Lachlan
Valley
Water Inc

Submission to IPART

on Rural Water Charging System Review

by Lachlan Valley Water

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EXECUTIVE SUMMARY

1. LVW is opposed to State Water's charges being determined by ACCC when that process will not be implemented consistently across all states, and asks the NSW Government to withdraw NSW from the ACCC price determination process until all states have bulk water prices determined under the same rules.

2. LVW agrees that there is wide variation between valleys and across farming systems but believes that a consistent methodology is required across NSW to measuring the impact of low water availability.

3. LVW supports a continuation of the current cost shares for the 2014 Determination, and if a review of cost shares is required for the following 2018 Determination, we support IPART undertaking periodic reviews of methodology at every second determination period.

4. LVW considers that a sequence of low or zero water availability years is an appropriate measure to determine a threshold for impact on customers' cash flows. LVW proposes the trigger of 2 consecutive years of less than 5% new AWD, and believes this is administratively simple and easy to understand.

5. As a period of low water availability extends past 2 years LVW recommends that a drought policy to waive fixed charges is required. The policy position of the Coalition in NSW for the 2011 election was to waive the fixed charges when general security licences have 2 successive years of zero allocation. We ask that the NSW Government now implement this policy.

6. LVW agrees that trade can be a valuable tool, but for general security licence holders during prolonged drought when there is zero AWD, it does not assist viability.

7. LVW strongly supports the retention of the 40:60 ratio of fixed to variable charges.

8. However, we are aware that there may be some customers who would prefer the stability of a known and constant annual charge, and we ask that State Water provide information on 2 pricing options, one at the 40: 60 ratio of fixed to variable charges, and one with a higher fixed charge and lower usage charge, for customers' consideration.

9. State Water can reduce their revenue risk, particularly during times of low water availability, by identifying as customers all those users where the supply of water requires State Water to provide additional services such as maintaining accounts, operation of structures or consultation by State Water, and by recovering the cost of providing their services to those customers.

10. A further option for State Water to manage their own risk would be for State Water to maintain a reserve fund in which surplus funds could be retained to assist in periods of low water availability.

11. LVW supports a continuation of the current user and government cost shares for the 2014 Determination, and if a review of cost shares is required for the following 2018 Determination, we support IPART undertaking periodic reviews of the methodology at every second determination period.

SUBMISSION ON RURAL WATER CHARGING SYSTEM

1. Introduction

Lachlan Valley Water (LVW) is the peak valley-based organisation representing 650 surface water and groundwater irrigator members in the Lachlan Valley, including irrigators within Jemalong Irrigation Limited (JIL). This submission has been prepared on behalf of all members, however, members also reserve their right to make a separate submission.

We welcome the opportunity to provide input to this review of rural bulk water charging systems, but due to the very short time frame available for this review we have provided a response only on the most critical issues and questions from the IPART Discussion Paper.

2. Terms of Reference

1. Examine ways that the billing of bulk water charges might be better matched to business cash flows, for example:
   a. Varying the timing of water bills and payment terms in relation to farm cash flow
   b. Varying the ratio of fixed to variable charges
   c. Options for differential fixed charges (based on seasonal conditions)
   d. Options for different variable charges (eg, stepped or volume based)
   e. Use of modern telemetered meters

2. Potential methods of determining the Government cost share for ACCC determined bulk water charges in NSW, which may include a role for IPART.

3. The potential impacts to customers, State Water, and the NSW Office of Water of future pricing arrangements, and make recommendations that will assist the NSW Government to maintain viable and economically sustainable provision of services to customers.

3. Assessment Criteria

IPART has requested comment on whether the proposed assessment criteria are appropriate.

We agree that the assessment criteria are appropriate but want to make clear at the outset that we are opposed to State Water's charges being determined by ACCC when that process will not be implemented consistently across all states. We urge the NSW Government to withdraw NSW from the ACCC price determination process until all states have bulk water prices determined under the same rules.

LVW is a member of NSW Irrigators Council (NSWIC) and we support the NSWIC position on the determination of prices by ACCC.

4. Water Availability and Customers' Cash Flows

IPART has requested comment on the most appropriate methods of analysing historical water availability to understand the relationship between water availability and cash flows.

The variation between valleys is very wide, and availability is influenced by the water accounting system operated in each valley. In valleys that operate either continuous accounting or 100% carryover, general security licence holders have a greater flexibility to carry water from one year to the next and manage some of their own supply risk. LVW believes that in these circumstances the average end-of-year Available Water Determination (AWD) becomes less important.

