



Ms Liz Livingstone  
Chief Executive Officer  
Independent Pricing and Regulatory Tribunal  
Level 15, 2-24 Rawson Place  
Sydney NSW 2000

Our ref: OUT21/4695  
File: PUB21/232

14 April 2021

Dear Ms Livingstone

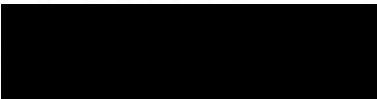
**Subject: Water Administration Ministerial Corporation draft price determination**

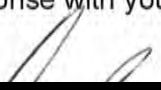

Thank you for the opportunity to respond to IPART's draft report and draft determination of Water Administration Ministerial Corporation (WAMC) prices for the period 2021-22 to 2024-25.

Please find attached a joint response to the draft report and draft determination from the Department of Planning, Industry and Environment and the Natural Resources Access Regulator.

We would welcome the chance to discuss any aspects of our response with you and can provide additional information to help inform IPART's decisions if needed.

Yours sincerely

  
Jim Bentley  
Deputy Secretary, Water  
Department of Planning, Industry and Environment

  
  
Grant Barnes  
Chief Regulatory Officer  
Natural Resources Access Regulator

## Response to the draft Water Administration Ministerial Corporation price determination

---

*From Department of Planning, Industry and Environment – Water and the Natural Resources Access Regulator*

---

### Summary of response to IPART's draft determination

In its draft determination, IPART has applied all of the adjustments and efficiency reductions recommended by its expenditure consultant, Cardno. This has resulted in a \$29.2 million reduction to Water Administration Ministerial Corporation's (WAMC) proposed revenue for delivering essential water management services in NSW.

The Department of Planning, Industry and Environment and the Natural Resources Access Regulator (NRAR) are concerned about the significant implications these cuts have for meeting essential water management services and key Government water priorities. We challenge the basis on which IPART justified each of the reductions.

We also consider that the cumulative impact of these reductions, on top of efficiency savings already offered by the department and NRAR to mitigate price impacts, will put at risk water resource management outcomes critical to water users, the environment and the regional NSW economy. We argue that the reductions to the proposed costs of providing water management services will result in unacceptable service delivery risks.

The relationship between cost reductions and water management risks is starkly evidenced by the fact that the draft determination makes cuts to the set of water management activities that the Independent Commission Against Corruption (ICAC) recommended be strengthened in late 2020. It recommended the establishment of a dedicated unit to drive water sharing plan implementation.

ICAC did not publish the results of its investigation into Barwon– Darling arrangements until November 2020. We consider it critical that IPART carefully consider ICAC's recent findings before finalising its decisions on WAMC costs. We note that this information was not available when WAMC agencies made their submissions or for IPART's public hearings.

We dispute Cardno's expenditure review methodology, particularly its inter-jurisdictional benchmarking methodologies, and its recommended adjustments to our proposed costs in tandem with arbitrary 'catch-up' and continuing efficiencies. Our submission requests that IPART consider a number of key matters, as summarised in this document.

## Summary of concerns with IPART's recommendations on costs

### **IPART's \$29.2 million reduction in proposed WAMC revenue and increases in operating expenditures of only 2.2% puts improvements in water management at risk**

Over the last four years, the NSW Government has invested in reforms to water management and improvements in service levels in response to several independent reviews and stakeholder expectations. IPART's draft report acknowledged that additional investment in key areas is needed to enable WAMC to provide a more sustainable, reliable water resource management system.

Despite reaching this conclusion, IPART's reductions to proposed costs equate to a 2.2% increase in operating expenditure when compared with the current determination. This is only a small increase on the levels of funding of 2016, which were found to be manifestly inadequate by multiple external reviews. It is also inconsistent with IPART's overarching conclusion that service improvements are justified.

The department and NRAR proposed that increases of 35% to WAMC costs are necessary to respond to the challenges of rural water management identified since 2016. The operational risks arising from each of the specific cuts included in IPART's draft recommendations are detailed in full in this response. We request that IPART consider these risks when determining the final revenue requirement.

### **We support customer affordability but are concerned by risks arising from the extent of the proposed cost reductions**

We agree with IPART about the need to manage affordability for rural water users while transitioning to the full cost recovery of water management services. This was evidenced in our proposed cap on price increases despite the costs of WAMC water management services increasing by 35%.

