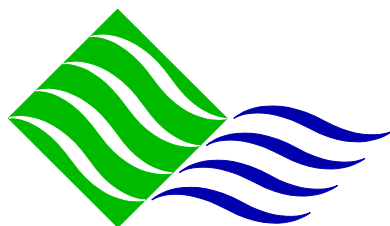


Murray Irrigation Limited
Submission to IPART
Review of bulk water charges for State
Water Corporation
Water – Draft Determination and Draft
Report

IPART 2010 Bulk Water Prices
Determination



Murray Irrigation Limited

Friday 16 April 2010

1. Introduction

Murray Irrigation holds five water access licences with the NSW Government and has issued contractual rights to its customers. Murray Irrigation's NSW Murray general security licence is equal to approximately 67 percent of the total general security water entitlements in the NSW Murray.

Murray Irrigation's total licence volume excluding its supplementary water licence is approximately 1,423,000, unit shares or 69 percent of the volume used in IPART's draft determination for the Murray. The company supplies irrigation water and associated services to 2,389 landholdings over an area of 748,00ha in the southern Riverina. Further information about the company and its operation is available at www.murrayirrigation.com.au.

Murray Irrigation welcomes the opportunity to respond to IPART's draft determination and draft report for the NSW State Water Corporation, March 2010.

Murray Irrigation is a member of NSW Irrigators' Council and is cognisant of its submission to IPART, particularly in relation to "macro" or non valley specific issues arising from the draft determination. This submission focuses on the issues that have specific relevance to Murray Irrigation and its customers arising from IPART's draft determination.

2. Determination period

Murray Irrigation supports a four year determination period because it provides irrigators and State Water with certainty and is also efficient in terms of the human and financial resources of both stakeholders and government consumed by the determination process. It is also aligned with the end date for a large number of the NSW water sharing plans in the Murray-Darling Basin.

3. Consumption forecasts

Murray Irrigation acknowledges the revenue volatility State Water is presented with as a result of variability in water usage driven by climate variability. Revenue volatility risks are exacerbated where a large proportion of revenue is driven by usage charges as proposed by the draft determination and State Water. Murray Irrigation appreciates the issues facing State Water, where 60 percent of the revenue is planned to be from usage charges, therefore price setting relies on the infrastructure operator assuming a volume of use. This is exactly the issue facing Murray Irrigation where; 1) customers are demanding reduced fixed charges 2) infrastructure costs are largely fixed and 3) operating costs are not strongly linked to the volume of sales. In response Murray Irrigation has altered its consumption forecast and deferred capital and maintenance expenditure, to reduce costs and minimise operating losses during this recent extended period of low water availability.

IPART's draft determination which uses a 20.3 percent reduction in the consumption forecast compared to State Water's proposed 28.1 percent is preferred to State Water's approach for the 2010 determination.

4. Revenue volatility

The revenue volatility provision included by IPART in the draft determination which will be borne by NSW General Security entitlement holders alone is not supported by Murray Irrigation for the following reasons;

- 1) The draft determination includes an increased Weighted Average Cost of Capital (WACC) which will provide benefits to State Water and assist State Water manage risks associated with revenue volatility.
- 2) The draft determination includes a reduction in the consumption forecast which will assist State Water reduce its revenue risk exposure as a result of lower water sales.
- 3) State Water should continue to be exposed to commercial pressure to adjust their business costs in response to reduced sales and not be insulated to this pressure by three mechanisms.

IPART has rejected the proposition from stakeholders that State Water's revenue and government dividends should not be insulated from commercial pressures to adjust costs and activities and deliver lower dividends in response to lower than budgeted water sales.

Murray Irrigation is acutely concerned the draft determination that provides State Water with three mechanisms for managing revenue risk. Murray Irrigation considers this approach is excessive and will remove the pressure that State Water has successfully responded to during the last determination to improve the efficiency of their business and to prioritise their expenditure when exposed to revenue shortfalls.

