

Melbourne Water proposes to commence a process of reform of waterways and drainage prices over the 2008 regulatory period with a view to moving away from property valuations as a basis for charging. Further reform is proposed for the 2013 regulatory period.

Individual price caps are proposed for waterway and drainage and diversion services.

It is proposed to continue the current methodology, approved by the Commission, for setting developer charges in development services schemes.

It is proposed that a core set of miscellaneous prices will be subject to the Commission's annual price approval process and additional miscellaneous prices will be subject to pricing principles.

This chapter sets out the proposed prices for waterways and drainage, diversions, developer and miscellaneous services for the 2008 regulatory period needed to recover the required revenues detailed in Chapter 11. The chapter also details the current prices and how the proposed prices differ from those in place during the 2005 regulatory period. It also provides details on the underlying cost justification for the proposed prices and discusses how the prices will change customer behaviour, as well as the impact these prices will have on customers.

Appendix 4 provides the price schedule setting out the proposed 2008/09 prices for waterways and drainage services, as well as diversions and miscellaneous services.

12.1 Principles

Clause 14 of the Water Industry Regulatory Order sets out the matters that must be taken into account in setting prices. In particular prices must:

- Provide appropriate signals to customers about the costs of providing particular services and choices regarding alternative supplies for different purposes
- Take into account the interests of customers including low income and vulnerable customers
- Enable customers to understand the prices charged
- Be consistent with a sustainable revenue stream for the business.

The proposed prices comply with these regulatory principles where applicable to waterways related services.

12.2 Waterways and drainage

12.2.1 Current prices

Melbourne Water's metropolitan prices for waterways and regional drainage services are calculated by multiplying a rate in the dollar by the 1990 Net Annual Value (NAV) of a property, subject to a minimum price. The metropolitan waterways and drainage prices for 2007/08 are set out in Table 12.1.

Table 12.1: Metropolitan waterways and drainage prices for 2007/08 (in 2006/07 dollars)

Minimum price (\$)	Rate in \$NAV (cents)
55.05	0.7728

The minimum price is currently paid by approximately 60% of residential customers and 14% of non-residential customers. Prices for typical residential customers range from the minimum to \$4,000, while prices for non-residential customers range from the minimum to over \$500,000.

The same rate in the NAV dollar applies to residential and non-residential customers with the exception of Koo Wee Rup Flood Protection District and Patterson Lakes special drainage areas, where higher rates in the dollar are charged to reflect the higher level of drainage services provided. Customers in the Shires of Baw Baw, South Gippsland and part of the Bass Coast pay a lower rate reflecting the fact that they receive waterways services but do not receive drainage services. Waterways and drainage prices for these areas for 2007/08 are set out in Table 12.2.

Table 12.2: Special drainage area prices for 2007/08 (in 2006/07 dollars)

	Minimum (\$)	Rate in \$NAV (cents)
Koo Wee Rup Flood Protection District		
Division A	55.05	3.600
Division B	55.05	2.000
Other Special Rate Areas		
Shires of Baw Baw, South Gippsland and part Bass Coast	31.46	0.3722
All other prices in the former special rate area	55.05	0.7728
Extra Fees for Patterson Lakes		
Tidal waterways	0.00	0.4066
Quiet Lakes	0.00	0.3346

12.2.2 Proposed prices

Microeconomic reform has seen water authorities across Australia move away from using property values as a basis for setting water, sewerage and drainage prices. In Melbourne, the use of property values in setting water and sewerage prices was phased out in the late 1990s. While there are some important differences with water and sewerage services (see Section 12.2.4), there is a need to develop pricing arrangements for waterways and drainage services that more effectively:

- Reflect the extent to which customers impact on, or benefit from, the services provided
- Achieve a higher level of transparency and customer understanding
- Deliver significant implementation and administration cost savings
- Take account of customer impacts relative to some other options
- Take account of the relationship between waterways and drainage services and other elements of the water cycle which promote more sustainable and efficient outcomes (e.g. creating incentives for greater stormwater re-use to reduce the demand on scarce potable water supplies)
- Provide an adequate and stable level of revenue to maintain services at an agreed standard.

An important first step in developing improved pricing arrangements is to move away from property based prices while recognising the need to manage customer impacts. Experience with the reform of water and sewerage prices indicates that any change to valuation based prices, including updating valuations, will result in material customer impacts. Therefore, reform of waterways and drainage prices to the preferred long-term position requires a staged approach. The staged approach will focus reform on areas of greatest gain first, while allowing sufficient time to work through complex issues and facilitate further work with State Government to clarify long-term objectives in relation to 'water cycle thinking'.