However, we do not agree with the extent of IPART's cuts to our proposed costs. We believe IPART should re-evaluate its draft cost adjustments and be clear about how it recommends recovering any revenue shortfall resulting from capped price increases.

### **IPART's efficiency cuts will have adverse impacts on water users and would result in a cumulative efficiency goal of over \$100 million over four years for WAMC agencies**

We support IPART's position that it is important for prices to capture gains in efficiency over time. As acknowledged by IPART, the department and NRAR have submitted plans to IPART for a \$73.6 million efficiency target over the 2021 determination period.

Despite this, IPART has applied further arbitrary catch-up and continuing efficiencies to the costs of WAMC activities, as well as adjustments to revenue. IPART has done this without considering the cumulative impact of these cuts on the capacity to deliver water management outcomes. IPART's review methodology appears focused on capturing gains from theoretical economies of scale and technological advancements.

We consider that a cumulative efficiency goal of over \$100 million is unrealistic and would have adverse impacts on water users. We also question the future incentives that this decision might create for regulated agencies who may otherwise voluntarily identify potential efficiency opportunities. IPART's draft decision applies an arbitrary methodology to judge the

relative efficiency of WAMC, a relatively unique price regulated service entity, and lacks the safeguard of analysis to ground-truth the methodological concepts.

**We are concerned that IPART has not sufficiently tested the relationships between Cardno's recommended reductions or their cumulative impact**

We argue that in applying all of Cardno's recommended reductions to our proposed costs, IPART is adopting fundamental flaws in Cardno's recommendations. This is particularly concerning for IPART's recommendations for the Regional Water Strategies program, where IPART has applied Cardno's recommendation to cut 25% of costs in each of the first two years without further testing.

We consider that Cardno has adopted a flawed approach to benchmarking compliance management efficiency by using a comparator that is not 'like-for-like'. Cardno's recommendations are both arbitrary and based on a misunderstanding of water planning options assessment.

Furthermore, the expected consequences of proposed reductions have not been presented in the Cardno report or acknowledged in IPART's draft report. For example, Cardno's suggested alternative approach to delivery and proposed cuts to the Regional Water Strategies program will lead to the delayed implementation of all 12 regional water strategies. However, Cardno did not present this qualifying information about this impact in its recommendation, including that a delay is contrary to Government election commitments to the NSW public. Cardno's report and IPART's draft report do not appear to have fully considered or presented the consequences of specific cuts on related activities.

In relation to compliance management, Cardno has adopted a flawed approach to assessing efficient compliance management costs by not using 'like-for-like' benchmarking comparators. This has led to IPART recommending a baseline amount for compliance management costs of \$5.8 million per year, partly on the basis that the non-urban metering reforms will be fully implemented by 2024 and that these reforms will address any benchmarking comparator concerns. This implementation date is at risk if metering prices cannot be determined before 1 July 2021.

**We welcome IPART's recognition that NRAR needs to be properly funded but are concerned that IPART's draft decision has negative long-term implications**

While we welcome IPART's recommendation on the total cost of compliance for the 2021 determination period, we are concerned by the methodology used to arrive at this draft position and also by the inferences in the draft report about the likely longer-term efficient water compliance costs.

In particular, we are concerned by the conclusion that the longer-term efficient compliance costs are \$5.8 million per year (\$2020–21). These costs approximate the levels of chronic underfunding that both the Matthews' and Ombudsman's inquiries found were manifestly inadequate to protect the interests of water users and the public. Returning to these levels would likely again generate significant community concern about the enforcement of water laws and undo the substantial progress made since 2018.

## **IPART's reprofiling of the Regional Water Strategies program expenditure will have perverse outcomes for stakeholders**

We are concerned that IPART's recommendation to reduce the efficient cost of these activities by 25% in each of the first two years of the regulatory period is excessive and will lead to a perverse outcome of negative outcomes for water users. IPART has based its recommended adjustment on Cardno's expenditure review finding, which is based on a fundamental misunderstanding of the role of stakeholder consultation in regional water planning. Cardno assumes that options assessment takes place after consultation instead of the more efficient approach of undertaking in parallel.

The planning and stakeholder engagement work must run in tandem and is an iterative process. For at least six of the regional water strategies that were released in draft in late 2020, the department is now undertaking detailed options analysis to develop several packages of options that can be taken back to local water utilities, joint organisations and the community for further consultation before recommendations are made to government for final solutions for each region. These regions are expecting the next stage of consultation to be based on rigorous analysis of the options and feedback provided so far. Communities are impatient for government to get on with the work of planning and preparation before the next drought.