However, we acknowledge that for valleys that operate with 50% carryover or less, average AWD is relevant and timing is very important.

In addition, we note that Water Sharing Plans (WSPs) for regulated rivers were gazetted in 2003/04, but due to drought many, including the Lachlan, were immediately suspended and not implemented until 2011. The WSPs imposed reductions in extraction limits, so that future availability may be slightly lower than the historical, pre-2003 water allocations.

IPART has asked whether the differences between valleys and associated farming systems mean that broad rules across valleys to measure the impact of water availability is not appropriate.

In view of our comments above and the information in the IPART Discussion Paper, in *Table 5.2, Average allocations by valley 1989/90 to 2008/09*, we concur that there is wide variation between valleys and farming systems but believe that a consistent approach across the state to measuring the impact of low water availability is required.

IPART has asked which customers are most affected by variability.

LVW concurs with IPART's view that general security users in regulated systems and unregulated are most affected. We consider that the impacts are likely to be more severe for general security users because at least part of the farm enterprise will be based on the availability of water.

IPART has asked whether there are circumstances where water availability affects high security users.

Table 1 below indicates that severe and prolonged drought will reduce water availability for high security customers. When availability falls to 30% or less the impact on high security customers is severe because they often have permanent plantings and high value enterprises based on a highly reliable source of water.

IPART has requested comment on what is an appropriate basis to determine a trigger level of water availability before there is a significant impact on customers' cash flows.

The Lachlan suffered severe drought from 2002 – 2010, as shown in Table 1 below, resulting in 6 years of zero water availability for general security users, and an average AWD of 2.75% over the 8 years from 2002 to 2010. High security users also suffered very low allocations in some years.

Our experience is that it was the sequence of low water availability years that cut farm cash flows. By the end of the second year of low or zero AWDs growers' reserves of water and cash were run down and their ability to manage their own risk was depleted.

We acknowledge that most irrigation businesses in the Lachlan valley are mixed farms, with some dryland as well as irrigation, so are not as highly dependent on irrigation as in some other valleys where the impact may bite earlier.

Table 1. Lachlan Allocation History

Year	High Security (%)			General Security (%)
	TWS	S&D	HS	
1989/90	100	100	100	120
1990/91	100	100	100	120
1991/92	100	100	100	120
1992/93	100	100	100	120
1993/94	100	100	100	120
1994/95	100	100	100	80
1995/96	100	100	100	100
1996/97	100	100	100	100
1997/98	100	100	100	65
1998/99	100	100	100	100
1999/2000	100	100	100	74
2000/01	100	100	100	84
2001/02	100	100	100	58
2002/03	100	100	100	3
2003/04	70	70	70	0
2004/05	50	30	30	0
2005/06	100	100	100	19
2006/07	80	80	80	0
2007/08	70	50	30	0
2008/09	70	50	30	0
2009/10	50	15	10	0

Source: NSW Office of Water

As noted above, LVW considers that a sequence of low or zero water availability years is an appropriate measure to determine a threshold for impact on customers' cash flows. The IPART discussion paper mentioned two alternatives for a trigger – either by reference to zero allocations, or by reference to the extraction (or AWD) being within the lowest 5% of modelled extraction (or AWDs) for that valley, ie, a 1 in 20 year occurrence.

At the Sydney hearing LVW advocated a trigger level of 2 successive years of less than 5% new AWD. We recommend that any such measure should refer to "low or zero" availability because from a practical point of view a 3% AWD is the same as zero in terms of earning income from a farming enterprise.

LVW proposes the trigger of 2 consecutive years of less than 5% new AWD because it is administratively simple and easy to understand.

However, we accept that a trigger of the actual extractions (or AWD) in consecutive years being within the lowest 5% of modelled extractions (or AWDs) for that valley is likely to be a more equitable approach across the whole state because it allows for the relative reliability in different valleys.

LVW would also like to emphasise that as the years of low water availability continue the cash flow deteriorates very quickly, and recommend that prolonged low water availability requires a drought policy response which is more than simply deferral of charges. We see that the initial trigger would allow access to deferral of charges or strengthened hardship provisions, but continued low availability of water should lead to waiving of fixed charges.

IPART has requested comment on the degree to which trading has allowed customers to maintain the viability of their business and maintain cash flow in times of drought.