After investigating a number of alternative pricing methodologies to valuation based prices, Melbourne Water proposes an initial round of price reform over the 2008 regulatory period that includes the following prices from 2008/09:

- Commence phasing in a single service price for residential customers by increasing the minimum price to \$57 while maintaining prices for customers who currently pay above the minimum
- Decrease reliance on property values for non-residential customers by increasing the minimum price to \$75, with further reform during the next regulatory period
- Ensure rural customers only pay for the services they receive by replacing existing prices for rural customers located outside the Urban Growth Boundary with a lower waterways service price of \$36 (see Figure 12.1)
- Commence charging customers in the extended area for the provision of waterways and regional drainage services by introducing a single service price of \$57 per year for residential customers, \$75 for non-residential customers and \$36 for rural customers located outside Urban Growth Boundary
- Continue discussions with customer committees within the special drainage areas to move towards an improved basis for pricing.

The proposed waterways and drainage prices to apply from 2008/09 are outlined in Appendix 4.

12.2.3 Underlying cost justification

The current approach to pricing waterways and drainage services needs to be reviewed because of:

- The high cost of maintaining 1990 property values for billing purposes (almost \$1 million per annum)
- The link between a customer's capacity to pay (the original basis for choosing property values) and their current price is questionable as:
 - There have been significant changes in property values since 1990
 - 60% of residential customers currently pay the minimum price
- The use of 1990 property values is inconsistent with values used by local governments for rating properties, thereby creating customer confusion and complaints
- The consistency of valuation based prices with Water Industry Regulatory Order principles (e.g. prices reflect cost of service) is questionable
- There are a number of inherited pricing inconsistencies and anomalies within existing arrangements
- Appropriate pricing arrangements need to be developed and implemented in Melbourne Water's extended boundary areas.

Residential customers

Residential customers receive a wide range of social, recreational, economic and environmental benefits from the provision of regional services which includes flood protection for households and community assets (e.g. roads) and higher quality waterways. These benefits are broadly available to all customers who live, work or travel within the catchment and can be considered to be essentially uniform for all customers.

Consequently, a single price based on the average cost of providing services to residential customers is a reasonable proxy for the benefits received and costs incurred by this group.

Non-residential customers

In contrast to residential customers, there are significant differences between non-residential customers (who range from cafes and shopping centres, to warehouses) in terms of:

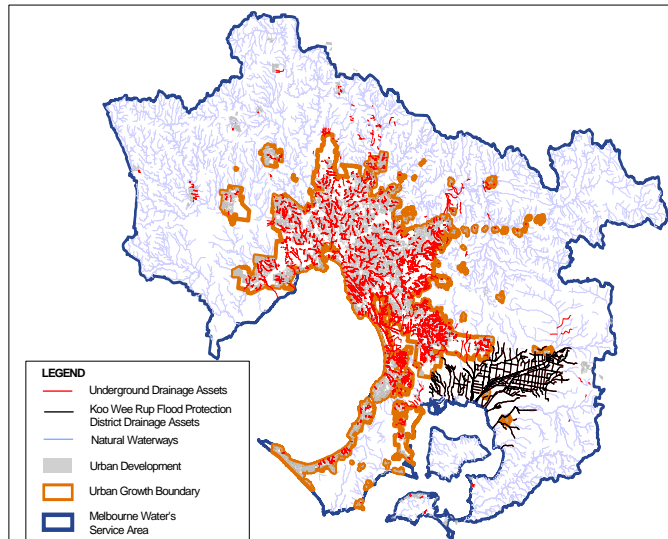
- The costs they impose on services (e.g. as measured by their contribution to stormwater run-off)
- The level of benefits they receive (e.g. the level of foregone earnings as a result of flooding)
- Opportunities to change behaviour to reduce the quantity (e.g. through stormwater reuse) or improve the quality of stormwater run-off from their property.

Rural customers

As illustrated by Figure 12.1, with the exception of the Koo Wee Rup Flood Protection District, Melbourne Water's regional drainage assets are located predominantly within urban areas which has been designated by the Urban Growth Boundary¹. As customers located outside the Urban Growth Boundary (which is largely comprised of rural properties) do not receive the full benefits of Melbourne Water's regional drainage services, it is proposed that these customers pay for the cost of waterways services only.

