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Mr James Cox
Acting Chairman and Chief Executive Officer
Independent Pricing and Regulatory Tribunal of NSW
PO Box Q290
QUEEN VICTORIA BUILDING NSW 1230

Dear Mr Cox

I am writing in response to your call for comment on the NSW Office of Water (NOW) submission to its current price review.

The Sydney Catchment Authority's comments are attached. In summary, it is important that a transparent independent process is in place for setting water resource management charges in NSW. It is the SCA's view that pricing should reflect the water available for sale (extraction limit) and not the usage allowed as a contingency (share component). This is particularly important as the amount of water used by the SCA is metered giving a high degree of certainty and transparency around the quantum of water it takes. NOW's proposed pricing approach for the SCA is inconsistent with the other customer charges and is not based on use.

In the interests of transparency, NOW should outline the link between the SCA's extraction of water and NOW's costs. It should also provide information on the benefits associated with the proposed expenditure and clarification of the basis for the imposition of the various separate Water Management Licence charges so that the basis for these charges can be assessed.

Should IPART determine a price increase for NOW in excess of that allowed in IPART's June 2009 metropolitan water price determination for the SCA, then the SCA should be allowed to pass this cost through in IPART's next SCA price determination.

If the Secretariat wishes to explore any of these matters further, kindly contact Kumar Rasiah, Senior Manager Economics, on 4724 2487.

Yours sincerely

A handwritten signature in black ink, appearing to read "Michael Bullen", written over a horizontal line.

MICHAEL BULLEN
Chief Executive

21.6.10

SCA Submission

The Independent Pricing and Regulatory Tribunal (IPART) determines maximum prices that may be charged for bulk water services provided by the NSW Office of Water (NOW). IPART has called for submissions in order to address matters raised by NOW regarding its prices to apply from 1 July 2011.

This submission discusses matters that the SCA wishes to bring to IPART's attention in relation to the current review. It is important for the community and, in particular, for water extractors, that there is an ongoing, independent and transparent process for setting bulk water resource management charges in NSW. Such a process is particularly important to the SCA, as these charges are necessarily passed through to Sydney Water's 1.6 million customers.

The SCA has identified two key principles in relation to the licensed water allocation to SCA, which determines the share of IPART determined efficient costs that SCA will bear. These are that:

- prices should reflect the actual average water available for sale (SCA extraction limit), and not temporary water usage allowed as a contingency (the SCA share component)¹, and
- should IPART award a price increase to NOW in excess of that allowed in IPART's June 2009 metropolitan water price determination for the SCA, the SCA be allowed to recover this in IPART's next price determination for the SCA.

SCA is charged bulk water prices for water resource management services provided by NOW. This charge is usage based, and is regulated by IPART for efficient delivery of water resource management services.

SCA is required to reimburse costs incurred by NOW in its role servicing the Water Administration Ministerial Corporation in issuing and managing SCA's Water Management Licence. These charges (a one-off Licence Fee and an annual Management Charge) are related to Water Resource Management services that are delivered by NOW. IPART has previously chosen not to regulate these charges². These charges are billed semi-annually by NOW based on itemised invoices.

SCA is also required to pay for works and services required for NOW's water resource management directives. This includes such items as water monitoring and telemetry equipment. These costs are directly funded by the SCA as they occur.

NOW should provide clarification of the basis for the imposition of separate Water Management Licence charges; details of the link between the SCA's extraction of water (in accordance with its Water Management Licence) and NOW's costs. It should also provide information on the benefits associated with the proposed expenditure, including data on actual and licensed extraction and data on compliance rates with its legislation and, where this is not possible, data on enforcement effort.

Without this information the SCA cannot determine whether costs recovered by the non-IPART regulated charges are also being recovered from the IPART regulated charges. This lack of transparency could lead to a perception that there is "double charging". There is also insufficient detail in NOW's submission regarding the relationship between NOW charges and the SCA's water usage. NOW is unclear as to how it has determined the SCA's level of financial contribution to NOW for the resource management of the SCA's catchments.

¹ NSW Office of Water (2010) Draft Water Sharing Plan for the Greater Metropolitan Region unregulated river water sources: background document, May, Pg. 43

² "Following consideration of information about the nature of the charges and the steps taken by DLWC to disclose costs to these agencies, the Tribunal will not be determining these charges." IPART (2001) Department of Land and Water Conservation from 1 October 2001 Determination No 3, 2001, December 2001

1. Services provided by NOW

The service provided by NOW is water resource management. In its issues paper, IPART describes this as “activities to ensure the long-term sustainability of the resource, to allow continued water extraction and maintain the health of the natural ecosystem.” (Pg. 11). IPART classified water resource management activities undertaken by NOW in its issues paper (ibid. Pg. 13) into five categories:

- *negotiating with other States and the Commonwealth on interstate water sharing arrangement*
- *developing and implementing water sharing plans for sharing water between the environment and extractive users*
- *administering water licences and approvals, assessing resource availability, allocating available water to licensees, monitoring compliance and, where necessary, taking appropriate enforcement action*
- *developing and implementing water trading rules and systems to support effective market operation*
- *advising on plans and strategies for the protection and enhancement of water courses, riparian corridors and groundwater dependent ecosystems.*

This is a reduction in scope since the last price determination³, as policy development and other Government functions are no longer to be charged to water users under the 2007 COAG Agreement⁴.

