Gwydir Valley Irrigators Association Inc.

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Gwydir Valley Irrigators Associations submission to

Review of Bulk Water Charges for State Water Corporation – Draft Determination

Independent Pricing and Regulatory Tribunal

April, 2010

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Executive Summary

GVIA is frustrated and angered at IPART's Draft Determination for State Water's Bulk Water Charges.

GVIA believes the proposed 85% real increase in high security charges and 35% real increase in general security charges in not only in excess of what State Water requested, but will put into jeopardy the financial viability of Gwydir Valley irrigators.

GVIA has identified eight major areas of concern with the draft Determination.

The Consumption Forecasting Model: GVIA strongly argues that IPART has not provided any evidence that justifies either the adoption of the 20-year rolling average or the 15-year rolling average consumption model, and provides significant evidence for the retention of the Long Run Average IQQM forecast tool.

GVIA argues that even the State Water purchased CIE report specifically rules out a structural break in the Gwydir.

The Volatility Allowance: GVIA argues that the proposed volatility allowance is both unfair and unnecessary, and that IPART's justification for is based on a very flawed selective quoting of the National Water Initiative. GVIA proposes that the solution to the issue of revenue volatility is an adjustment of State Water's dividend requirements so it is better able to manage its own cash flow.

The Weighted Average Cost of Capital: GVIA has called questioned the overall justification of the application of a WACC, and has also strongly argued that the WACC, if one must be applied, be set at the lower end of the range, and that the application of a WACC premium as a way of retaining State Water's BBB credit rating be totally rejected.

The High Security/General Security Ratio: GVIA has expressed its extreme disappointment that IPART has ignored its very constructive suggestions for a high security/general security charging ration based on actually costs, and has instead chosen to recommend a "scarcity" based system.

GVIA has clearly demonstrated why a "scarcity" based system is totally inappropriate for State Water charging, as well as asserting if the proposed pricing structure was adopted it would potentially be ruinous for high security irrigators.

GVIA has re-submitted its proposal for a cost-based approach.

Price Paths: GVIA has expressed its concern for the proposed "Glide-Path" to price setting, highlighting that the approach leads to inflated pricing at the end of the Determination period, and this is likely to result in an inflated starting point for the next pricing period.

GVIA has requested that IPART, in consultation with GVIA consider this matter further.

Fish Passage Works when Triggered by Dams Safety Upgrades: GVIA has called on IPART to reverse its Draft Recommendation on Fish Passage Works Trigged by Dam Safety Upgrades, and argues that these costs should be a 100% Government cost.

GVIA strongly argues the works are only required because they weren't installed when the dam was built, and therefore should be viewed as a legacy cost.

Further, under the impactor pays principle, the impactor is not those that receive benefit from the dam, but the government that has ordered the safety upgrade, that in turn triggers the requirement for fish passage works.

The Murray-Darling Basin Authority Costs: GVIA argues that the Gwydir should be exempt from State Water MDBA costs as State Water carries out no operational tasks in the valley that impact on the role of the MDBA.

Further, it argues that if a share of these costs must be applied to the Gwydir, they should be proportional to the Gwydir's flow contribution to the wider Murray-Darling system.

Bill Impacts: GVIA is highly critical of IPART's economic analysis of the impact of the price increases on the viability of Gwydir Valley irrigation businesses.

It argues IPART is flawed in it overall approach, and failed to meet its statutory obligations by not specifically analysing the impacts in the Gwydir.

GVIA also expresses its view that it is entirely inequitable that IPART should offer an annualised Cap on price increases to some valleys but not to others.

GVIA has identified 10 recommendations which appear on the next page.

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GVIA Recommendations

Recommendation 1: On receipt of this submission IPART immediately arrange to meet directly with the GVIA executive, with a the genuine view to modifying its Draft Determination so as to greatly reduce the financial impact on Gwydir irrigators.

Recommendation 2: That the Long Run Average Integrated Quantity and Quality Model remains the forecasting tool for consumption estimates in the Gwydir Valley.

Recommendation 3: That IPART remove the volatility allowance from its Draft Determination, and that it ignores the impact of State Water's dividend policy when setting bulk water charges.

Recommendation 4: That IPART use its considerable discretion to set the WACC at 6.3%, the lower end of the range, and there must be recognition that State Water/NSW Government should not pursue its BBB credit rating at the expense of the irrigators of the Gwydir Valley.

Recommendation 5: IPART should adopt the High Security/General Security charging model proposed by GVIA in this submission (or a similar model based on actual costs and the percentage of water made available to each class on average).

Recommendation 6: That IPART enters into further negotiation with GVIA on the relative merits of the "Glide Path" approach, compared with the setting of prices to achieve revenue recovery for each year of the Determination. Matters to be discussed include pricing start point for the first Determination post 2013/14, and pricing discounts that could be applied to the "full recovery" model.

Recommendation 7: That IPART reverse its draft Determination decision on cost shares where fish passage works are triggered by pre-1997 Dam Safety Upgrade works, and that the associated costs be deemed to be 100% Government costs.

Recommendation 8: That IPART remove the MDBA cost allocation from the Gwydir, and if a cost allocation must remain, it is proportional, based on inflows from the tributary streams into the main streams of the Darling and Murray Rivers.

Recommendation 9: That IPART immediately commission a full and independent study of the financial impact of the proposed prices on the financial viability of Gwydir irrigators, and that it amends its prices to a level that is financial sustainable for Gwydir irrigators.

Recommendation 10: That IPART offer a maximum cap on price increases to all valleys covered by the Determination.

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Introduction:

The Gwydir Valley Irrigators Association (GVIA) represents in excess of 200 irrigators in the Gwydir Valley of NSW, centred on the town of Moree.

The organisation is voluntary, funded by a cents/ megalitre levy on regulated unregulated and groundwater irrigation entitlement. In 2008/09 the levy was paid on in excess of 93% of the entitlement.

The Association is managed by a committee of 11 irrigators and employs a full-time executive officer, a full time irrigation extension officer and a part-time administrative assistant.

All members of the GVIA are customers of State Water, and a number of GVIA members sit on State Water's Gwydir Customer Service Committee.

GVIA is a member of the NSW Irrigators Council, and as well as providing this submission, the Association fully endorses the submission made by NSW Irrigators Council.