¹ Defined in the State Government's Melbourne 2030 which indicates the long term limits of urban development and where non-urban values and land uses should prevail in metropolitan Melbourne

Figure 12.1: Urban Growth Boundary and Melbourne Water assets



Extended areas

Given that customers within the extended areas will receive an equal level of waterways and regional drainage services to other areas within Melbourne Water's service area, it is proposed that prices be uniformly applied across the whole of the Port Phillip and Westernport catchment areas.

12.2.4 Changes in customer behaviour

Melbourne Water provides waterways and drainage services on a regional basis. Unlike water and sewerage services, waterways and drainage services provided to individual customers are not metered, as revenue from volumetric stormwater prices would only be collected during rainfall events. It is, therefore, not possible to accurately measure the unique benefits individual customers receive or the costs they impose on the diverse nature of the waterway and drainage services.

Expenditures in individual catchments are prioritised on a regional basis that generally provide benefits over long periods of time. Consequently, expenditures within any given catchment vary significantly from one regulatory period to the next, whereas benefits do not vary significantly. If prices reflected actual expenditure within regulatory periods and were levied on a catchment basis, this would result in significant volatility and adverse customer impacts. There would also be significant differences in the prices that would be applied between catchments. This could lead to inequitable outcomes given that customers outside a catchment and customers in future periods could enjoy the benefits from works paid for by existing customers within the catchment ².

² Examples of where customers living outside a catchment could benefit from Melbourne Water works within that catchment include a farmer using a road that would have otherwise been flooded to transport their crop to market or a residential customer enjoying the aesthetic benefits of visiting a healthy waterway.

Melbourne Water, therefore, proposes that the objective for the 2008 regulatory period should be to:

- Move to a basis for pricing that is more reflective of the costs and benefits associated with different classes of customers
- Establish pricing arrangements that are more cost effective to administer i.e. so that the revenue collected from customers is spent on delivering outcomes rather than calculating bills.

Finally, it is worth noting that continuing with the current basis for pricing is an unattractive option because:

- Current prices bear no relation to costs
- It is a poor reflection of customers' capacity to pay
- Simply updating property values based on the most recent valuation will involve significant customer impacts and substantial ongoing administrative costs.

12.2.5 Customer impact issues

While price reform is proposed on a number of different fronts, and will affect customers differently, the proposed prices for customers in the existing service areas would increase on average by CPI+1% per year over the 2008 regulatory period. This increase is consistent with delivering the service outcomes discussed in Chapter 5 and expenditures in Chapters 8 and 9. The proposed prices for the different customer groups and associated impacts are discussed below.

Residential customers

Melbourne Water proposes to transition residential prices to the average cost by increasing the minimum price by \$2 plus inflation each year over the 2008 regulatory period and maintaining prices for customers who currently pay above the minimum until the transitional arrangements are complete in 2012/13.

Setting the minimum price at \$57 in 2008/09 would increase customer bills by \$2 in real terms for 60% of residential customers (about 804,000) who currently pay the minimum price of \$55. Prices for 40% of customers currently paying above the minimum (about 539,000) would remain constant in real terms.

Table 12.3 outlines the proposed price path for residential customers over the 2008 regulatory period. The average price for a customer paying above the minimum in 2007/08 has been used to illustrate the price path for these customers.

Table 12.3: Proposed price path for residential customers – 2008/09 to 2012/13 (in 2006/07 dollars)

		Current	Proposed				
		2007/08 (\$/yr)	2008/09 (\$/yr)	2009/10 (\$/yr)	2010/11 (\$/yr)	2011/12 (\$/yr)	2012/13 (\$/yr)
Residential properties	Paying minimum price	55.05	57.10	59.23	61.43	63.71	66.08
	Above minimum price (average)	88.13	88.13	88.13	88.13	88.13	66.08

Non-residential customers

As experienced with the reform of water and sewerage prices, there are challenges associated with moving away from property values for the non-residential sector given the large diversity in property sizes, land uses, land management activities and prices paid by customers. Any form of tariff reform will result in customer impacts and would take time to manage and implement.

An extensive review that commenced following the Commission's 2005 Price Determination explored a number of price reform options for non residential customers. The review highlighted the diversity within current non residential prices and the significant potential impacts of moving to a more cost reflective approach.

As a first stage reform measure, Melbourne Water proposes that the current minimum price be increased to \$75 in 2008/09 and property values be retained pending further analysis and development of reform proposals for inclusion in the next regulatory period.

Increasing the minimum from \$55 to \$75 in 2008/09 increases the number of non-residential customers paying the minimum price from around 16,000 (14%) to approximately 27,200 (23%). This reduces reliance on property values and establishes a higher base price upon which future tariff reform can take place.