Note also that PriceWaterHouseCoopers in IPART’s Review of NOW Expenditure⁵ excludes some metropolitan water planning activities from this scope because they are inconsistent with the “making available of water” requirement (eg. demand management, infrastructure planning). SCA supports clear delineation of water resource management activities in NOW’s planned expenditure. Specifically, NOW provides licensing of SCA access to water resources in the catchments. Licensing involves monitoring, review and administration.

2. SCA’s Water Management Licence

The SCA is licensed under the *Water Act 1912* as an interim measure until the relevant provisions of the *Water Management Act 2000* commence. With the draft Water Sharing Plan (WSP) for the Greater Metropolitan Region now on public display, and at commencement of the WSP, SCA will transition to the *Water Management Act 2000*.

The Water Management Licence allows the SCA to abstract water, operate in-stream works and storages and to discharge from storages into rivers and streams; and requires the SCA to provide flows for the environment and riparian users.

3 Water charges

Bulk water usage

SCA is charged bulk water prices for water resource management services provided by the NOW. This charge is volumetric based, and is regulated by IPART based on efficient delivery of Water Resource Management (WRM) services.

Other water users in the South Coast region pay a two part tariff. When the two parts are added together the total equals the SCA’s tariff. However, these users, unlike SCA do not

³ cf. IPART (2004) Bulk Water Prices from 2005/06 Issues Paper, Discussion Paper DP78, September, Pg. 7

⁴ IPART (2009) Review of prices for Water Administration Ministerial Corporation From July 2010 Water — Issues Paper, July Appendix B, Pg. 50

⁵ PriceWaterhouseCoopers & Halcrow (2010) Review of NSW Office of Water’s water management expenditure, April, Pg. 68

have their usage metered, so that it is possible that their actual charge per megalitre is greater or less than that of the SCA depending on their consumption. As metering is rolled out, this anomaly should disappear.

The following table shows the trends in price, usage, and consequently total cost (price times usage) for Bulk Water for SCA. Prices will have risen in nominal terms by 18% over the current price path.

Year	Applicable charge (\$/ML)	SCA Usage Net of Purchases * (ML pa)	Total Cost (\$ pa)
2001	\$1.80	626,915	1,128,447
2002	\$1.80	625,387	1,125,697
2003	\$2.16	631,625	1,364,310
2004	\$2.67	556,565	1,486,029
2005	\$2.72	519,467	1,412,950
2006	\$3.00	524,316	1,572,948
2007	\$3.06	504,143	1,542,678
2008	\$3.18	478,353	1,519,037
2009	\$3.36	490,283	1,647,372
2010**	\$3.54	500,653	1,772,060

* SCA purchases approximately 4GL pa from the Fish River Water Scheme in "normal" years, but has not purchased any water for some time due to drought.

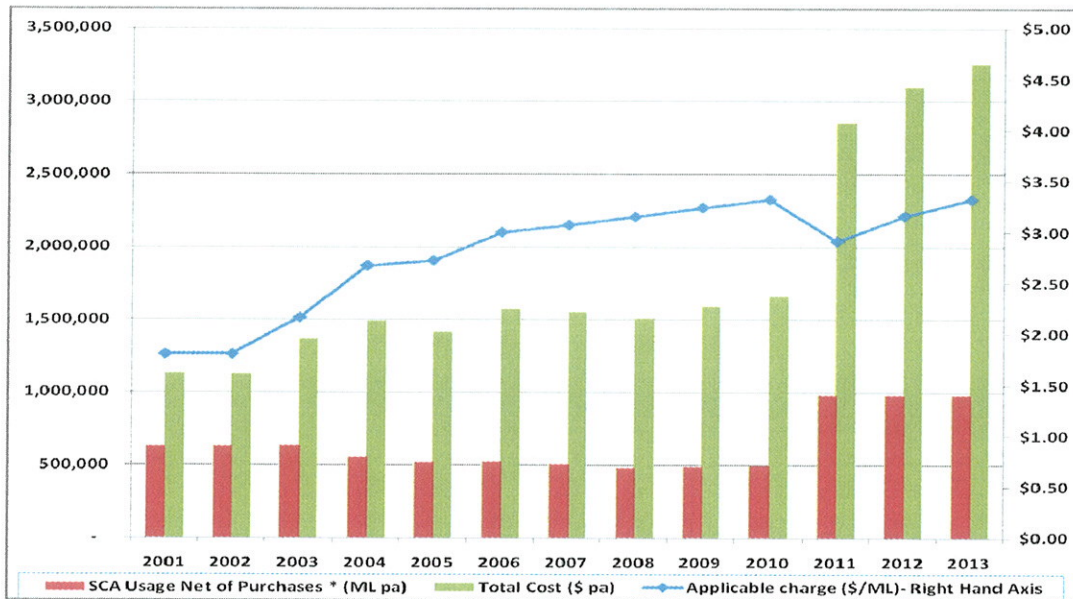
** Estimated.