While GVIA welcomes the opportunity to provide feedback on IPART's draft determination, GVIA must express its frustration and anger at the way IPART has effectively failed to heed the arguments put forward by GVIA and other irrigation organisation during the Determination process to date.
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General Comments:

GVIA needs to express its extreme frustration and anger at IPART's Draft Determination for State Water's Bulk Water Charges. IPART has recommended charges in excess of those sought by State Water.

For high security irrigators State Water asked for increases of 72%, and IPART seeks to deliver increases of 85%. For general security irrigators State Water asked for 33% and IPART seeks to deliver 35%.

GVIA is used to the nature of the claims State Water has historically made to IPART Determinations, and has had an expectation that IPART is capable of recognising the ambit nature of these claims, and will fairly play its role as an independent adjudicator. This expectation has been shattered by the Draft Determination.

Furthermore, GVIA very strongly believes that the Draft Determination, which in effect seeks to make State Water a near-to-zero risk business, demonstrates a complete disconnect between the financial needs of State Water and the financial needs of its customers. GVIA is stunned that IPART could endorse a triple-headed approach of risk elimination – changes to consumption forecasts, increased WACC and the introduction of a volatility allowance.

The Draft Determination has fortified the monopoly position that State Water enjoys, at the very time when its customers are suffering huge financial impacts as the result of the on-going drought.

GVIA cannot fathom how IPART can determine that the massive price increases it is proposing will have no material impact on the profitability of farm businesses.

GVIA challenges IPART to provide examples of commercial businesses that have successfully increased their charges in real terms at more than 20% per annum for extended periods of time.

The reality is that commercial business must remain competitive, and while modest prices rises may play a role, there needs to be, and is, a constant drive for efficiencies which often keep price increases at levels below CPI.

Commercial business also know and accept that the financial health of their businesses are tied directly to the financial health of their customers, and that profit margins cannot be maintained when their customers are facing financial hardship, conversely, both business and customers recognised that there is opportunity for increased profit margins when customers are doing well.

After 8 years of drought many of State Waters' Gwydir Valley customers are at a financial tipping point that is simply not reflected in IPART's flimsy analysis of the impact of increased charges. General Security irrigators in the Gwydir Valley have now entered their third year of zero increments.

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The table below shows increments over the past 8 years.

Table 1: Annual History for the Past 8 Years

Year	Percentage (%)	Volume (Gl)
2002/03	0	0
2003/04	30.72	156.65
2004/05	4.6	15.2
2005/06	21.86	111.63
2006/07	0	0
2007/08	24.27	123.56
2008/09	0	0
2009/10	0	0
Average	10.18	50.88

GVIA is not an alarmist organisation by nature, and it and its members accept the need to pay reasonable charges to State Water in all but the most crippling water supply restrictions.

However, GVIA strongly believes that if the prices as proposed are implemented it will be a very real case of the NSW Government seeking a short-term dividend gain while putting at peril the viability of Gwydir Valley irrigators and the communities they support.

GVIA has numerous concerns with the Draft Determination and will highlight them through-out this submission. Principle concerns include:

1. The Consumption Forecasting Model
2. The Volatility Allowance
3. The Weighted Average Cost of Capital
4. The High Security/General Security Ratio
5. Price Paths
6. Fish Passage Works when Triggered by Dams Safety Upgrades
7. The Murray-Darling Basin Authority Costs
8. Bill Impacts

While GVIA will demonstrate through this submission the absolute folly of the Draft Determination, it also calls on the Tribunal to meet directly with GVIA and it members, with the view to significantly modifying its Draft Determination so the financial impost on Gwydir irrigators is greatly reduced.

Further, GVIA reserves the right to take additional action to protect its members from the crippling impact of State Water charges, particularly during this on-going drought.

Recommendation 1: On receipt of this submission IPART immediately arrange to meet directly with the GVIA executive, with a the genuine view to modifying its Draft Determination so as to greatly reduce the financial impact on Gwydir irrigators.

Consumption Forecasting Model

State Water's decision to purchase an alternative consumption forecasting model from the Centre for International Economics (CIE) smacks of a child changing the rules of backyard cricket simply because he wasn't getting the results he wanted. And IPART's decision to support in principle that change is like mum (the umpire) agreeing to the change because he is the favoured child.

The decisions totally ignores the fact that any change from the tried and true rules, aimed at favouring one participant, will always have negative impacts on all the rest of the players.

IPART's approach in the Draft Determination simply further highlights the ridiculousness of making ill considered changes to tried and tested rules.

While IPART may have had good intentions in proposing a 20-year rolling average rather than the 15-year proposal purchased by State Water, it has a massive negative impact on Gwydir irrigators, and has just further demonstrated that any attempt to move away from the Long Run Average Integrated Quantity and Quality model (IQQM) is just an attempt to play with figures.

Table 2 outlines the impact of the various models on Gwydir Valley's consumption forecasts.

Model	Volume (Ml)	% Change from IQQM
IQQM	309,164	
State Water – 15 yrs	275,597	-10.9%
IPART – 20 yrs	247,734	-19.9%

GVIA strongly argues that neither State Water nor IPART have put up any substantial arguments that in any way justify moving away from the use of the IQQM in the Gwydir Valley.

GVIA acknowledges that over the last Determination Period State Water did not make its predicted level of deliveries, and in fact if any of the above consumption forecast models had been used, it still would not have made the predicted level of deliveries.

This simply demonstrates what is known to all irrigators who operate in the Gwydir Valley - water availability is highly volatile. The problem for State Water, largely driven by the short-term dividend demands of the NSW Government, is that its business planning cycle focus is far too short.

There is no evidence to date to suggest that there has been any long-term decline in water availability in the Gwydir Valley, and as the graph on the following page clearly demonstrates there have been many periods of similar low availability over the past 119 years.