Table 12.4 outlines the proposed price path for non-residential customers over the 2008 regulatory period. The average price for a customer paying above the minimum in 2007/08 has been used to illustrate the price path for these customers.

Table 12.4: Proposed price path for non-residential customers – 2008/09 to 2012/13 (in 2006/07 dollars)

		Current			Proposed		
		2007/08 (\$/yr)	2008/09 (\$/yr)	2009/10 (\$/yr)	2010/11 (\$/yr)	2011/12 (\$/yr)	2012/13 (\$/yr)
Non-residential properties	Paying minimum price	55.05	75.12	77.73	80.42	83.21	86.10
	Above minimum price (average)	455.00	470.79	487.12	504.03	521.52	539.61

Rural customers

Moving to a waterways service price of \$36 in 2008/09 for rural customers located outside the Urban Growth Boundary would result in an average \$45 decrease for about 47,000 residential and non-residential customers.

It is also proposed that historic exemptions be removed for 3,200 farm properties in the Yarra and Maribyrnong catchments which have received services following previous extensions of Melbourne Water's service area in 1981 and 1984. This would ensure these customers contribute equitably to reflect the benefits they receive. Of these properties, 95% are located outside the Urban Growth Boundary and would pay a price of \$36 for waterways services.

Table 12.5 outlines the proposed price path for rural customers over the 2008 regulatory period. The average price for a customer paying above the minimum in 2007/08 has been used to illustrate the price path for these customers.

Table 12.5: Proposed price path for rural customers – 2008/09 to 2012/13 (in 2006/07 dollars)

		Current 2007/08 (\$/yr)	2008/09 (\$/yr)	2009/10 (\$/yr)	Proposed 2010/11 (\$/yr)	2011/12 (\$/yr)	2012/13 (\$/yr)
Rural properties	Paying minimum price	55.05	35.89	37.14	38.43	39.76	41.14
	Above minimum price (average)	112.44	35.89	37.14	38.43	39.76	41.14

Extended areas

Introducing 1990 property values as a basis for charging residential and non-residential customers in the extended areas is expensive and likely to result in customer confusion and be difficult to explain.

It is recommended, therefore, that in light of the proposal to move residential customers to a single service price over the 2008 regulatory period, a flat service price of \$57 be applied in 2008/09 for all residential customers (approx 118,000) in the extended area. Due to further investigations planned for non-residential prices and potential future reforms, it is also proposed that a flat service price of \$75 be applied in 2008/09 for all non-residential customers (approx 5,000 customers) in the extended area as an interim measure.

An estimated 54,000 customers outside of the Urban Growth Boundary would pay a fixed waterways service price of \$36.

Table 12.6 outlines the proposed price path for extended area customers over the 2008 regulatory period.

Table 12.6: Proposed price path for extended area customers – 2008/09 to 2012/13 (in 2006/07 dollars)

	Current 2007/08 (\$/yr)	2008/09 (\$/yr)	2009/10 (\$/yr)	Proposed 2010/11 (\$/yr)	2011/12 (\$/yr)	2012/13 (\$/yr)
Residential properties	N/A	57.10	59.23	61.43	63.71	66.08
Non-residential properties	N/A	75.12	77.73	80.42	83.21	86.10
Rural properties	N/A	35.89	37.14	38.43	39.76	41.14

Special drainage areas

Customers in the Koo Wee Rup Flood Protection District and Patterson Lakes special drainage areas represent 0.3% of Melbourne Water's customer base. Melbourne Water sets prices for these customers in consultation with local customer advisory committees.

Melbourne Water has consulted on its intention to reform special drainage area prices over the 2008 regulatory period. Working with customer advisory committees to appropriately manage any customer bill impacts will be an important consideration in this process. In the interim, it is proposed that the current approach and principles used to set prices for these customers be retained for around 3,000 customers in the Koo Wee Rup Flood Protection District and approximately 1,200 customers in the Patterson Lakes area.

12.2.6 Stakeholder consultation

A working group with representatives from Melbourne Water and the Department of Sustainability and Environment was established to agree on long term objectives, review the options available to reform waterways and drainage prices, and explore options for managing customer impacts.

Melbourne Water has consulted with retail water businesses on implementation issues. Local government in Melbourne Water's extended area has also been consulted on service levels and proposed prices.