Figure 1 illustrates the pattern of these historical trends, but includes forecast prices, volumes sold and revenues (costs) to NOW (SCA).

The most significant issue for SCA is the proposed entitlement basis of the charge, which will be more than double the forecast extractions over the price path. In particular, the use of the share component (the maximum extraction from any source in any year), instead of the extraction limit (the maximum extraction over all sources in any year) is at odds with the approach for other users such as irrigators.

The information contained in the NOW supplementary submission (January 2010) is general and there is no specific dollar amount attributed to resource management actions for metropolitan water utilities. It is not possible to determine costs associated with SCA's water use. Using these costs, it appears that the South Coast region (containing the SCA's operating area) bears an unusually high share (circa 33%) of WRM costs for unregulated use in NSW. SCA appears to incur 55% of the unregulated WRM cost in the South Coast region and 20% of all unregulated costs in NSW.

Figure 1: Price and Total Cost to SCA



*After 2009/10 licensed quantity which is approximately twice usage (115% to 130% of forecast usage). This is NOW's interpretation of the Water Sharing Plan outcome.

Costing NOW's regulatory effectiveness

NOW's regulatory effectiveness is likely to be as significant a driver of SCA costs as NOW pricing for bulk water. NOW should provide detailed information on the level and effectiveness of its regulatory effort. This should include information on the results or benefits associated with the proposed expenditure; in particular,

- data on actual and licensed extraction in the region, transparently showing trends over the price path of extraction in excess of license.
- information on compliance rates with its legislation (eg. volume of unlicensed extraction/area of illegal irrigation/no. of licence breaches detected) and where this is not possible, at minimum it should provide data on enforcement effort (volume of unlicensed extraction subject to prosecution action/licensees prosecuted)

Water Management Licence related charges

The SCA at licence commencement in 2001 was charged \$420,000 as a water management Licence Fee; and is levied an ongoing water management charge in the range of \$100,000 to \$250,000 per year. The following table shows those costs:

Year ending June	2001	2002	2003	2004	2005	2006	2007	2008	2009**
Water Management Licence Charge (\$)	420,000	147,000	228,877	244,741	139,412	182,881	127,109	125,651	102,619

**NOW does not include a forecast of Utility charges for future years in its Submissions.

The Licence Fee and Water Management Charge are intended to cover the actual costs incurred by the Ministerial Corporation in dealing with the application for, and ongoing management of, the Licence respectively. Schedule 7 of the SCA's Water Management Licence states:

Part 9, of the Water Act 1912 contains provisions for the Ministerial Corporation to recover costs in managing the Licence...

Water Management Charges are the ongoing costs incurred by the Ministerial Corporation in managing the Licence. The costs associated with management activities are likely to vary from year to year, with higher costs being incurred in years when reviews and/or special studies or investigations are being carried out.

Cost recoverable activities relating to managing the Licence are likely to include (but are not limited to):

- Statutory reviews (initial six month review and then every five years;) and other reviews if required;
- Monitoring and studies including audit and compliance monitoring; biophysical monitoring and special studies/investigations (if required);
- Administration including annual reporting, auditing, general day to day administration of the licence; other water management functions and determining water management charges.

4. SCA's contribution to resource management.

The SCA spends more than \$20 million per year to better protect and manage Sydney's drinking water catchment areas. The funds are used for:

- Developing the SCA's understanding of the catchment and its processes through research;
- Protecting the catchment from risks and rehabilitating existing harm;
- Implementing the Regional Plan;
- Engaging and communicating with the catchment community
- Management of the lands owned by the SCA (special areas plus other freehold holdings).
- Extensive monitoring activities. The SCA undertakes continuous water quality monitoring and sampling at 12 sites.
- Ensuring that the SCA's activities are consistent with ensuring the long-term sustainability of environmental resources (audit and review)

Meeting regulatory requirements

Continuous water quality monitoring activities are required under the Water Management Licence. To the extent that NOW can require SCA to undertake certain activities, the direct costs of NOW's regulatory requirements on the SCA are greater than those costs NOW recovers through price alone. It is important to recognise the total costs to SCA (and therefore Sydney Water customers) of NOW's regulatory requirements.

The SCA has environmental flow requirements under its water management licence for river health benefits downstream of the dams. In addition to the above costs to store the water, SCA's forward capital program allows for possible changes to the environmental flow regime, which are additional costs incurred to meet its regulatory obligations.

Currently there is no direct recovery of the opportunity cost of environmental flow releases. Given the possible magnitude of future environmental flow releases the SCA considers that the economic cost of environmental flow releases should be explicitly identified and fully recovered.