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Chart 1 – Modelled Water Availability in the Gwydir Valley

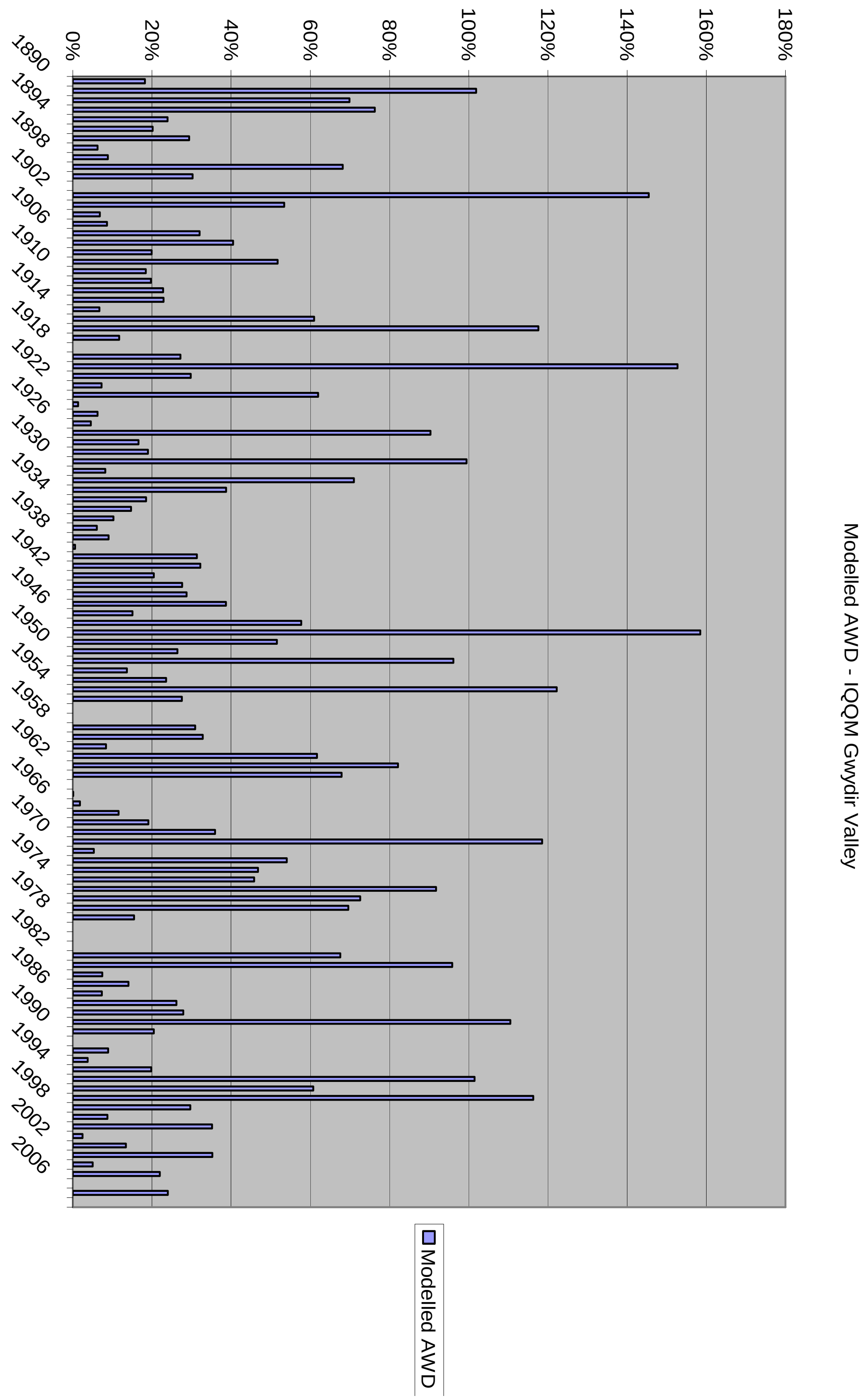
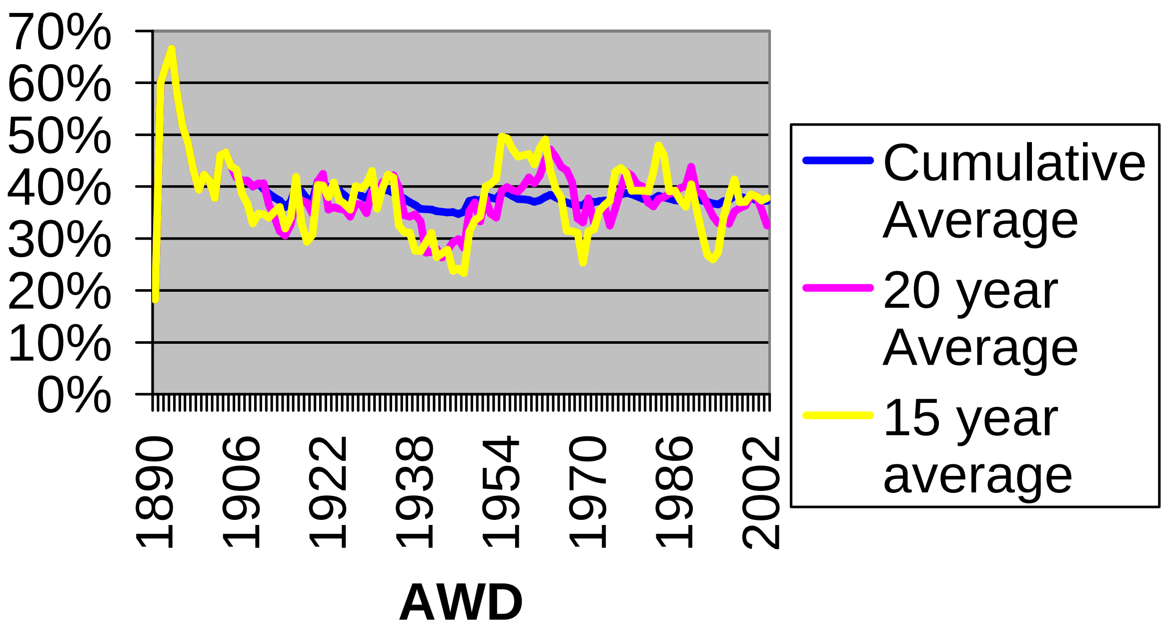


Chart 2 models the AWD, and how the average varies when either the rolling 15-year or the rolling 20-year average is applied.

Chart 2 - Average AWD Modelled by IQQM



This chart clearly demonstrates that there is no long-term advantage in either of the two proposed models, as over the long-term the result would be the same as retaining the Long Rum IQQM.

However, the Chart equally demonstrates the unfair consequences to both irrigators and State Water of using either of the two proposed models.

To put it very simply, neither of the proposed models has any credibility for forecasting future availability, and therefore are very poor at setting valid consumption forecasts. The consequences are severe.

For example, if IPART was attempting to set prices in 1992 using the 15-year average, it would have set forecasts considerable lower than the long-run average AWD, yet we can see that in the following four years there was in fact a major improvement in water availability, and State Water would have significantly over-recovered, not just through increased deliveries, but through an inflated price, pumped up by the low forecast.