12.2.7 Community consultation

A number of submissions were received from the community in response to Melbourne Water's 2008 Waterways Water Plan Consultation Draft. Some of these questioned whether Melbourne Water's waterway and drainage services should be funded directly by the State Government, as done for waterway services outside Melbourne Water's service area. While some Government funding is received for specific programs, for the purposes of this Water Plan Melbourne Water has assumed that the vast majority of its costs will continue to be provided on a full cost recovery basis. Consequently, Melbourne Water has focused on developing prices that recover its costs from customers in the most efficient and equitable manner practical.

12.3 Diversion prices

12.3.1 Current prices

Melbourne Water currently administers about 1,900 active licences and farm dam registrations for diversion of some 45,000 megalitres (ML) of surface water from waterways. Licences in the Yarra catchment, Stony Creek, Kororoit Creek, Laverton Creek and Skeleton Creek are for supply of water from unregulated streams. Licences for the Maribyrnong River are supplied from a regulated river system via releases made to the river from Rosslynne Reservoir. Licences are issued according to the period when water can be diverted from the waterway, peak (year round) or off-peak (winter fill), and whether the water is diverted for consumptive or non-consumptive uses (whereby water is returned to the system under a discharge licence).

Active licences that have an entitlement of greater than 5 ML are metered to monitor a licensee's compliance with their allocated entitlement, which is subject to water availability.

Diversion prices are set to recover the costs for services related to billing and collections and monitoring and enforcing customer compliance with licence conditions.

Melbourne Water's current diversion prices comprise two components – an annual service price for the administration of licences and a volumetric price that applies to each ML of the licence entitlement (as opposed to actual usage).

In addition to the annual service and volumetric prices, once-off administration fees are charged to process applications for new licences, transfer licence entitlements or reissue licences.

The diversion prices applying in 2007/08 are shown in Table 12.7.

Table 12.7: Diversion prices for 2007/08 (in 2006/07 dollars)

Licence	Annual service price (\$/Annum)	Volumetric per ML price (\$/ML)
Unregulated waterways		
All months	173.66	11.71
Off-stream winter-fill	173.66	5.90
On-stream winter-fill	173.66	5.90
Licensed farm dam	173.66	5.90
Dam operating licence	61.46	N/A
Non-consumptive	173.66	1.13
Power generation (plus \$16.59 per kilowatt)	173.66	N/A
Regulated waterways		
All months	173.66	35.12
Off-stream winter-fill	173.66	5.90
Administration fee		Fee (\$)
Unregulated waterways		
Works/construction licence		526.83
Transfer of ownership (including temporary)		87.80
Transfer of ownership with dam sharing agreement		175.61
Resource assessment fee for downstream trade/transfer		282.9
Resource assessment fee for upstream or cross catchment trade/transfer		565.85
Licence renewal fee following failure to renew (domestic and stock)		87.80
Licence renewal fee following failure to renew (all other licences)		175.61
Reissue after Melbourne Water cancellation or breach of conditions		487.80
Diversion licences - meter		Cost of meter
Regulated waterways		
Diversion licence		273.17
Works/construction licence		526.83
Transfer of ownership along Maribyrnong River (includes temporary)		87.80
Licence renewal fee following failure to renew (domestic and stock)		87.80
Licence renewal fee following failure to renew (all other licences)		175.61
Reissue after Melbourne Water cancellation or breach of conditions		487.80
Diversion licences - meter		Cost of meter

12.3.2 Proposed prices

Melbourne Water proposes to retain the existing two part tariff structure for diversion services which comprise an annual service price and a volumetric price, as well as individual one-off administration prices where relevant. Consistent with reforms introduced in the 2005 regulatory period, and the WIRO principles, it is proposed to increase prices to achieve full cost recovery in order to:

- Strengthen price signals around scarce water resources
- Inform customer decisions on water use
- Ensure that service levels meet changed Government requirements and customer expectations.

Due to continuing drought conditions, which have caused considerable hardship on many licence holders, there has been a need to balance cost reflectivity principles with equity and affordability considerations in determining prices for the 2008 regulatory period.

Melbourne Water has attempted to balance these considerations by applying a larger increase to volumetric prices than annual service prices, as customers are more able to respond to the volumetric price signal by decreasing their costs through more efficient water use.

Melbourne Water's proposal for the 2008 regulatory period is to increase annual service prices by an average of 4% per annum, increase volumetric prices by an average of 16% per annum and increase administration fees on average by 4% per annum.

The increase in prices is due to additional costs incurred to meet changes in water resource management requirements along with new initiatives to improve customer service. These include:

- Contributing to the creation of a State-wide register for water entitlements and collection of an environmental water reserve contribution from water users under the State Government's White Paper
- Additional labour to more effectively manage customer compliance and enforcement with license requirements and to manage emerging requirements for licensing stormwater diversions in accordance with the CRSWS
- Implementing technology to improve the level of information customers receive on their metered water levels and status on restrictions or bans on extracting water, and to meet the Commission's requirements in relation to performance reporting
- Implementation of Streamflow Management Plan requirements in regards to monitoring water flows.

