

Gwydir Valley Irrigators Association Inc.

458 Frome St, PO Box 1451, Moree NSW 2400

Gwydir Valley Irrigators
Associations submission to

*Review of Prices for State
Water Corporation*

Independent Pricing and Regulatory
Tribunal

October, 2009

TABLE OF CONTENTS

TABLES	4
FIGURES	4
EXECUTIVE SUMMARY	5
GVIA RECOMMENDATIONS	7
INTRODUCTION:	10
GENERAL COMMENTS:	11
SPECIFIC RESPONSES TO QUESTIONS IN THE IPART WATER – ISSUES PAPER RELEASED IN JULY 2010:	12
1. The appropriateness of State Water’s proposed service levels for the forthcoming determination period.	12
2. The appropriateness of State Water’s forecast operating costs for 2010 determination period, including the approach taken to allocate indirect operating costs (such as corporate overheads) between valleys.	12
a. <i>Works Approvals:</i>	14
b. <i>Environmental and Heritage Thematic Plan</i>	14
c. <i>Dam Safety Thematic Plan –</i>	16
d. <i>Research -</i>	16
e. <i>Land Management Thematic Plan</i>	16
f. <i>Emergency and Security Thematic Plan</i>	17
g. <i>Corporate</i>	17
3. Whether there is scope for State Water to achieve further efficiency gains over the 2010 determination period?	17
4. The information provided by State Water on its past and forecast capital expenditure, and the prudence and efficiency of this expenditure?	18
5. An appropriate rate of return to apply on State Water’s RAB and the means of estimating this rate?	19
6. Whether it is appropriate to address State Water’s revenue risk by adjusting the WACC?	21
7. The implications of transferring pricing responsibility from IPART to the ACCC for the Murray Darling Basin and any transitional arrangements that IPART might put in place to ensure a smooth transition?	22
8. The appropriateness of State Water’s proposed approach to depreciation, asset classes and lives?	22
9. Appropriate output measures for the 2010 determination period. These should be aligned to projects or activities that State Water plans to undertake over the forthcoming determination period.	22

10.	The usefulness of valley based reports.	23
11.	Whether the cost sharing approach used in the 2006 Determination remains appropriate.	23
12.	State Water's consumption forecasts, as outlined in its submission.	24
13.	The implications for prices and for State Water's financial viability of continued reduced water availability.	26
14.	The appropriate approach to translate user's share of the revenue requirement into State Water's prices.	27
15.	What transitional path and rate of increase is reasonable for prices in valleys where prices are not yet at full cost recovery.	27
16.	Options for meeting the cost of providing water in valleys in which cost reflective prices may not be practical.	27
17.	The appropriate balance between fixed and usage charges.	28
18.	The impact of State Water's proposed prices on its customers.	29
19.	The appropriateness of introducing a mechanism, such as scarcity pricing, to address State Water's revenue volatility; and a different sharing of revenue risks between irrigators and State Water.	34
20.	Whether there are any practical limitations that would need to be considered if a form of scarcity pricing was introduced.	35
21.	The appropriateness of State Water's proposal to recover the cost of meter service provision.	35
22.	Whether consumers support the continuation of the Yanco Creek levy.	35
23.	Whether the consumers support the introduction of other levies.	35
24.	Whether it is appropriate to maintain rebates to irrigation companies and districts (ICDs).	35
25.	The level of these rebates, if appropriate, and the justification for this position.	36
26.	The appropriate balance between high security and general security entitlement prices.	36
27.	The appropriate length for the 2010 determination period.	38
	OTHER MATTERS	38
	User Definition	38
	Government's responsibility to meet fix and usage charges on adaptive environmental water	39
	MDBA and BRC Pass Through Costs	40
	Supplementary Water	40