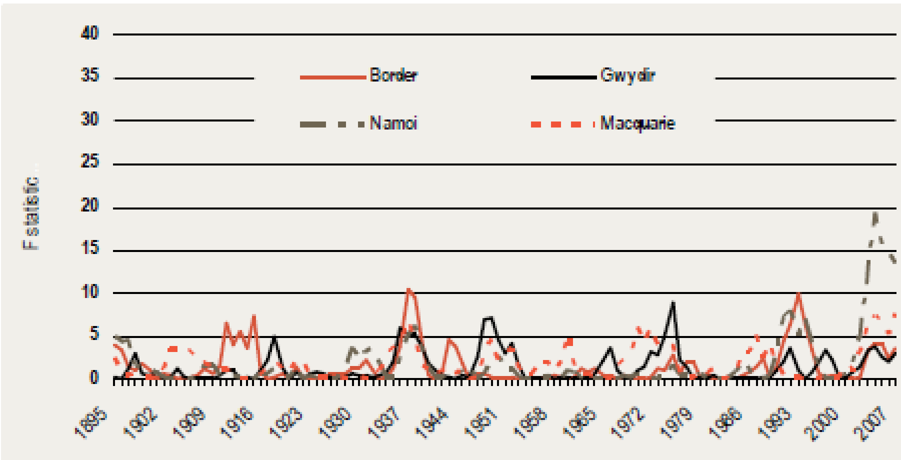
Similarly, State Water would risk significant under-recovery if a Determination had been made in 1983.

The argument proposed by State Water in its purchased report was that a statistically relevant structural break had occurred in the current decade.

GVIA offers no comment as to the veracity of this conclusion for other NSW Valleys, but points to the report's ***Chart 4.8 Structural Change in Northern and Central River Valleys*** to prove that even CIE could not demonstrate any structural shift in the Gwydir Valley.

Chart 2 – Structural Change in northern and central valleys (CIE)

4.8 **Structural change in northern and central river valleys**

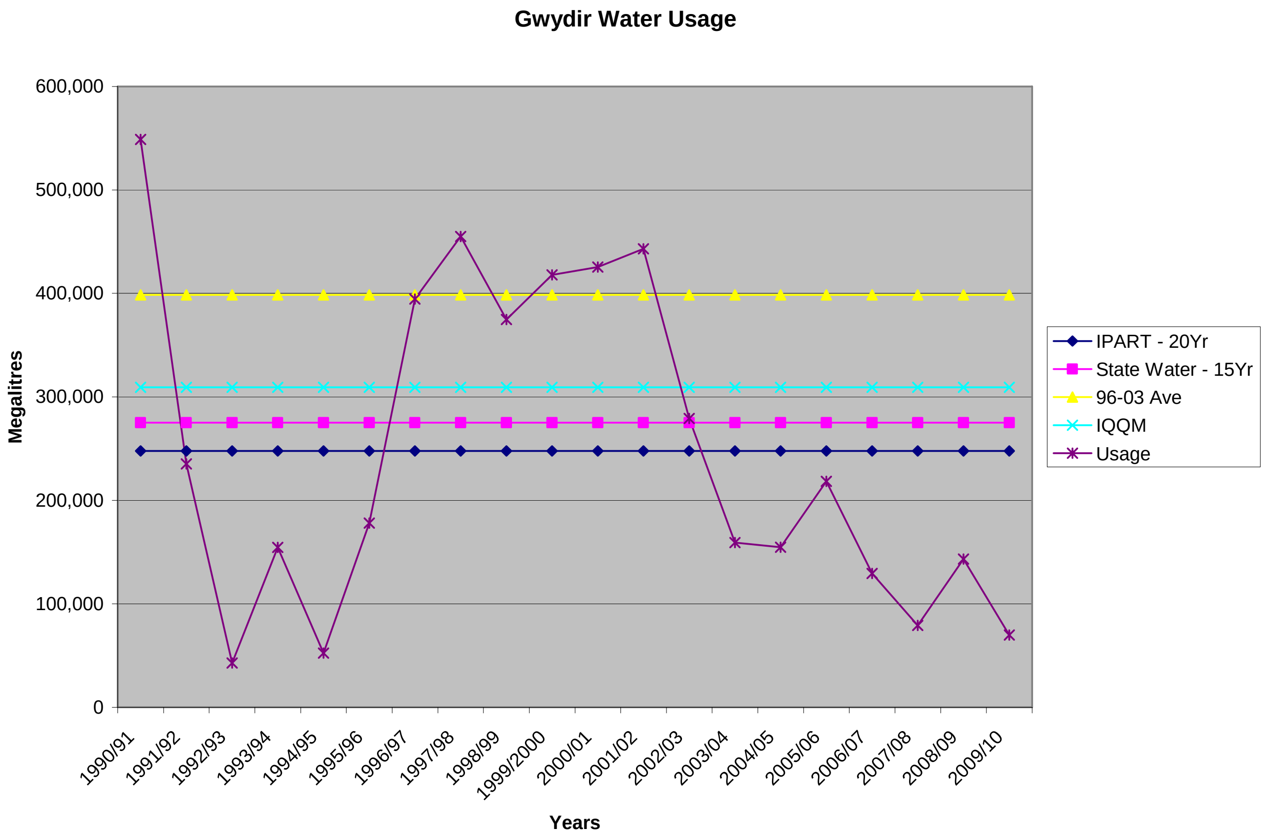


[a] The year is the beginning year for the five year period. The regression is for the period 1896 to 2009.
Data source: The CIE.

This chart clearly shows that there is no evidence of any unusual structural change in the Gwydir Valley, and demolishes the State Water/CIE argument for the adoption of the 15-year rolling average in the Gwydir Valley.

The following graph, showing actual extractions in the Gwydir Valley further demonstrates that while volatility is a feature of the Gwydir Regulated Water Source, there is no evidence of long-term decline.

Chart 3 – Gwydir Valley Water Use



This chart clearly demonstrates the volatility experienced in the Gwydir, but also shows that if there was justification for a low forecast based on recent year's extractions, there should have also been a very high forecast for the period 1996 – 2003.