Melbourne Water is also working with the State Government to clarify the framework for unbundling diversion prices for regulated waterway systems to meet requirements under the Government's Our Water Our Future. A decision is likely to be made within the 2008 regulatory period.

The diversion prices proposed to be applied in 2008/09 are shown in Table 12.8.

Table 12.8: Diversion prices for 2008/09 (in 2006/07 dollars)

Licence	Annual service price (\$/Annum)	Volumetric per ML price (\$/ML)
Unregulated waterways		
All months	182.75	13.65
Off-stream winter-fill	182.75	6.88
On-stream winter-fill	182.75	6.88
Licensed farm dam	182.75	6.88
Dam operating licence	62.44	N/A
Non-consumptive	182.75	1.25
Power generation (plus \$16.75 per kilowatt)	182.75	N/A
Stormwater	182.75	13.65
Regulated waterways		
All months	182.75	41.17
Off-stream winter-fill	182.75	6.88
Administration fee		Fee (\$)
Unregulated waterways		
Diversion/stormwater licence		320.38
Works/construction licence		537.78
Transfer of ownership (including temporary)		92.33
Transfer of ownership with dam sharing agreement		185.60
Resource assessment fee for downstream trade/transfer		320.38
Resource assessment fee for upstream or cross catchment trade/transfer		589.36
Licence renewal fee following failure to renew (domestic and stock)		86.81
Licence renewal fee following failure to renew (all other licences)		173.61
Reissue after Melbourne Water cancellation or breach of conditions		584.79
Regulated waterways		
Diversion licence		320.38
Works/construction licence		537.78
Transfer of ownership along Maribyrnong River (includes temporary)		92.33
Licence renewal fee following failure to renew (domestic and stock)		86.81
Licence renewal fee following failure to renew (all other licences)		173.61
Reissue after Melbourne Water cancellation or breach of conditions		584.79
Diversion licences – meter		Cost of meter

12.3.3 Underlying cost justification

Melbourne Water's proposed prices are reflective of the overall efficient costs associated with providing diversion services and are considered consistent with Water Industry Regulatory Order requirements as the proposed prices:

- Create incentives for the sustainable use of water resources by providing signals to water users about the costs of providing services during peak and off-peak filling periods and setting prices that promote the extraction of water during higher flow periods
- Introduce prices for obtaining a new licence for stormwater diversions providing customers with signals around alternative supplies
- Take into account the interests of customers by setting prices that attempt to balance cost reflectivity principles with equity and affordability considerations
- Acknowledge that customers are familiar and readily understand and support the two part tariff structure which is used by other water authorities
- Provide a sustainable revenue stream for Melbourne Water that is based on an efficient level of expenditure.

Melbourne Water is currently finalising its Customer Charter for Diversion Services with the Commission. As a result of feedback received, Melbourne Water will need to implement measures not included in proposed diversion prices and further consult with customer committees on other suggested amendments. Melbourne Water is working to resolve these issues before the Determination is released.

12.3.4 Changes in customer behaviour

River and stream diversions are subject to water availability and, therefore, there is a need to manage the limited water resource and enforce compliance with licence conditions to protect the rights of users along with protecting the needs of the environment.

It is important that price signals are provided to customers in terms of the value of, and access to, water during different filling periods.

Melbourne Water considers that setting differential prices according to peak and off-peak filling periods provides customers with information on the underlying costs of providing services and therefore, facilitates a better understanding of economically desirable water trading opportunities. In addition, applying a larger increase to volumetric prices than annual service prices will strengthen signals around the value of water resources and promote the diversion of water from waterways during higher flow periods.

12.3.5 Customer consultation

Melbourne Water has consulted on proposed services, costs and diversion prices for the 2008 regulatory period with its customer advisory committees. Feedback received from the advisory committee representing licence holders on regulated waterway systems indicates that the proposed costs and price increases are not considered unreasonable. However, the committee placed a greater weighting on Melbourne Water delivering the proposed actions to improve information services than providing additional resources to manage customer compliance with license requirements.

The advisory committee representing licence holders on unregulated waterway systems were supportive of Melbourne Water's proposals and recognised that increased compliance monitoring is necessary to protect water entitlements for all diverters.

Both committees noted that the major concern for license holders is currently the security of access to water resources.