Effective stakeholder engagement is resource intensive and represents a significant component of the proposed costs. The idea the effective stakeholder engagement can be undertaken with fewer resources during years 1 and 2 appears to misunderstand and oversimplify the nature of the work involved.

The department is working to timeframes set by the NSW Government. This necessarily resulted in a rapid expansion and acceleration of the program to effectively cover the whole state, despite uncertainty of future funding availability to deliver the full program. A consequence of this is difficulty in retaining a steady and consistent team of staff, with a high reliance on temporary contracts. This is inefficient due to the time and cost of recruitment and training of staff and has consequential impacts on other programs. Proposed cuts to program funding over the regulatory period will continue this problem as the department responds to program needs without funding certainty for a major proportion of program costs.

Consistent feedback from the community is that it is frustrating when different departmental staff come out to talk with them every time due to staff turnover. Reducing costs in years 1 and 2 risks exacerbating this turnover and diminishing the effectiveness of stakeholder engagement.

If the 25% reductions are made, there is also a real likelihood that the resources required to continue and extend climate risk analysis, and putting the results of this into context for each region, will not address this pressing need. The climate results to date clearly demonstrate the challenge that climate change presents across the state for adaptation and response in water management arrangements. Delay or failure to address these issues in a well informed and timely way presents concerning risks to regional economies.

Delaying implementation of the regional water strategies also presents a risk to strategic, whole- of- catchment planning and may lead to inefficient investment in business case development, as well as less than optimal selection of and timing for infrastructure

investment. The proposed cost of strategy development is small in relation to the cost of investment in business cases and infrastructure.

We request that IPART reconsider the implementation risks resulting from Cardno's recommendations and adjust the final revenue requirement to reflect our price proposal. We question the relevance of Cardno's experience to make this recommendation and, if necessary, suggest that alternate advice from an appropriate expert may benefit IPART's processes.

### **IPART's reductions to water plan performance and assessment costs will lead to a drop in service levels and an inability to meet statutory requirements**

Most notably IPART's recommended adjustments will result in an inability to meet statutory requirements under the *Water Management Act 2000* (NSW) and *Commonwealth Water Act 2007*. In particular, reporting under s43 and s43A, also s10, s44 and s51 of the *Water Management Act* will be compromised. Further, we will not be able to adequately address recommendations from both the Natural Resources Commission (NRC) and the Independent Commission Against Corruption (ICAC) that NSW should commit more resources to water sharing plan monitoring programs and establish a dedicated unit. The NRC has raised issues about the adequacy of implementation in its recent water sharing plan reviews. This was also highlighted in audits of plans under s44 of the *Water Management Act 2000*.

### **We will not be able to undertake surface water and groundwater modelling to support key water security priorities**

We disagree with IPART's interpretation that our obligations for this activity are largely 'business as usual' and unchanged from the current determination period. We consider that our 2020 pricing submission to IPART clearly articulated the increased scope of modelling work. This is an incremental and material increase to what was reviewed for inclusion in the 2016 determination period. The additional work includes modelling to support several expanded Government priorities including floodplain harvesting, regional water strategies, and sustainable diversion limit adjustment mechanism (SDLAM) projects.

It is positive that WAMC's 2016 notional revenue requirements were cushioned due to arrangements for external funding of this increased activity and the avoidance of double counting. However, these funding agreements have expired. This means that there is now no alternate funding for these WAMC monopoly services. We request that IPART review the information included in our submissions relative to the 2016 determination scope of works when finalising the revenue requirement.

### **We disagree with IPART's draft finding that 25% of our proposed intergovernmental activities are outside the scope of WAMC**

We assert that there has been an error of methodology to exclude 25% of intergovernmental activities as not a monopoly service. We are concerned that the draft report has removed a component of our cross-border intergovernmental programs from the WAMC intergovernmental activity on the grounds that it contains a policy development component.

We acknowledge that there is a policy development component of this activity, but argue that this policy development directly supports delivery of WAMC activities and therefore is within the scope of WAMC.

We ask that IPART review this decision in the context of its current determination that 50% of the cost of this activity should be paid by users and 50% paid by Government. We believe

that by assigning a 50% share to Government, IPART has acknowledged the validity of efficient policy development costs being included in the Government share within the WAMC price determination.