The Case for Retaining the Long Run Average Integrated Quantity and Quality Model (IQQM):

1. IQQM is the primary water management and policy tool for NSW. It forms the basis of the Gwydir Regulated River Water Sharing Plan (It seems almost incredulous that the NSW Office of Water would jointly fund CIE to develop an alternative model for a specific revenue raising purposes, while they furiously defend the veracity of the IQQM.
2. It is the most robustly constructed and tested water availability model for the Gwydir Valley.
3. It fairly accounts for volatility, while providing long-term certainty.
4. It matches water availability with the natural business cycles of those that depend on water – be they irrigators or State Water.
5. There has been no evidence presented to show any structural decline in long-term water availability has predicted by the IQQM.

The Case Against both the 15-Year Rolling Average and the 20-Year Rolling Average:

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1. The CIE report not only fails to provide any evidence of a significant structural change in the Gwydir Valley, it actually clearly demonstrates that there has been no structural change.
2. The assertion that climate change will lead to lower water availability in the Gwydir Valley during the next four years is completely without supporting evidence. CIE structural change analysis shows no evidence and CIE admits itself in regards to climate change “It is too early to draw inference from data in these areas” (CIE, p50).

   In terms of the most comprehensive study into the likely effect of climate change the CSIRO concluded in its $50 million Sustainable Yield Project that by 2030 water availability in the Gwydir may increase by 34% or decrease by 29% (CSIRO, p39). Even if CSIRO’s best estimate is accepted of a 9% decline in General Security water use, this is a lower figure than what is proposed by both the State Water and IPART models. And it must be remembered that CSIRO is only predicting that degree of decline by 2030, and not for the period of 2010 to 2014.

   In proposing a 19.9% reduction over the Determination period IPART seriously runs the risk of becoming a climate change “laughing stock”, which has done nothing more that played with a series of numbers to artificially manipulate State Water’s journey towards becoming a zero risk business.

   In summary, both the State Water and IPART’s proposed models are without any underlining foundation, neither CSIRO climate change evidence or the statistical analysis purchased by CIE provide justification for a change in the consumption forecast model.

   There is also no evidence presented that a figure derived from the average of the past 15 or 20 years has any value in predicting consumption over the next four years.

   In fact both the Modelled AWD graph and the past 20 years Usage Graph provided earlier in this submission clearly shows that in the Gwydir the high degree of volatility can mean extremely rapid changes in availability.

   As the recent rains in Queensland and Far Western NSW have demonstrated very clearly, a turn around from an extended period of low water availability to an extended period of high availability is only one rainfall away.

   Recommendation 2: That the Long Run Average Integrated Quantity and Quality Model remains the forecasting tool for consumption estimates in the Gwydir Valley.

The Volatility Allowance

As GVIA has previously acknowledged in the submission water availability/consumption in the Gwydir Valley is highly volatile.

And while GVIA can understand in broad terms the arguments made by IPART in its Draft Determination in regards to the volatility allowance, GVIA contends these arguments are fundamentally flawed.

Firstly, IPART has underpinned it decision to propose a volatility allowance on a completely spurious quoting of the National Water Initiative.

"There are costs associated with revenue volatility, as shortfall resulting from revenue volatility may occur before windfalls leaving State Water to carry revenue shortfalls from years to year. Under principles of the National Water Initiative these shortfalls are to be recovered from the water access entitlement holders. The National Water Initiative states that:

Water access entitlement holders are to bear the risk of any reduction or less reliable allocation…arising from reductions to the consumptive pool as a result of seasonal or long-term changes in climate; and ….drought. " (IPART, p45).

IPART has selectively quoted from a part of the NWI which specifically deals with the assignment of risk should future governments introduce changes to water allocations or entitlements, and has nothing to do at all with costs associated with the delivery of water.

For government body such as IPART to deliberately quote such a passage out of context calls into question the integrity of the IPART process.

Further more, the NWI, provides no support for the introduction of the proposed volatility allowance.

IPART's proposal is even more offensive because it assumes that prior to over-recovering, State Water will under recover.

GVIA can only conclude that this startling assumption is based on State Water's recent performance. However, it has been clearly demonstrated in the above section on Consumption Forecast, that there is an equal likelihood in the Gwydir Valley of State Water over-recovering during the next determination period as under-recovering.

IPART has fallen into the somewhat understandable trap of thinking just because we have had a few tough years, next year will also be tough. But as the graphs have demonstrated the Gwydir has a very significant record of rapid reversals from drought like conditions.

While four-year Determination are practical, both State Water and IPART must accept that four-years does not in any way represent the natural cycles of the water delivery business in the Gwydir, and the expectation that revenue results will match revenue expectations during any four year period is entirely unreasonable.

The challenge for State Water is for it to be given the freedom as a business to manage its own revenue volatility.

Surpluses from over-recovery need to be invested within the business, to help fund the business during periods of under-recovery.

A significant road-block to this occurring is that State Water's shareholder, the NSW Government, demands a 70% return of profits in the form of a dividend.

While this may be a reasonable demand for a business with a high degree of revenue stability, it is not a reasonable demand for a business with highly volatile revenue.

State Water should be able to retain a significant proportion of over-recovered funds, so it can manage its periods of under-recovery.

Under its Act IPART must take into consideration the appropriate payment of dividends to Government. It is clearly inappropriate for government to seek a 70% dividend return at the expense of managing its revenue volatility.

Should the NSW Government refuse to amend it dividend policy, then it must be responsible for bearing the costs. The NSW Government is in a much better position to manage State Water's revenue volatility than the irrigators of the Gwydir Valley.

Irrigators must manage their own revenue volatility and certainly do not have the luxury of being able to pass on that perceived cost by applying a volatility allowance to their customers. They manage it by ensuring the retention of enough equity in their business so as to the fund revenue shortfalls during droughts.

Recommendation 3: That IPART remove the volatility allowance from its Draft Determination, and that it ignores the impact of State Water's dividend policy when setting bulk water charges.

The Weighted Average Cost of Capital

GVIA has a major issue with Government expecting to generate an immediate cash return from the provision of infrastructure assets.

Government is completely inconsistent in its application of return expectations from the provision of assets.

For example, public transport systems and road networks are all provided for by government, with no expectation of directly recovering operating costs, let alone a return on the capital contribution.

However, when it comes to some assets, most notably water and electricity, government seeks to generate a return.

GVIA concedes that it is outside IPART's role to do away with the requirement to provide some return, but it is well within IPART's role to ensure that the WACC is not increased.

GVIA notes that the Draft Determination identifies a WACC range 6.3% to 8.6%, and that IPART have conveniently settled on the mid-point WACC of 7.4%.