12.4 Developer charges

Melbourne Water proposes to continue the current methodology for setting developer charges in development service schemes. The methodology consists of:

- Identifying future capital expenditure for each year of the expected life of the development service scheme
- Identifying forecast developable hectares for each year using an estimate of development density
- Applying a pre-tax real discount rate (consistent with that determined by the Commission) to convert future cash flows into present value terms
- Setting the developer charge such that the present value of future income equals the present value of future costs. Future income is equal to the developable hectares in each year multiplied by the developer charge
- Reviewing the financial assumptions relating to each scheme on an annual basis and reviewing engineering specifications every five years.

Examples of charges for development scenarios covered by Melbourne Water's developer charges (greenfield, redevelopment and non-scheme areas) can be found in Appendix 5 and a detailed description of Melbourne Water's developer charges and how they are calculated can be found at <http://ldm.melbournewater.com.au>.

Since September 2005, Melbourne Water has operated a general stormwater quality offset (a financial contribution to Melbourne Water for regional water quality works) on new development. This provides a mechanism for equitably addressing stormwater quality standards that optimise contributions made by onsite works, development service scheme and regional initiatives. Melbourne Water proposes to retain this program and its associated principles in its current form.

The following areas are discussed in the sections below:

- Addresses issues raised by the Commission in its 2005 Price Determination
- Reforms of development service schemes
- Identifies customer impact issues associated with a government initiative to further promote at source water sensitive urban design
- Updates the stakeholder consultation process.

12.4.1 Issues raised by the Commission

In its 2005 Price Determination, the Commission raised issues in relation to developer charges generally and drainage developer charges. In particular, the Commission recommended that Melbourne Water change its methodology to recognise:

- That only those assets that directly contribute to servicing development are recovered via developer charges (i.e. exclusion of sunk costs)
- That there is an interaction between waterways and drainage annual rates and developer charges
- Adjustments for errors in forecasting.

Responses to these issues are set out below.

In considering water and sewerage developer charges, the Commission was of the view that only those assets that directly contribute to servicing development are recovered via developer charges. Melbourne Water contends that the instance of sunk assets in development service schemes is negligible due to the absence of pre-existing assets in the schemes. Schemes are highly localised geographically to minimise cross subsidies and planned so that infrastructure is only provided when specified growth triggers are reached.

The Commission observed in its 2005 Price Determination that it would be appropriate for Melbourne Water to consider the interaction between its drainage charges and developer charges over the next regulatory period.

In other words, it is contended that a revenue offset be considered to discount up front developer charges by an amount equivalent to the present value difference between the costs of maintaining brand new drainage assets and the ongoing annual drainage rates paid by householders in new estates. While this may be valid for pipelines and hard engineering assets, a major and increasing proportion of development service scheme assets are made up of soft engineering works such as wetlands, which have consistently high maintenance costs (e.g. grass cutting, vegetation maintenance, etc) over their entire lives.

In view of the likely reduction in materiality (due to the offsetting impact of soft engineering maintenance profiles), and the ongoing nature of the annual drainage charge structure reform process, which increases the complexity of responding to this issue, Melbourne Water does not propose the introduction of revenue offsets for the 2008 regulatory period.

The Commission has commented that annual scheme financial reviews only adjust charges paid by future developments for errors in forecasting. The charges are also regarded as heavily dependent upon long-term forecasts and, therefore, Melbourne Water has substantial discretion over the size of developer charges at any point in time. In response, Melbourne Water considers that attention to detailed planning as well as regular financial reviews (annual) and engineering reviews (five yearly) are the keys to maximising forecasting accuracy and minimising discretion over the setting of developer charges. Scheme rate adjustments for annual financial reviews are also limited to no more than +/- 10 % per annum (following consultation with the development industry) and, therefore, cross subsidisation is not considered excessive.

12.4.2 Reforms of development services schemes

Over the 2005 regulatory period a number of reforms have been or are in the process of being implemented to improve the robustness of the development services schemes from a pricing perspective. These include:

- Revision and periodic review of interim charges paid by developers while new development service schemes are being prepared to more accurately signal the expected final rate. Developers will continue to receive refunds if the final rate is less than the interim rate.
- Reform of development service scheme provisions to more accurately estimate likely additional expenditures or loss of contributory land area
- Retirement of completed schemes and conversion of nearly complete development service schemes to “inactive” status in order to more effectively manage the overall portfolio of schemes
- Review of the criteria for adjusting development service scheme rates following engineering reviews
- Review of redevelopment services scheme program and implementation of a risk management plan
- Bi-annual review of the general stormwater quality offset rate.