### **We understand IPART's desire for efficient groundwater monitoring and critical needs water supply consent transaction charges**

We welcome IPART's recommendation to improve the cost reflectivity of fee-for-service consent transaction charges. However, while we are concerned that the recommended 20% decreases will impact groundwater assessment processing times, we accept that IPART has balanced cost reflectivity of charges with affordability considerations.

### **We consider that NRAR's proposed consent transaction costs were properly validated**

IPART's draft decision to reduce NRAR's consent transaction charges appears to be based on Cardno's final report, which states that 'given the lack of validation of the costs that drive the proposed charges and the relative immaturity of the business processes in both agencies to capture and record costs that reflect the activities, that a relatively large efficiency challenge of 20% should be applied to the charges proposed by the agencies to arrive at efficient costs'.

For the public record, NRAR considers that its water consent transaction costs included in its proposal were adequately validated. NRAR commissioned a reputable consultant to develop a detailed, bottom-up cost model that was then tested and normalised by a top-down assessment. NRAR provided this complete model to Cardno, together with background notes about how it was constructed.

### **In principle, we support the transparent and full cost recovery of the user share of MDBA and BRC costs**

In our response to IPART's Review of Water Management Prices from 1 July 2021 Issues Paper, we did not support implementing separate Murray–Darling Basin Authority (MDBA) and Border Rivers Commission (BRC) charges at this time. Rather, we thought changes to the pricing structure were best considered over the 2021 regulatory period to allow enough time to consider the interactions among all rural water management pricing components and the overall impact on customer bills and revenue.

We stand by this view. However, we are supportive of IPART's efforts to make MDBA and BRC costs more transparent to users and to set pass-through charges at full cost recovery.

### **We included business governance support costs for transparency and not in error**

We contest IPART and Cardno's assertion that we included our business support costs in error<sup>1</sup>. As explained to Cardno during the expenditure review, these costs were not duplicated in our forecasts. Rather, they were included in the activity costs for transparency reasons and to give stakeholders a line of sight of the amount of business governance support costs included in our proposed overheads. We request that IPART correct this assertion in the final report.

---

<sup>1</sup> Review of prices for the Water Administration Ministerial Corporation from 1 July 2021 to 30 June 2025, p33

## **The IPART draft determination makes recommendations that Government should fund compliance activities without explicitly including the costs in the efficient Government share**

While the department and NRAR welcome these recommendations, IPART should contemplate what occurs if the Government decides to not fund, or only partially fund, these activities. We respectfully suggest that IPART considers other funding scenarios in framing its final determination to ensure water users continue to receive the benefits of WAMC services.

## **Summary of concerns with IPART's methodology to determine draft prices**

IPART has applied in full the adjustments and efficiency reductions as recommended by its expenditure consultants, Cardno.

In our response to Cardno's expenditure review report, we raised several concerns with Cardno's review methodology and recommended adjustments. While Cardno and IPART accepted some of our arguments, we are concerned that IPART has applied all of Cardno's recommended adjustments without considering the fundamental flaws in Cardno's decision-making.

We accept that IPART had a limited amount of time in which to conduct a rigorous analysis in time for the release of the draft report and determination. We urge IPART in preparing its final determination to revisit several its draft decisions.

Specifically, we have concerns with IPART's application of:

- Cardno's use of benchmarking with Victoria to determine the efficient cost of compliance management. We raised a number of flaws in the benchmarking approach during the expenditure review and we are concerned that the benchmarking approach with these flaws has been adopted into IPART's draft recommendations. Fundamentally, we are concerned that Cardno did not complete an assessment as to whether Victoria is a suitable comparator in terms of its comparability to NSW across a range of criteria including differences in legislative and regulatory scope, the relative effectiveness and maturity of compliance activity and differences in landscapes, geographical expanse, irrigated agricultural spread and water industry structure. Rather, it seemed that Victoria has been selected as a comparator due to the ready availability of data. NRAR is happy to engage with IPART directly to provide more information on Cardno's benchmarking flaws and the development of a more robust benchmarking approach.
- Cardno's assumption that NSW metering implementation will result in significant compliance cost reductions (based on Victorian comparisons) and that the metering frameworks of Victoria and NSW are the same. IPART's draft decision that \$38.9 million of compliance costs over four years should be funded by Government is partly based on the current state of metered water take in NSW. This analysis suggests that NRAR's Government funded compliance costs are needed for a short term only and that this Government share will not be required after 2025 as NRAR matures and, most notably, NSW metering reform is completed. We understand that Victoria has almost universal telemetry, whereas the NSW metering policy at this stage



requires telemetry for less than 25% of metered sites by 2025. Unless this policy position changes in NSW before 2025, the extent of compliance efficiencies is likely to be far less than has IPART and its consultants have assumed. The current WAMC decision should not set expectations regarding long-term efficient compliance costs based on these metering assumptions. The costs of compliance should be assessed in 2025.