GVIA does not have the technical skills to enter into the argument about the justification of a particular WACC. However, GVIA is very suspicious when a proposed WACC falls right on the mid-point range, which suggests the setting of an appropriate WACC is not as an objective process as it first appears, and indeed must contain a significant objective element.

GVIA would strongly suggest the Government Bond Rate of 4.6% would be the most appropriate guide for the setting of State Water WACC as it effectively represents the "risk-free" rate.

State Water as a monopoly business should not expect a return above the rate that Government borrows from the private sector.

However, GVIA understands given the draft Determination IPART is unlikely to move away from the range it has identified, and therefore GVIA calls on IPART to set the WACC no higher the 6.3%.

GVIA is also very concerned about parts of the arguments used by IPART to justify the increased WACC. GVIA notes that IPART has highlighted the retention of BBB credit rating for State Water is an objective of the NSW Government.

GVIA also notes that IPART has identified a number of options for maintaining that credit rating – of which an additional WACC premium is one of them.

IPART correctly identifies that a change in State Water's dividend policy would also allow for the retention of the BBB policy.

It appears from GVIA's limited understanding of these issues that State Water and the NSW Government has deliberately structured its business to put pressure on its credit rating, and would like to rely solely on an inflated WACC to maintain it.

GVIA asserts that a higher than necessary WACC is putting great pressure on the financial sustainability of Gwydir irrigators, and the NSW government's head long pursuit to generate short-term revenue streams will completely backfire if the very real possibility of the collapse of the Gwydir irrigation industry eventuates. This will not only impact on the financial security of irrigators and their families, but also on the communities they are part of and support financially. The NSW government will be swapping a small short-term revenue gain for a massive decrease in economic activity and a corresponding increase in welfare safety-net payments.

Recommendation 4: That IPART use its considerable discretion to set the WACC at 6.3%, the lower end of the range, and there must be recognition that State Water/NSW Government should not pursue its BBB credit rating at the expense of the irrigators of the Gwydir Valley.

The High Security/General Security Ratio

GVIA is extremely disappointed that IPART appears to have completely ignored GVIA's very constructive input in our previous submission on how to fairly develop a High Security/General Security pricing structure, and instead has proposed a structure that would have ruinous consequences.

The IPART proposal would see fixed High Security prices rise by over 148% in real terms over four years, and GVIA notes that this increase would be even more if IPART did not apply a "glide path" pricing approach, as the proposed ratio of 5.27 is not achieved by the final year of the Determination.

GVIA is adamant that it is entirely inappropriate for any form of scarcity model to be used in developing State Water charges.

Scarcity pricing is only appropriate when it is used as a legitimate tool to control use. Use in the irrigation industry is already controlled through the development and application of the rigorous entitlement and allocation system, including water sharing plans.

Even if water was free, its use would be restricted due to the allocation system.

Scarcity pricing might be appropriate when applied to the sale of a good like water, but State Water is not in the business of selling water, it is in the business of capturing, storing and delivering water, and scarcity pricing should play no role.

State Water's claims that the current arrangements do not reflect the costs and benefits associated with high security. It is legitimate for State Water to ensure the costs are fairly reflected in High Security/General Security charges, but the benefits are reflected entirely in the cost of entitlements and therefore should remain outside the realm of State Water charging.

GVIA is well aware that the proposed pricing structure is revenue neutral to State Water, and that any reduction in High Security charges will be borne by increases in general security charges. However, GVIA and its members are committed to fostering a viable irrigation industry in our valley for all irrigators and are therefore committed to the implementation of a fair and equitable system.

For convenience GVIA has reproduced below the relevant section of its previous submission to IPART on this matter.

GVIA supports differential pricing between high security customers and general security customers, but has not been comfortable with the model previously used by State Water and IPART to determine a high security premium (based on Water Sharing Plan Conversion factors), and completely rejects State Water's proposed "scarcity" model.

GVIA proposes a more appropriate model would be based on high security charges recouping the costs associated with delivering high security water; and therefore it has looked at total valley revenue requirements, and divided them by the average High Security use.

It should be noted High Security includes all high security classes, including Urban Water Supplies, Domestic and Stock and High Security agriculture.

In making this comparison GVIA has used the same base numbers as used in the State Water submission including:

Total High Security entitlement – 21,458 megalitres
Total Gwydir Forecasted Consumption (15-year rolling average) – 275,597
Total Gwydir Forecasted Consumption (IQQM) – 309,164
Total Gwydir Revenue Requirement (2010/11) - $5,104,000

The model assumes 100% High Security use, on the basis of 100% being made available.

Table 2: Comparison of High Security Contribution through SW model & Alternative Model /General Security

Model	***Percentage of total average water use***	***Revenue Needed to be Generated***
State Water's Model	*N/A*	*$486,023*
GVIA's with 15 year Forecast	*7.8%*	*$398,112*
GVIA's Model with IQQM Forecast	*7%*	*$357,280*

Table 3: Impact on Proposed Prices (2010/11) All other factors remaining the same

Model	***HS Entitlement Charge***	***GS Entitlement Charge***	***Usage charge***	***HS Revenue***	***GS Revenue***	***Total Revenue***
State Water's Model	***11.54***	***3.52***	***11.11***	***$486,023***	***$4,617,977***	***$5,104,000***
GVIA's with 15 year	***7.44***	***3.69***	***11.11***	***$398,112***	***$4,705,888***	***$5,104,000***

Forecast						
GVIA's Model with IQQM Forecast	***7.44***	***3.69***	***9.91***	***$357,280***	***$4,746,720***	***$5,104,000***

GVIA believes its model represents a rational way of proportioning actual cost, and is much more equitable and justifiable than either the existing model or State Water's proposed model.

GVIA wants to be very clear that although it has quoted State Water's revenue requirements in the above example, it does not accept the validity of these requirements as has been detailed throughout the rest of the submission.
And while GVIA has provided two versions of its model, its clear preference, as documented throughout this submission is to use the IQQM based Consumption forecast.

GVIA can envisage that this High Security/General Security pricing model may not be attractive to all valleys, but believes it could be implemented on a valley-by-valley basis.

The GVIA model is based on 100% high security usage. If analysis of High Security usage shows long-term usage is less than this, GVIA would suggest the High Security fixed charge is raised to cover any difference.

However, it should be noted that it is the usual practice in the Gwydir for any High Security water not used by the entitlement holder, to be transferred to a general security entitlement holder for use.

Recommendation 5: IPART should adopt the High Security/General Security charging model proposed by GVIA in this submission (or a similar model based on actual costs and the percentage of water made available to each class on average).

