentives to pursue efficiency improvements. The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

Additionally, our pricing approach allows a water business to retain the benefits of any cost efficiencies it generates until the end of its regulatory period. In other words, a water business has an incentive to outperform the operating and capital expenditure benchmarks we accept for the purpose of estimating its revenue requirement and prices. This is consistent with providing incentives for water businesses to pursue efficiency improvements.

ESC Act section 8A(1)(a) requires us to have regard to ‘efficiency in the industry and incentives for long term investment’.

We consider that adopting forecasts of efficient expenditure that reflect the service priorities of the customers of each water business promotes efficiency in the water industry.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

We have had regard to incentives for long term investment by adopting:

- A 10-year trailing average approach to estimating the benchmark cost of debt (see Section 4.4.1).
- A regulatory rate of return that we consider will enable Yarra Valley Water to recover borrowing costs associated with its investment in services, and generate a return on assets.⁶¹

ESC Act section 8A(1)(b) requires us to have regard to the ‘financial viability of the industry’.

We consider that the financial viability of the industry is secured by approving prices that provide a high degree of certainty that each water business can maintain an investment grade credit rating. Further, prices should enable each business to generate cash flow to service financing costs arising from investments to meet service expectations.

We have had regard to this matter in Chapter 6.

ESC Act section 33(3)(b) requires us to have regard to the ‘efficient costs of producing or supplying regulated goods or services and of complying with relevant legislation and relevant health, safety, environmental and social legislation applying to the regulated industry’.

In preparing our final decision, we have had regard to the extent Yarra Valley Water has demonstrated its forecasts reflect efficient costs to deliver services valued by customers, and to deliver on relevant legislation and relevant health, safety, environmental and social obligations.

⁶¹ The regulatory rate of return is comprised of the cost of debt and the return on equity.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

Industry specific matters

ESC Act section 33(3)(a) requires us to have regard to the ‘particular circumstances of the regulated industry and the prescribed goods and services for which the determination is being made’.

Our pricing approach allows each water business to propose outcomes, tariff structures and expenditure that reflect its particular circumstances. We consider that taking into account the particular circumstances of each water business is consistent with taking into account the particular circumstances of the water industry.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

We have had regard to the prescribed services listed in the WIRO in making our final decision. This includes adopting operating and capital expenditure benchmarks that we consider will allow Yarra Valley Water to deliver services that are covered by the prescribed services listed in the WIRO.

ESC Act section 33(3)(c) requires us to have regard to the ‘return on assets in the regulated industry’.

Our final decision provides for Yarra Valley Water to generate a return on assets through:

- Our consideration of the regulatory asset base (Section 4.3).
- Our consideration of the cost of debt (Section 4.4.1).
- Our consideration of the return on equity (Section 4.4.2).

ESC Act Section 33(3)(d) requires us to have regard to ‘any relevant interstate and international benchmarks for prices, costs and return on assets in comparable industries’.

In assessing costs, prices and return on assets we have had regard to relevant interstate benchmarks:

- indicative bills paid by customers in other jurisdictions in Australia⁶²
- operating and capital expenditure costs per connection throughout Australia⁶³
- tariff structures applied by water businesses throughout Australia⁶⁴
- the regulatory rate of return set by other regulators.⁶⁵

We are not aware of any international benchmarks that are relevant to our final decision.

WI Act section 4C(b) requires us to ‘ensure that regulatory decision making and regulatory processes have regard to any differences between the operating environments of regulated entities’.

Our pricing approach allows each water business to propose outcomes, a revenue requirement, expenditure and tariffs that reflect its particular circumstances and operating environment.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

Our price review also considers the views of stakeholders affected by Yarra Valley Water’s proposals, including through submissions and public meetings.

⁶² Bureau of Meteorology, *National performance report 2020-21; urban water utilities, part A*, February 2022.

⁶³ Bureau of Meteorology, *National performance report 2020-21; urban water utilities, part A*.

⁶⁴ Includes Icon Water, Sydney Water, Hunter Water, Central Coast Council, Power and Water Corp, Urban Utilities, Unity Water, SA Water and TasWater.