Tables

TABLE 1: STATE WATER’S PROFIT \$’000	12
TABLE 2: FORECAST OPERATIONAL EXPENDITURE GWYDIR VALLEY (\$09/10) \$M.....	13
TABLE 3: FORECAST CAPITAL EXPENDITURE (\$09/10) \$M	19
TABLE 4: THE REAL COST PER MEGALITRE FOR EACH MEGALITRE DELIVERED IN THE GWYDIR VALLEY (PROPOSED 2010/11 PRICES - 40% FIXED / 60% USAGE) *.....	28
TABLE 5: THE REAL COST PER MEGALITRE FOR EACH MEGALITRE DELIVERED IN THE GWYDIR VALLEY (PROPOSED 2010/11 PRICES – 90% FIXED / 10% USAGE) *	29
TABLE 6: STATE WATER’S PROPOSED GWYDIR PRICES.....	30
TABLE 7: HIGH SECURITY WATER BILL (\$) - 1000 MEGS ENTITLEMENT / 90% USAGE	30
TABLE 8: GENERAL SECURITY WATER BILL (\$) – 1000 MEGS ENTITLEMENT / 90% USAGE	31
TABLE 9: GENERAL SECURITY WATER BILL (\$) – 1000 MEGS ENTITLEMENT / 60% USAGE	31
TABLE 10: GENERAL SECURITY WATER BILL (\$) – 1000 MEGS ENTITLEMENT / 30% USAGE	31
TABLE 11: GENERAL SECURITY WATER BILL (\$) – 1000 MEGS ENTITLEMENT / 10% USAGE	31
TABLE 12: THE AVERAGE ANNUAL COST OF A MEGALITRE OF GS IN THE GWYDIR AND PROFIT FROM THE ANNUAL ASSIGNMENT MARKET	32
TABLE 13: COMPARISON OF HIGH SECURITY CONTRIBUTION THROUGH SW MODEL & ALTERNATIVE MODEL /GENERAL SECURITY	37
TABLE 14: IMPACT ON PROPOSED PRICES (2010/11) ALL OTHER FACTORS REMAINING THE SAME.....	37

FIGURES

FIGURE 1: GWYDIR WATER USE 1994-2009	25
FIGURE 2: AGGREGATE OF SIX GWYDIR VALLEY IRRIGATED COTTON GROWERS ASSET AND LIABILITIES PERFORMANCE	33
FIGURE 3: AGGREGATE OF SIX GWYDIR VALLEY IRRIGATED COTTON GROWERS PROFIT PERFORMANCE	34

Executive Summary

The Gwydir Valley Irrigators Association (GVIA) welcomes the opportunity to participate in this IPART Determination on State Water's Bulk Water Charges.

GVIA acknowledges the considerable improvement in State Water's business improvement over the past Determination period, and congratulates it on its achievements of profits during the worst drought in NSW's Irrigation Industry's history.

In closely considering IPART's issue paper, State Water's submission, and other matters GVIA has developed thirty-six recommendations for IPART's consideration.

GVIA's primary concerns can be summarised as follows:

- a. State Water is trying to portray its business as highly risky, primarily due water availability/supply fluctuations, and yet it has managed to produce profits through a period of very low water availability for both itself and its customers. This excellent performance makes it very hard to sustain an argument that revenue need to be further protected by applying a higher Weighted Average Cost of Capital and adopting new consumption forecast methods.
- b. State Water is trying to mask significant increases in operational expenditure by identifying it as new thematic expenditure. In the main these claims do not stand up to close scrutiny.
- c. Borrowing to fund significant Dam Safety Up-Grade expenditure (100% Government responsibility) is placing State Water's credit rating at risk, and this in turn is being used by State Water to try and justify higher charges. The inequity of this is the pressure on the credit rating is being caused by decisions that provide no additional benefit to water users, but will lead to higher costs if a higher WACC is imposed, and also increased asset management costs.
- d. State Water is proposing to adopt a "scarcity" tax, as a component of its High Security Fixed Charge. This approach is counter to the basic user pays principles which we understand form the basis of the IPART endorsed charging policies, and as such is an action well outside the role of State Water.
- e. Dam Safety Upgrade expenditure (driven entirely by State Government requirements and 100% Government Share) is triggering fish passage capital expenditure, resulting in State Water applying a 50% user share to customers.
- f. The definition of "user" is far too narrow.
- g. There has been a significant reduction in the users' capacity to pay over the past four-years.

In response to the above concerns GVIA is proposing.