There is no doubt that trading is a valuable tool, and enabled some farmers to cover their fixed water charges during the drought. In the Lachlan we saw prices for temporary transfer water rise to $400 - $600/ML during 2008/09 and '09/10. However, the IPART discussion paper indicates that the gross value of sales was only $1 million in 2008/09 and $800,000 in 2009/10, so clearly the volumes traded were very low. Total usage in those years was 23 GL in '08/09 and 9 GL in '09/10. Total entitlement on the Lachlan is around 650 GL.

However trade is not an option for those licences which have zero AWD, so for general security licence holders during severe and prolonged drought, where the need is high, trading does not assist viability.

5. Tariff Structures and Policy Options to Address Customer Cash Flow

IPART has requested comment on the key issues in the current suite of price tariffs, pricing policies and payment terms that cause hardship in periods of low water availability.

One of the key issues is that prices and tariffs must be consistent with the National Water Initiative (NWI) pricing principles, that is, they must represent efficient costs and the user pays principle.

Fixed and Variable cost ratios

The 40:60 ratio of fixed to variable charges is preferred by many customers because it aligns far better with customer cash flows and capacity to pay, because when irrigators have water they can earn income and pay their charges. It is also seen by customers as encouraging efficient operation in a monopoly situation, as opposed to a higher proportion of fixed charges.

LVW strongly supports the retention of the 40:60 ratio of fixed to variable charges.

However, we are aware that there may be some customers who would prefer the stability of a known and consistent annual charge, and for that reason we ask that State Water provide information on 2 pricing options, one at the 40: 60 ratio of fixed to variable, and one with a higher fixed charge and lower usage charge, for customers' consideration.

We understand that the costs and benefits to State Water for each option would be priced into the options. If alternative pricing options were to be considered we suggest that each individual irrigator should have the option at the start of a pricing cycle to choose their preferred option, and would have to stay with that option for the whole pricing year cycle. The irrigator would also need to maintain all licences on the same option.

IPART has asked for our views on the tariff structure options presented, and whether we agree with IPART's preliminary view.

LVW supports a deferral of charges as a risk management option that should be open to users, but recommends that if deferred, the charges then do not become payable until there is a minimum of 20% new AWD, to allow the customer some ability to earn income to pay the charges. We recommend that individual customers should be able to choose whether or not to exercise this option, and note that their choice will probably depend on the relative interest rates of State Water and their main lender.

IPART has asked whether there are any other tariff structure or policy options that should be considered.

<u>User pays</u>
State Water could increase their ability to manage their own revenue risk, particularly during times of low water availability, by identifying as customers all those users where the supply of water requires State Water to provide additional services such as maintaining accounts, operation of structures or consultation by State Water, and recovering the cost of providing the services to those customers. This would include Basic Landholder Rights and discretionary environmental water under Water Sharing Plans, eg, Environmental Contingency Allowances.

We welcome the statement by IPART at the Sydney hearing that NSW Office of Water have been asked to consider a policy framework that will address this issue at the 2014 price determination. We recommend that State Water be encouraged to do the same in their next submission.

<u>Reserve Fund for State Water</u>
LVW believes that the proposals for an enhanced hardship policy or deferral of charges do not negate the requirement for State Water to manage their own risk, and that one option for this would be for State Water to maintain a reserve fund in which surplus funds could be retained to smooth revenue in periods of low water availability.

Should NSW Government policy prevent State Water from implementing this standard risk management strategy, we do not believe that customers should pay, by means of a volatility or higher Weighted Average Cost of capital, for the higher risk profile of State Water.

Drought Policy

As noted in (4) above, after more than 2 consecutive years of zero water, irrigation enterprises have generally exhausted their own risk management reserves, and deferral of charges does not offer significant assistance. LVW believes that at this stage a drought policy to waive fixed charges is required.

The election policy position of the Coalition in NSW for the 2011 election was to waive the fixed charges when general security licences have 2 successive years of zero allocation. We ask that the NSW Government now implement this policy.

6. Cost Shares

IPART has requested comment on the cost share options presented, and whether there are any alternative options.

LVW agrees that the current cost sharing ratios have been reviewed intensively in previous determinations by IPART and that they represent a transparent and clearly explained methodology.

We believe it is important to continue a transparent process for determining user and Government cost shares and that the process provides a degree of consistency in application for all parties. We also note IPART's comment that it has made few changes to the cost shares over recent determinations, and therefore from the point of view of administrative efficiency we do not believe it is necessary to review cost shares at every determination.

LVW supports a continuation of the current cost shares for the 2014 Determination, and if a review of cost shares is required for the following 2018 Determination, we support IPART undertaking periodic reviews of methodology at every second determination period.