⁶⁵ Independent Pricing and Regulatory Tribunal NSW, *Final Report - Review of WaterNSW's rural bulk water prices*, 9 September 2021; Independent Pricing and Regulatory Tribunal NSW, *Final Report - Review of prices for Sydney Water*, June 2020; Essential Services Commission of South Australia, *SA Water's water and sewerage retail services: 1 July 2020 - 30 June 2024*, Price Determination, 1 July 2020; Queensland Competition Authority, *Final report - Seqwater bulk water price review 2022–26*, March 2022; Queensland Competition Authority (QCA), *Final report - Rural irrigation price review 2020–24, Part A: Overview*, January 2020; Office of the Tasmanian Economic Regulator, *Final report - Investigation into TasWater's prices and services for the period 1 July 2022 to 30 June 2026*, May 2022.

Customer matters

ESC Act section 8(1) requires us to have regard to the fact that the ‘objective of the Commission is to promote the long-term interests of Victorian consumers’.

We consider that promoting efficiency in delivering outcomes that align to service priorities of customers is consistent with promoting the long-term interests of Victorian consumers.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).
- Our assessment of financial viability (Chapter 6).

ESC Act Section 8(2) requires us to ‘have regard to the price, quality and reliability of essential services’ in seeking to achieve the objective in section 8(1) of the ESC Act.

We consider that promoting efficiency in delivering outcomes that align to service priorities of customers, and allowing businesses to meet regulatory and policy obligations is consistent with this objective.

In terms of prices, the following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our consideration of demand (Section 5.1).
- Our consideration of tariffs (Section 5.3).

In terms of the quality and reliability of services, the following sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our consideration of outcomes (Section 3.2).

WIRO Clause 11(d)(i) requires us to have regard to whether Yarra Valley Water’s prices ‘enable customers or potential customers of the regulated entity to easily understand prices charged by the regulated entity for prescribed services or the manner in which such prices are calculated, determined or otherwise regulated’.

We consider that the following matters are relevant when considering whether Yarra Valley Water’s prices enable customers or potential customers to easily understand prices, or the manner in which prices are calculated, determined or otherwise regulated:

- feedback from customers during a water business’s engagement
- the structure of individual tariffs
- the proposed form of price control
- any changes to tariffs and how water businesses explain them to customers.

The following sections of our final decision involved consideration of this factor:

- Our consideration of tariffs and the form of price control (Section 5.2 and Section 5.3).

WIRO Clause 11(d)(ii) requires us to have regard to whether Yarra Valley Water’s prices ‘provide signals about the efficient costs of providing prescribed services to customers while avoiding price shocks where possible’.

We consider prices can provide signals about efficient costs when a tariff is applied to customers benefiting from the service covered by the tariff, and tariffs send appropriate signals about efficient costs.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1).
- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

WIRO Clause 11(d)(iii) requires us to have regard to whether Yarra Valley Water’s prices ‘take into account the interests of customers of the regulated entity, including low income and vulnerable customers’.

We consider that customer value established through prices and customer outcomes, as well as tariff structures, and assistance available to customers having difficulty paying bills is relevant to this objective.

The following chapters and sections of our final decision involved consideration of this factor:

- Our consideration of customer engagement (Section 3.1)
- Our consideration of outcomes (Section 3.2)

Appendix B – Commission’s consideration of legal requirements

- Our consideration of guaranteed service levels (Section 3.4)
- Our consideration of tariff structures and prices (Chapter 5)

Health, safety, environmental and social obligations

ESC Act Section 8A(1)(d) requires us to have regard to ‘the relevant health, safety, environmental and social legislation applying to the industry’.

Our final decision proposes to approve a revenue requirement that will enable Yarra Valley Water to deliver the outcomes valued by customers, and on its legal and regulatory obligations.

The following chapters and sections of our final decision involved consideration of this factor:

- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of the form of price control (Section 5.2).

WI Act section 4C(c) requires us to ‘ensure that regulatory decision making has regard to the health, safety, environmental sustainability (including water conservation) and social obligations of regulated entities’.

Our final decision proposes to approve a revenue requirement that will enable Yarra Valley Water to deliver the outcomes valued by customers, and on its health, safety, environmental sustainability and social obligations.

The following chapters and sections of our final decision involved consideration of this factor:

- Our assessment of the revenue requirement (Chapter 4).
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).
- Our assessment of tariffs (Section 5.3).