- a. Maintenance of the Weighted Average Cost of Capital at 6.5%.
- b. Retention of the Long Run Average IQQM as the consumption forecast modelling tool.
- c. A rigorous review and analysis by IPART of State Water's proposed Thematic Expenditure, to accurately determine how much of it should be recognised as a component of baseline Operational Expenditure.
- d. Recognition by IPART that the pressure State Water may be facing on its credit risk rating is being driven largely by the NSW Government's decision to carry out non-commercial Dam Safety upgrades using borrowed funds, and therefore should not result in higher charges to users.
- e. The adoption of a cost-based High Security/General Security pricing ratio regime, as proposed by GVIA.
- f. A ruling that any fish passage work requirement triggered by Pre-1997 Dam Safety Upgrades be assigned as a 100% Government Cost.
- g. A broadening of the definition of user, and the development of more direct charges to identifiable users, as well as a Community Service Obligation payment to cover recreational use.
- h. That IPART adjust down full-cost recovery prices to reflect the users reduced ability to pay.

GVIA Recommendations

Recommendation 1: IPART commission a study of State Water's Operational Expenditure, benchmarking its performance against similar efficient businesses.

Recommendation 2: IPART independently assess the cost efficiency of the hydrometric service information provided to State Water by NOW.

Recommendation 3: That IPART evaluate the efficiency of the Work Approval costs being applied by NOW to State Water, and in particular the justification for a discount to be applied in recognition of the volume of work from a single client.

Recommendation 4: That EMP Implementation expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

Recommendation 5: That Environmental and Heritage Assessment Procedures expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

Recommendation 6: That the Fish Passage Program expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

Recommendation 7: Heritage Management Expenditure should be a 100% Government cost.

Recommendation 8: That water quality program expenses be paid for directly by government, or a differential pricing structure be developed that levies this cost onto urban, and domestic and stock customers.

Recommendation 9: That the Dam Safety Thematic Plan expenditure should be deferred, but if not, IPART must first ensure that it is not already been accounted for in either OPEX or Dam Safety Capital, and if it is genuine new expenditure it should be applied to Dam Safety Upgrade Capital expenditure.

Recommendation 10: That the research expenditure be funded out of profits.

Recommendation 11: That Land Management Thematic Plan Expenditure, if assessed by IPART to be genuine new expenditure, should be funded by State Water's unregulated business activities.

Recommendation 12: That the Emergency and Security Thematic Plan be viewed as a community cost, and funded directly by State or Federal Government.

Recommendation 13: That data cleansing be recognised as part of Baseline OPEX.

Recommendation 14: That the cost of developing an interstate tagging system should be recovered through the National Water Market Systems programme.

Recommendation 15: That OH&S Audits be recognised as an ongoing requirement, and therefore accounted for in Baseline OPEX.

Recommendation 16: IPART closely assess the prudence, and likelihood of State Water carrying out its budgeted for Environmental Planning and Protection work, with the view to removing it from State Water's regulated capital expenditure budget.

Recommendation 17: That IPART commission a study of the efficiency and prudence of State Water's capital expenditure, and this study includes a benchmarking component against similar efficient organisation.

Recommendation 18: That IPART apply a WACC no greater than 6.5%, and prevents any attempt by State Water to move away from its 40% Fixed / 60% Usage tariff system.

Recommendation 19: That IPART independently assess State Water's claim that its proposed adjustment to asset lives for depreciation purposes will have no net affect.

Recommendation 20: That IPART receive an annual report from State Water on expenditure, and any under expenditure of capital should result in a RAB adjustment and a consequential adjustment to the following year's prices.

Recommendation 21: That IPART receive an annual report based State Water's internal performance indicators, and monitor the results against State Water's operational expenditure.

Recommendation 22: That when fish passage work requirements are triggered by Pre-1997 Dam Safety Upgrades, the fish passage costs should be included as part of the Upgrade costs and allocated accordingly (100% Govt).

Recommendation 23: That IPART continue to use the long-run IQQM data as the basis of its consumption forecast model.

Recommendation 24: State Water prices should reflect the following factors in terms of how to equitably recoup user shares:

- a. Maximum 40% fixed component
- b. Minimum 60% usage component
- c. An equitable High Security/General Security ratio (As proposed by GVIA later in this submission)
- d. The use of the long-term IQQM Consumption forecast

Recommendation 25: Valleys not at full price recovery should be subject to price rises equal to the maximum price rise being faced by a valley deemed to be at full cost recovery.