Murray Irrigation considers IPART's draft determination will result in State Water extracting monopoly rents and wealth transfer from customers with NSW Treasury being the ultimate beneficiary. Murray Irrigation reiterates the argument presented in its October 2009 submission. In contrast the southern connected Murray-Darling Basin the Victorian and South Australian Governments both subsidise bulk water prices even though the principles of the National Water Initiative purport to relate to **all** states and territories. Murray Irrigation believes one of IPART's central responsibilities as a regulator is to protect customers from monopoly rents.

Murray Irrigation also requests IPART confirm how the additional revenue collected to insulate State Water against revenue volatility will be protected from NSW Treasury. Given the high proportion of State Water profit that is expected to be paid to NSW Treasury as dividends, this is a pertinent point. History has shown that surpluses accumulated by Government owned entities have been subsumed by Government and subsequently not available for the purpose they were collected.

IPART's draft determination results in less revenue from water users overall than State Water's approach. However using the WACC premium does not result in valleys paying less. IPART's approach results in significantly more additional revenue being collected from the Murray compared to State Water's approach (Table 4.7, pg. 44 compared to Table 4.8, pg. 48).

If a revenue volatility provision is included in the final determination **and** a premium for high security entitlements (refer point 10) applies in the final determination then the volatility provision should apply to general security entitlements.

5. MDBA Costs

Murray Irrigation finds it totally unsatisfactory the Murray Darling Basin Authority (MDBA) expenditure has escaped regulatory or public scrutiny under the *Water Act 2007* (Cth).

Murray Irrigation supports IPART's comments in relation to MDBA costs. Murray Irrigation is acutely aware of the escalation in MDBA costs, the complete absence of scrutiny and their potential implications for bulk water costs and water resource management costs paid by water users in the southern connected Murray-Darling Basin.

In the face of the information available about MDBA costs Murray Irrigation supports IPART's approach to MDBA costs on the basis of past practice. In particular Murray Irrigation supports the sharing of these costs across valleys in the Murray-Darling Basin as proposed and consistent with the 2006 determination.

Whilst State Water argues these are "pass through" costs State Water also incurs costs and receives payments on behalf of River Murray Water, it is too simplistic to argue these costs should form part of the NSW Office of Water's costs. Furthermore the costs included in the State Water submission for the MDBA should be reflective of the functions related to bulk water supply performed by State Water in other valleys.

Murray Irrigation is having difficulty reconciling the information in the draft determination in relation to MDBA costs and NSW Murray costs, particularly in comparison with the information provided by State Water in their September 2009 submission. This issue will be addressed directly with Tribunal staff.

6. Price path

Murray Irrigation supports IPART's approach to setting prices to smooth cost price increases over the determination period; this is particularly important where annual expenditure volatility exists, driven by lumpy capital investments.

7. Price structure

Murray Irrigation supports the draft determination's proposal to maintain the current price structure, where 40 percent of the target revenue is recovered from fixed charges and 60 percent from variable usage charges.

8. Cost share ratios

Murray Irrigation supports IPART's decision not to re-open the debate about cost sharing ratios in this determination. In supporting IPART's decision Murray Irrigation notes it is Murray Irrigation's opinion that water users in the NSW Murray are effectively subsidising many beneficiaries of the regulated river system, or "free riders."

In the River Murray there are a multitude of businesses and recreational activities that are reliant on a regulated Murray that are not licensed to consume water and currently make no contribution to either capital or river operation costs, however these industries place

demands and incur costs on State Water and River Murray Water, the majority of which are passed on to water users.

9. Common cost allocation

Murray Irrigation supports IPART's approach because it logically should result in the most equitable outcome.

10. High security and general security entitlement charges

Murray Irrigation supports the introduction of a higher fixed charge for high security entitlements. Murray Irrigation's October 2009 submission to IPART provided Murray Irrigation's arguments for the justification of a fixed charge premium for high security entitlements compared to general security entitlements.

Murray Irrigation encourages IPART to continue to consider this issue in conjunction with other aspects of their determination. It is important that consideration of this issue is not made in isolation from the volatility premium. The removal of the high security premium **and** the retention of the volatility provision in the draft determination would result in inequitable treatment of general security entitlement holders. This outcome should be avoided.