Price Paths

While GVIA has some sympathy with IPART's "Glide Path" approach to pricing as a tool to minimise price shock, GVIA cannot help but to express some cynicism as well – "How genuine is IPART's concern when it can propose price rises of 148%?" The "Glide Path" approach can bee seen as a tool to set higher closing prices, and therefore a higher starting point for the following Determination.

The table below shows the impact of the "Glide Path" approach, compared to setting prices to recover full revenue requirements from Year 1. While GVIA has used IPART's calculated revenue requirements and consumption forecast in the Table, it does not in any way represent an endorsement of the IPART revenue requirements or consumption forecasts. In the example below GVIA has adopted a constant High

Security/General Security ratio of 3.28, which although equal to State Water's proposed ratio; its use is not an endorsement of that ratio.

GVIA makes the point that given the model below leads to full revenue recovery every year of the Determination, there should be further discounting of charges, reflecting the earlier revenue collection when compared with IPART's "Glide Path" approach.

Recommendation 6: That IPART enters into further negotiation with GVIA on the relative merits of the "Glide Path" approach, compared with the setting of prices to achieve revenue recovery for each year of the Determination. Matters to be discussed include pricing start point for the first Determination post 2013/14, and pricing discounts that could be applied to the "full recovery" model.

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Table 4: Comparative Pricing and Revenue Collection Model

2009/10	2010/11	2010/11 Revenue Generated		2011/12 Revenue Generated		2012/13 Revenue Generated		2013/14 Revenue Generated	Total Increase	Total % Increase	Total Determination
		5,100,000		5,083,000		5,120,000		5,230,000			20,533,000
		2,040,000		2,033,200		2,048,000		2,092,000			8,213,200
		3,060,000		3,049,800		3,072,000		3,138,800			12,320,600
Fixed HS 6.08	9.86	211576	11.99	257281	13.72	294404	15.11	324230	9.03	149%	
Fixed GS 3.37	3.39	1727764	3.64	1855181	3.91	1992790	4.21	2145690	.84	25%	
Usage 8.96	10.82	2680482	11.40	2824167.6	12.02	2977762.68	12.66	3136312	3.70	41%	11618761
		4619822		4936630		5264957		5606232			20427641
Fixed HS 6.08	11.53	247410.74	11.53	247410.74	11.58	248483.64	11.84	254062.72	5.76	95%	
Fixed GS 3.37	3.51	1788924.15	3.51	1788924.15	3.53	1799117	3.61	1839891	.24	7%	
Usage 8.96	12.35	3059514.9	12.31	3049605.54	12.4	3071901.6	12.67	3138789.78	3.71	41%	
		5095850		5085940.43		5119502.69		5232743.15			20534036

Revenue Requirement
IPART"S Proposed Glide Path Pricing
Immediate Full Recovery Pricing

Fish Passage Works when Triggered by Dams Safety Upgrades

While GVIA supports IPART decision not to re-open the “cost shares” debate in general, GVIA is very disappointed that IPART has not ruled that “fish passage works triggered by pre-1997 Dam Safety Upgrades” should be treated as a 100% Government cost.

GVIA calls on IPART to reconsider this decision.

While IPART identifies that fish passage is required because dams prevent fish movements, and therefore the “impactor” (irrigator) should pay, IPART appears to have failed to properly consider the following two points:

1. *It was recognised long before 1997 that dams impact on free fish movement, and therefore the provision of fish passage infrastructure is infact a legacy cost.*

2. *The specific driver for the fish passage works is not that the construction of the dam has impacted on fish passage; it is that the upgrade works will trigger a requirement to carry-out fish passage works. Therefore, under the “impactor” pays definition it is clear that the impactor under these circumstances is the government, and it should therefore bear 100% of the costs.*

Recommendation 7: That IPART reverse its draft Determination decision on cost shares where fish passage works are triggered by pre-1997 Dam Safety Upgrade works, and that the associated costs be deemed to be 100% Government costs.

The Murray-Darling Basin Authority Costs

Like other irrigator organisations GVIA is very concerned about the lack of transparency and accountability when it comes to the passing-on of the Murray-Darling Basin Authority costs.

Furthermore, GVIA is totally opposed to any of the Murray-Darling Basin Authority costs being levied on the Gwydir Valley by State Water.

While there may be a legitimate argument for Gwydir Valley irrigators to bear some of the MDBA’s planning and regulatory costs, and that may become apparent in the NSW Office Of Water Determination process, GVIA does not believe that there is any basis for extracting a contribution towards the operational services State Water may undertake on the Basin’s behalf.

GVIA is unaware of any operational task, which occurs within the Gwydir Valley, which impacts on the management of the Murray-Darling Basin as a whole. Therefore, no cost should be levied on Gwydir Valley irrigators.

Further more, should IPART be convinced that some genuine tasks do occur outside the Gwydir Valley, and that Gwydir irrigators should make some contribution to it, there does not appear to be any justifiable logic in the way costs have been proportioned between valleys.

An appropriate way to apportions costs for a common good would be on the basis of contribution of total flows to the Murray-Darling system.

While not wishing to impact on neighbouring valleys, t is a hydrologic fact that both the Namoi Valley and the Borders Rivers contribute far greater volumes into the wider Murray-Darling Basin than the Gwydir, yet the Border Rivers are asked to provide approximately a third of the contribution of Gwydir Valley irrigators, and the Namoi only contributes marginally more than the Gwydir.

Recommendation 8: That IPART remove the MDBA cost allocation from the Gwydir, and if a cost allocation must remain, it is proportional, based on inflows from the tributary streams into the main streams of the Darling and Murray Rivers.

Bill Impacts

If the implications were not so serious, IPART's analysis of the impact of the proposed price increases on Gwydir Valley irrigators would be laughable.

It is almost incomprehensible, that an organisation like IPART, which is expected to have some economic credentials, could conclude that annualised increases of up to 16.6% will have only minimal impacts on a farm business.

In some ways it is almost irrelevant as to what proportion a cost makes up of a farm business, any increase has an effect on the business's level of profitability.

However, it is worth considering how larges increases can massively affect profits, even when they are applied to costs that represent less than 10% of a business's turn-over.

For example, GVIA is aware of one large farm business which currently turns over approximately $3.56 million per annum. The farm relies on high security water, and uses approximately 66% of it entitlement. For 2009/10 its State Water bill will be approximately $149,504; if the IPART Draft Determination stands its State Water bill will rise in for years to $294,688 - a whopping 97% increase.