Recommendation 26: That any planned shortfall in revenue from a valley, because cost reflective pricing is deemed impractical, should be compensated by a fully funded government CSO payment to State Water.

Recommendation 27: That at the very minimum IPART maintain a maximum Fixed Charges revenue component of 40%.

Recommendation 28: That IPART recognises the Gwydir Valley's customer's reduced capacity to pay, before approving any increase in State Water's charges.

Recommendation 29: That IPART should examine the cost efficiency of State Water's proposed method of recovering cost associated with the servicing of meters rolled out under the possible metering project.

Recommendation 30: IPART should develop a framework to ensure no "double payment" metering fees, should the proposed metering project roll out during the next Determination period.

Recommendation 31: 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 32: That IPART oblige State Water to charge DECCW fixed and usage charges on the ECA.

Recommendation 33: IPART should develop a price regime that recovers fixed and usage charges (at the high security rate) for replenishment flows water, and the charge should be levied either directly on the landholder beneficiaries or to NOW.

Recommendation 34: That the NSW Government be obliged to pay a CSO to State Water, equivalent to 5% of the Gwydir's user revenue share, on behalf of recreational users.

Recommendation 35: That IPART in making its Determination make definitive statement that the holders of environmental adaptive water be subject to the same water charging regime as other water entitlement holders.

Recommendation 36: That IPART remove any allowance for MDBA pass through cost, when calculating State Water's total costs for the Gwydir Valley.

Recommendation 37: That in the next Determination IPART fully considers the merits of establishing a fixed charge component for supplementary water.

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 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.

The GVIA welcomes the opportunity to provide input into the "Review of Prices for State Water Corporation", through the NSW Independent Pricing and Regulatory Tribunal (IPART) process.

The Association's contact details are as follows:

Chairman: Ian Cush
Chief Executive Officer: Michael Murray
Ph 02 67521399
Fax 02 67521499
Mobile 0427 521399
Email gvia@bigpond.com

458 Frome St,
PO Box 1451,
Moree, 2400

General Comments:

Firstly, GVIA would like to acknowledge the work of State Water, both in terms of its reforms over the past four years, and for its open and co-operative way that it has engaged with its customer's in the lead up to this Water Charges Determination process.

State Water is a more efficient and customer focussed organisation today, than what it was four years ago, and GVIA supports State Water in its efforts to become more efficient.

In providing this support GVIA has had to accept some significant reductions in locally based State Water staff; and while GVIA still holds some concerns, early indications suggest that the new State Water is up to the challenge of effectively servicing its customers under its new management structure.

GVIA believes the challenge for State Water is to continue to improve its efficiency, to the point where its pricing requirements are driven down, rather than constantly calling for real price increases.

In making this Determination of Regulated Water Charges for State Water, GVIA calls on IPART to carefully consider the following.

1. Under the 2006-2010 Determination, the prices set by IPART for State Water were considered to bring the Gwydir Valley to 100% cost recovery. Yet, State Water is proposing real increases of approximately 33% over the four-year Determination period. GVIA challenges IPART to reject these proposed increases, and apply a more realistic price path that reflects commercial practices. Few businesses today can get away with price increases that match CPI; at best they receive CPI – Efficiency Savings.
2. The primary drivers pushing up State Water's prices appear to be:
 - Modest, but real increases in operating costs, primarily being categorised as new thematic expenditure.
 - A significant reduction in forecast consumption/sales, through the proposed adoption of a new consumption forecasting model.
 - A significant increase in the Weighted Average Cost of Capital (WACC).
 - Significant capital expenditure, primarily driven by meeting Dam Safety Committee compliance standards.

GVIA will demonstrate through this submission that there are significant flaws in State Water's arguments surrounding each of these cost drivers.

3. During the period of the last Determination, State Water and its customers have had to endure what has undoubtedly been the worst drought in the NSW Irrigation Industry's history, yet State Water has been able to achieve regulated revenues equal to 67% of forecast, make a profit in two of the past three years,

and pay significant dividends to its shareholders, a feat that most of its customers have been unable to achieve.