- Cardno's recommendation to reprofile our Regional Water Strategies program and remove 25% of costs in each of the first two years of the determination period. It is a matter of fact that Cardno's recommendation to reprofile regional water planning costs will only serve to delay the implementation of vital water planning measures without providing benefits to users or the community. It is alarming that IPART has accepted Cardno's recommendation to delay implementation of a Government election commitment, particularly without also giving due consideration to the operational risks of that recommendation. We suggest that IPART engage with us directly on this matter to ensure its recommendations do not result in perverse outcomes for water users and the broader community.
- Cardno's assertion that the level of surface water and groundwater modelling activities are unchanged from the 2016 determination period. It is apparent that Cardno did not fully investigate and compare the submitted current program of works with what was included in the 2016 WAMC price review. We suggest that IPART engage with us directly on this matter to make this comparison and re-evaluate its recommendation for the final report and determination.
- Cardno's assertion that our water planning and performance assessment are unchanged from the current determination period. Cardno made this assertion despite clear evidence that our monitoring, evaluation and reporting (MER) framework has expanded since 2016. We ask that IPART review the evidence of the increased workload that was provided to Cardno during the expenditure review period.

## Catch- up and continuing efficiencies

We agree with IPART that the WAMC revenue requirement and resulting water management charges should include efficiency gains over time to deliver the best value for money for users and the NSW taxpayer. However, as a matter of principle we believe that efficiency measures should be well targeted, represent achievable targets to incentivise meaningful action, and avoid compromising water management outcomes. We are concerned that IPART's methodology is not well targeted. We consider that the applied methodology favours the application of relatively small cuts across the board and with a large cumulative impact. It appears to prioritise generic efficiency targets over water management outcomes.

As detailed by IPART in its draft report and determination, both Cardno and IPART applied a three-step process to establish our efficient costs of water management services. We have specific concerns with each of the steps in the process to establish efficient costs that IPART and its consultant Cardno have applied, namely:

1. Reviewing proposed changes in our activities and costs and applying scope adjustments where it was considered that our proposed changes were inefficient. We note that IPART states that the scope adjustments do not apply to the utility's base

expenditure<sup>2</sup> despite applying top-down adjustments to our compliance, regional water planning and intergovernmental activities.

2. Reviewing business processes relative to a 'frontier' company and applying a catch-up efficiency adjustment where business processes could be improved. We note IPART did not include substantiating information of the department's or NRAR's comparable 'frontier' company in the draft report, nor did it provide examples of effective 'frontier' company business processes that we could adopt to deliver real savings rather than service shortfalls.
3. Reviewing available data on efficiency gains in well-performing utilities and broader productivity trends to replicate competitive market characteristics, applying a continuing efficiency to all our proposed activity costs, IPART uses long-run Australian Bureau of Statistics (ABS) multi-factor productivity (MFP) in the Australian Economy<sup>3</sup> to calculate the continuing efficiency adjustment. We note that headline MFP figures can be influenced by large gains in specific sectors, such as mining, that have little relevance to rural water management. The ABS states that 'care should be taken when interpreting year to year productivity growth for the market sector and by industry. Users are encouraged to continue viewing productivity growth through growth cycles'.<sup>4</sup>

Finally, given the department and NRAR made clear to IPART and Cardno that they had already made \$73.6 million in targeted efficiency savings to avoid costs over the 2021 determination period, we question the value of applying further untargeted and arbitrary cuts to our proposed costs.

---

<sup>2</sup> Review of prices for the Water Administration Ministerial Corporation from 1 July 2021 to 30 June 2025, p21

<sup>3</sup> Review of prices for the Water Administration Ministerial Corporation from 1 July 2021 to 30 June 2025, p31

<sup>4</sup> [www.abs.gov.au/articles/productivity-measurement-time-pandemic](https://www.abs.gov.au/articles/productivity-measurement-time-pandemic)