Other matters

ESC Act section 8A(1)(c) requires us to have regard to ‘the degree of, and scope for, competition within the industry, including countervailing market power and information asymmetries’.

In relation to the above, Yarra Valley Water does not face any competition in the delivery of its prescribed services within its region. Our final decision takes this into account through our consideration of forecast efficient costs, and considering the service priorities of customers as revealed through a business’s customer engagement.

The following sections of our final decision involved consideration of this factor:

- Our assessment of engagement (Section 3.1)
- Our assessment of outcomes (Section 3.2)
- Our assessment of efficient operating expenditure (Section 4.1) and capital expenditure (Section 4.2).

We consider that our pricing approach helps to address market power and information asymmetries relating to the water businesses. Our PREMO water pricing approach provides incentives for a water business to provide its “best offer” to customers in its price submission. This is described in further detail in a report we released in 2016.⁶⁶

ESC Act section 8A(1)(e) requires us to have regard to the ‘benefits and costs of regulation (including externalities and gains from competition and efficiency) for: (i) consumers and users of products or services (including low income and vulnerable consumers); and (ii) regulated entities’.

We have had regard to benefits and costs of regulation by:

- Implementing a price review process so that water businesses may receive streamlined price reviews if they submit a high quality price submission. This reduces the costs of regulation for water businesses and the commission.
- Focusing our assessments of price submissions on the materiality of proposals to customer interests (including low income and vulnerable services), including in terms of price, bill and service impacts.
- Designing our guidance so we minimise the compliance costs for water businesses. Our guidance noted that much of the information required in price submissions should be readily available to water businesses as it would be relevant for other purposes such as corporate planning and project prioritisation and justification.⁶⁷

ESC Act section 8A(1)(f) requires us to have regard to ‘consistency in regulation between States and on a national basis’.

Similar to other state and national regulators, our economic regulatory approach:

- uses the building block method to estimate a water business’s revenue requirement
- allows water businesses to implement various forms of price control, including price caps and revenue caps

⁶⁶ Essential Services Commission 2016, *Water Pricing Framework and Approach, Implementing PREMO from 2018*, October, pp. 11–13.

⁶⁷ Essential Services Commission, *2023 water price review: Guidance paper*, p. 2.

- allows for consultation with key stakeholders during a price review, including through the release of a draft decision.

WI Act section 4C(a) requires us to ‘ensure that the costs of regulation do not exceed the benefits’.

We have sought to ensure that the costs of regulation do not exceed the benefits by:

- Implementing a price review process so that water businesses may receive streamlined price reviews if they submit a high quality price submission. This reduces the costs of regulation for water businesses and the commission.
- Focusing our assessments of price submissions on the materiality of proposals to customer interests (including low income and vulnerable services), including in terms of price, bill and service impacts.
- Designing our guidance so we minimise the compliance costs for water businesses. Our guidance noted that much of the information required in price submissions should be readily available to water businesses as it would be relevant for other purposes such as corporate planning and project prioritisation and justification.⁶⁸

⁶⁸ Essential Services Commission, 2023 water price review: *Guidance paper*, p. 2.

Appendix C – Service standards

We have accepted the following standards, and conditions of service and supply, and associated targets for Yarra Valley Water. Service standards are set out in the Water Industry Standard – Urban Customer Service (Urban Water Industry Standard). Accordingly, in early 2023-24, we will update the Urban Water Industry Standard to adopt these service standards and targets.

Water service standards – excluding flow rates

	2023-24	2024-25	2025-26	2026-27	2027-28
Maximum number of unplanned water supply interruptions a customer may experience in any 12-month period	2	2	2	2	2
Average time taken to attend priority 1 bursts and leaks (minutes)	24	24	24	24	24
Average time taken to attend priority 2 bursts and leaks (minutes)	36	36	36	36	36
Average time taken to attend priority 3 bursts and leaks (minutes)	286	286	286	286	286
Average time taken to restore customers' water supply – planned (minutes)	113	113	113	113	113
Average time taken to restore customers' water supply – unplanned (minutes)	101	101	101	101	101

Water service standards – flow rates

	Diameter of the property water service pipe (mm)				
	20	25	32	40	50
Minimum water flow rate (litres per minute)	20	35	60	90	160