Assuming a 10% level of profitability, the farm currently makes $356,000 per annum. However, a $145,184 increase in water costs will slash that profit to $210,816 – a massive 40%, even though the water charges only represent 8% of total costs.

The situation for Gwydir General Security irrigators is far worse. Over the past 8 years Gwydir General Security allocations have averaged just 10%, and no irrigation enterprise can operate profitably at that level of allocation.

Any increase in water costs at these very low levels of allocations will directly lead to further increases in losses.

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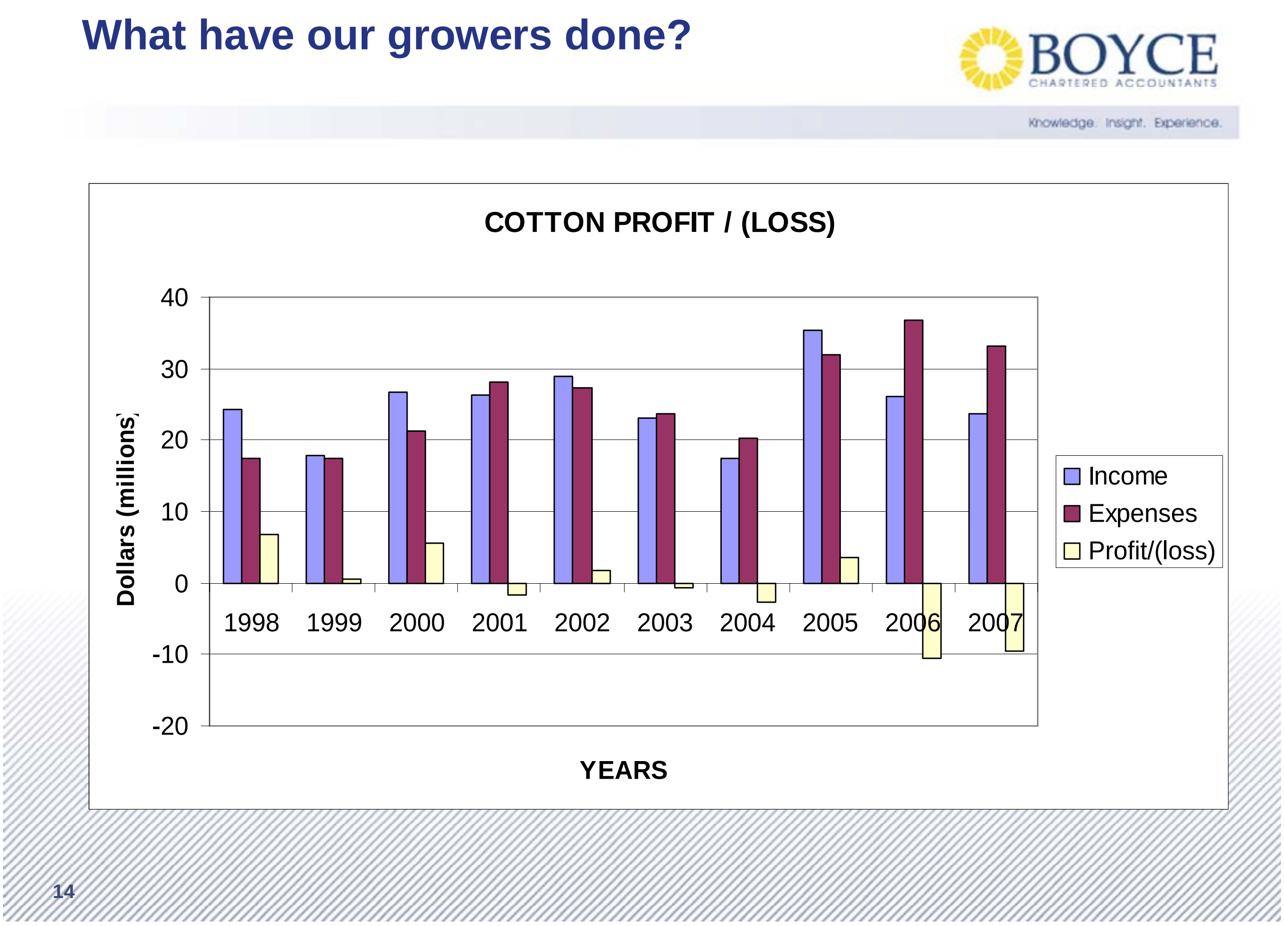
The following graph from the Boyce Chartered Accountants Cotton Comparative Studies highlights the current level of profitability for Gwydir Valley General Security irrigators.

The proposed prices rises will without doubt increase the negative gap between income and expenses.

Chart 5: Cotton Industry Profitability



IPART should not, and can not, simply look at water charge costs in isolation. While a modest increase in a single cost centre may not on its own have a significant impact, businesses face upward costs pressures from all quarters.

Most costs are somewhat contained by market forces, but cost increases from monopoly organisations like State Water and local government councils are largely unrestrained and are often many times greater than CPI.

Gwydir irrigators are currently facing not only the enormous costs increases proposed by State Water, but similarly large increases are being proposed by Moree Plains Shire Council. Both these costs are largely fixed costs during years of low water allocations, and therefore cannot be recouped from increased production.

Finally, GVIA is insulted that IPART failed to do any specific economic analysis on the Gwydir Valley, despite the gravity of proposed increases, and then when it does do sensitivity analysis for general security irrigators it uses 60% allocations which is at a level that supports the IQQM Consumption Forecasts, but which has been rejected by IPART for that purpose.

GVIA concludes that IPART has completely disregarded its statutory obligations to consider Gwydir Valley irrigators' capacity to pay, and has failed in its obligation to protect irrigators from monopoly abuse.

Further more GVIA is insulted that IPART can recommend a cap on annualised increases of 10% for some valleys (extraordinarily those that were not recognised at having reached full cost recovery in current Determination periods) but has recommended increases in excess of that cap for Gwydir Valley members.

GVIA is incensed by this treatment and argues that if a Cap is to be applied, it should be applied equally to all valleys.

Recommendation 9: That IPART immediately commission a full and independent study of the financial impact of the proposed prices on the financial viability of Gwydir irrigators, and that it amends its prices to a level that is financial sustainable for Gwydir irrigators.

Recommendation 10: That IPART offer a maximum cap on price increases to all valleys covered by the Determination.

Submission ends