11. Upper bound pricing

Murray Irrigation continues to oppose the transition to upper bound pricing, where practicable, and considers upper bound pricing is effectively a tax on the productive sector. The NSW Government, to Murray Irrigation's knowledge, is the only Government in the Murray-Darling Basin that includes a rate of return on capital in rural water pricing. In addition, other jurisdictions are failing to recover the actual bulk water costs from irrigators. This disadvantages NSW irrigators in the highly competitive market place. IPART's determination is an important opportunity to ensure that NSW irrigators are only paying for the efficient cost of bulk water services and are not disadvantaged in the market by the determination.

12. Wholesale discounts or rebates

Murray Irrigation is disappointed with IPART's approach to wholesale discounts or rebates.

The concept of wholesale discounts or rebates for large customers has been a feature of bulk water determinations since the referral of bulk water charges to IPART's predecessor. The 2006 determination introduced a fixed price rebate, in Murray Irrigation's case this was \$1.566M, previously Murray Irrigation had paid 60 percent of the NSW Murray general security entitlement charge. This discount and the different percentage discounts for different irrigation infrastructure operators were determined by IPART.

The draft determination proposes a 40 percent reduction in the wholesale rebate received by Murray Irrigation in 2010/11 increasing to a 43 percent reduction in 2013/14. In 2010/11 this will be equal to an effective price increase for Murray Irrigation and its customers of 47 percent, (subsequent price increases from 2010/11 to 2013/14 are relatively small). This contrasts with the 5.6 percent increase for NSW Murray general security entitlement charges reported in chapter 10, table 10 page 120 of the draft determination.

The dramatic reduction in Murray Irrigation's wholesale discount and associated increase for Murray Irrigation and its customers effectively minimises any price increase to other entitlement holders in the NSW Murray. Given that Murray Irrigation's customers hold the largest volume of water entitlements in the NSW Murray, the implications of pricing decisions on customers' bills presented in chapter 12 of the draft determination is misleading because it ignores the impact of reduction in the wholesale discount on prices paid by Murray Irrigation and its customers.

IPART has provided no explanation for the reduction except to accept State Water's proposition, which was based on avoided costs calculated per entitlement, when the avoided costs are not entitlement driven.

State Water's approach also results in each bulk scheme being treated equally relative to the volume of water entitlement held.

In reality there are substantial differences between bulk schemes in terms of their interface with State Water's operations and the benefits their operations and infrastructure provide to State Water for river regulation.

State Water's approach adopted by IPART effectively ignores the ancillary benefits to river regulation provided by Murray Irrigation. Specifically Murray Irrigation's capacity to release regulated flows to the Edward River, River Murray, Billabong Creek, Wakool River and Niemur River.

Furthermore, the wholesale rebate was established by IPART, not State Water. Murray Irrigation considers IPART when proposing such a significant change to State Water's charges requires justification based on its own analysis. It should not rely solely on the limited analysis presented by State Water.

At the formation of Murray Irrigation in 1995 and the establishment of the company's bulk water licence, increased revenue was provided to State Water's predecessor by the licensing of conveyance water entitlements. In Murray Irrigation's case this volume was 330,00 unit shares (now 300,000 unit shares). At 2009/10 general security entitlement charges this is \$660,000 of revenue. This benefit is independent of State Water's avoided costs argument. Prior to the creation of Murray Irrigation's bulk licence no revenue was collected for conveyance water, which was not separately licensed, but accounted as part of "river operational losses."

Murray Irrigation considers significantly greater justification and analysis is required from IPART to warrant change of the scale proposed. This change is not based on increased costs but reallocation of costs from one group of customers to another by IPART, based on State Water's advice. The draft determination proposal to reduce Murray Irrigation's wholesale rebate to the extent it has places Murray Irrigation's effective price increase at the upper end of the price increases proposed by IPART across NSW in **one** year, it is not even smoothed over the determination, as are other price increases.

Murray Irrigation requests IPART revisit the draft determination in relation to wholesale rebates and recommends continuation of the current rebate at the 2009/10 levels adjusted for CPI.