Sewerage service standards

	2023-24	2024-25	2025-26	2026-27	2027-28
Maximum number of sewer blockages a customer may experience in any 12-month period	2	2	2	2	2
Average time taken to attend sewer spills and blockages (minutes)	47	47	47	47	47
Average time taken to rectify a sewer blockage (minutes)	139	139	139	139	139
Maximum time taken to contain a sewer spill (minutes)	240	240	240	240	240

Appendix D – Guaranteed service level scheme

We have adopted the following service level obligations and corresponding payment amounts for failure to attain the stated obligation as the guaranteed service level scheme for Yarra Valley Water. Guaranteed service levels are approved in the Water Industry Standard – Urban Customer Service (Urban Water Industry Standard). Accordingly, in early 2023-24, we will update the Urban Water Industry Standard to reflect the guaranteed service levels set out below.

In accordance with clause 20(b) of the Urban Water Industry Standard, Yarra Valley Water must ensure that any payment is made to a customer as soon as practicable after a customer becomes entitled to the guaranteed service level payment.

Yarra Valley Water is not required to make a payment where the failure to meet the service level is due to the action or inaction of the customer or a third party. For the avoidance of doubt, a third party does not include any person or firm acting on behalf of Yarra Valley Water.

Yarra Valley Water’s guaranteed service level scheme

Service level obligation	Payment (\$)
Planned interruptions to water and sewer supply	
We interrupt your water for more than five hours	\$50
The planned interruption is longer than we said it would be	\$50
We fail to give at least one week’s notice of planned water interruptions	\$50
We interrupt your water between 5am and 9am and/or 5pm and 11pm	\$50
Unplanned interruptions to water and sewer supply	
Your water supply is lost for more than four hours	\$50
An additional \$50 if the loss of your water supply extends more than 12 hours	\$50
We fail to restore your sewerage service within four hours. This does not include sewer service interruptions caused by your pipework.	\$50
An additional \$50 if we fail to restore your sewerage service within 12 hours. This does not include sewer service interruptions caused by your pipework.	\$50
You experience more than two unplanned water or sewerage interruptions during any 12-month period – \$50 for the third and each subsequent unplanned interruption	\$50
If we do not provide an adequate water flow rate (unless there is a restriction in place), we will waive the Water Supply System Charge until we meet the minimum standard rate	Waiver of Water Supply System Charge

[Continued next page](#)

Yarra Valley Water's guaranteed service level scheme (continued)

Service level obligation	Payment (\$)
Sewage spills caused by a fault in our sewerage system	
We fail to contain a sewage spill within your house within one hour of it being reported to us	\$1,000
You experience a subsequent sewage spill in your house within 12 months which isn't contained within one hour of it being reported to us	\$2,000
We fail to contain a sewage spill on your property within four hours of it being reported to us	\$1,000
You experience a subsequent sewage spill on your property within 12 months which isn't contained within four hours of it being reported to us	\$2,000
Water quality	
You contact us about two or more separate water quality issues in a 12-month period – \$50 for the third and each subsequent issue	\$50
An advisory notice is issued (covers a precautionary boil water advisory, do not drink or do not use advisory):	
<ul style="list-style-type: none"> Less than 50 of Yarra Valley Water's customers 	\$5000 community rebate per Local Government Area
<ul style="list-style-type: none"> 50 or more of Yarra Valley Water's customers 	\$10,000 community rebate per postcode affected
<ul style="list-style-type: none"> 50 or more customers covered by more than one retail water business 	\$10,000 community rebate per postcode impacted
Response to customers	
If we do not reply to your contact within four working days	\$50
Debt recovery actions	
We commence legal action or take steps to restrict your household's water supply prior to taking reasonable endeavours to contact you and provide information about the help that is available for customers experiencing financial difficulty	\$300

Note: These are nominal amounts, that is, the amount of payment will not be impacted by inflation.

Appendix E – Inputs to calculation of long-term inflation

Inflation – annual estimates (per cent)

	2023-24	2024-25	2025-26	2026-27	2027-28	Average
RBA geometric mean	7.0	4.1	3.1	2.5	2.5	3.8
Bond breakeven	7.0	2.3	2.3	2.3	2.3	3.3