12.4.3 Customer impact issues

With the exception of Clause 56 of the Victorian Government's Sustainable Neighbourhoods package to create more sustainable and livable communities, i.e.: local government is required to set water sensitive urban design requirements for residential subdivisions with the costs to be met by developers, customer impacts are minimal given that no significant changes are proposed.

New measures for residential subdivisions were introduced from October 2006 as part of the State Government's Sustainable Neighbourhoods package (Victorian Planning Provisions) to create more sustainable and liveable communities. The measures replace existing Clause 56 provisions in planning schemes.

The new provisions require local government to become more involved in managing the achievement of best practice water quality objectives within each subdivision by setting requirements for individual developers.

For Melbourne Water, the impact of Clause 56 is to downsize planned water quality works in future development service schemes in proportion to expected water quality outcomes achieved by developers under council guidance. Local government and developers have required assistance in coming to terms with the new requirements. Melbourne Water has therefore established a dedicated resource for the provision of technical assistance and support to local government.

12.4.4 Stakeholder consultation

Melbourne Water maintains an ongoing forum, the Development Services Scheme Review Group, consisting of development industry peak bodies and local government representatives. The purpose of the group is to maintain overarching principles governing the operation of development service schemes and consider issues relevant to the effective operation of schemes from a stakeholder's viewpoint. The principles are set out in Appendix 5.

12.5 Miscellaneous services

Melbourne Water provides a small number of miscellaneous waterways and drainage services to the public. Some are similar in nature to the retail water businesses, such as services to the land development industry and information statements. Other services are specialist in nature, i.e. hydrological and flood level data provision.

In its December 2006 Framework and Approach paper, the Commission raised concerns about the range, definition and pricing for miscellaneous services. In particular, the Commission felt that the prices proposed for miscellaneous services should address the following principles:

- Prices should be consistent with the broader objectives of the business
- Prices should be effective in providing adequate signals to customers
- Proposed prices need to have consideration for their impact on customers.

Following consideration of the responses to its Framework and Approach paper, the Commission's March 2007 Guidance Paper further proposed that businesses identify within their Water Plans a core set of miscellaneous services that will be subject to the annual price approval process and subsequently included in the tariff schedule. The Commission proposed that non-scheduled miscellaneous prices should be set such that they:

- Reflect the direct costs of service provision (including materials and/or costs associated with contractors)

- Reflect the internal costs incurred by the water businesses such as labour, transport and general overheads
- Exclude costs previously accounted for in approved prices for new miscellaneous services
- Are transparent.

Melbourne Water's miscellaneous prices for waterways and drainage services are identified in Appendix 4 and summarised in Table 12.9.

Table 12.9: Definitions of key regulated miscellaneous charges

Definition of charge	Fee charged to	Basis for charge
Property flood level information – provision of a flood level certificate in PDF format within 10 days of receiving a request under S. 264 of the <i>Water Act 1989</i> .	Information retailers (ANSTAT, Land Data)	Recovery of administrative costs
Provision of hydraulic data – stream flow, levels, storm intensity and rainfall in hardcopy or digital format within 10 days of receiving a request.	Public	Recovery of administrative costs
Build overs – costs of processing development proposals that involve construction over Melbourne Water easements.	Developers	Recovery of administrative costs
Stormwater connections - Melbourne Water requires all new stormwater connections to be made to the local council system. Where this is not possible a stormwater connection application must be made to Melbourne Water under S.145 of the <i>Water Act 1989</i> .	Developers	Recovery of administrative costs
Flood feasibility studies - Melbourne Water's assistance in determining the most appropriate drainage works that would be required to service a development.	Developers	Recovery of administrative costs
Encumbrance and certificate fees (Property Information Statements) provided consistent with S.158 of the <i>Water Act 1989</i> .	Public / developers	Recovery of administrative costs

12.6 Form of price control

At this stage, Melbourne Water proposes to use individual price caps for its waterways and drainage, diversions and miscellaneous services over the 2008 regulatory period. This continues the approach used during the 2005 regulatory period and means that each of the prices approved by the Commission will be escalated annually by applying the 'CPI+X' formula with no rebalancing between prices within the regulatory period. It will provide customers with certainty regarding the prices they will face in the future.

In addition, Melbourne Water proposes to continue to use the Commission's drainage pricing principles for its special drainage areas to facilitate the reform of prices for these areas over the 2008 regulatory period. Pricing principles are also recommended for development service schemes and the stormwater quality offsets program.