Table 1: State Water's Profit \$'000

Year	05/06	06/07	07/08
Profit before income tax and superannuation actuarial gains/(losses)	12,963	9,829	(19)
Dividend	7,937	5,747	0

Specific Responses to Questions in the IPART Water – Issues Paper released in July 2010:

1. *The appropriateness of State Water's proposed service levels for the forthcoming determination period.*

GVIA is generally supportive of State Water's proposed service level.

GVIA's expectations are that State Water will be able to effectively manage the capture, release and delivery of regulated water; allocate and manage the sharing of supplementary flows whenever they become available; and maintain State Water's assets in a serviceable condition.

In carry-out the above tasks, GVIA expects that State Water always endeavours to do them in the most cost effective manner possible, and should always be seeking to make efficiency gains.

State Water has demonstrated over the past four-years that it is capable of achieving performance efficiencies, and while those achievements should be recognised and applauded, they should not result in State Water becoming complacent.

2. *The appropriateness of State Water's forecast operating costs for 2010 determination period, including the approach taken to allocate indirect operating costs (such as corporate overheads) between valleys.*

While GVIA is relatively happy with the level of service given to its member's by State Water, it is much harder for GVIA to make a definitive statement as to the appropriateness of the costs, as no comparative benchmarking information has been provided by either State Water or IPART.

In the absence of such information GVIA can only assume the efficient OPEX calculated for the last Determination, remains a valid starting base, but calls on IPART to carryout benchmark study of State Water’s costs.

A summary of State Water’s proposed operational expenditure for the Gwydir Valley is provided in the table below.

Table 2: Forecast Operational Expenditure Gwydir Valley (\$09/10) \$M

Activity	2009/10	2010/11	2011/12	2012/13	2013/14	Total
	3.612	3.869	3.884	3.859	3.911	19.135
Customer Support 100% User	.037	.038	.037	.036	.035	
Customer Billing 100% User	.036	.037	.036	.035	.034	
Metering and compliance 100% User	.229	.234	.230	.223	.218	
Water Delivery & Other Operations 100% User	.637	.671	.660	.640	.626	
Flood Operations 50% User	.055	.056	.055	.053	.052	
Hydrometric Monitoring 90% User	.540	.559	.567	.550	.538	
Water Quality Monitoring 50% User	.061	.062	.061	.059	.057	
Corrective Maintenance 100% user	.343	.321	.315	.306	.299	
Routine Maintenance 100% User	.879	.946	.939	1.013	1.144	
Asset Management Planning 100% user	.358	.365	.359	.348	.340	
Dam Safety Compliance 50% user	.213	.220	.219	.226	.216	
Environmental Planning Protection 50% User	.043	.175	.224	.194	.180	
Renewal & Replacement 90% User						
Insurance 100% User	.181	.185	.182	.176	.172	

Recommendation 1: IPART commission a study of State Water’s Operational Expenditure, benchmarking its performance against similar efficient businesses.

GVIA strongly argues that all businesses today must continually seek to achieve efficiency savings, and it is not acceptable for State Water to argue that it needs two years to consolidate its gains to date, prior to achieving further efficiencies.

GVIA believes particular attention should be given to the cost of services out-sourced by State Water – especially the hydrometric services.

GVIA understands that State Water is to seek cost reductions from the NSW Office of Water (NOW) for its hydrometric services, but believes IPART should independently assess the efficient costs of this service.

Recommendation 2: IPART independently assess the cost efficiency of the hydrometric service information provided to State Water by NOW.

GVIA is somewhat concerned by the way State Water has chosen to demonstrate its costs, choosing to quote a largely stable Baseline OPEX, but then add significant real cost increases under the line item of Thematic Expenditure.

GVIA is highly dubious about the “new and additional” nature of this Thematic Expenditure, its need, its timing, and its relevance and value to users, and calls on IPART to intensely examine the justification for this expenditure.

GVIA’s specific concerns are summarised as follows:

- a. ***Works Approvals:*** GVIA concedes that State Water is subject to the same works approval regime as irrigators, but does question whether the costs being applied to State Water by NOW are efficient, and in particular believe a discount should be applied due to the volume of the work.

Recommendation 3: That IPART evaluate the efficiency of the Work Approval costs being applied by NOW to State Water, and in particular the justification for a discount to be applied in recognition of the volume of work from a single client.

b. Environmental and Heritage Thematic Plan

- i. ***EMP Implementation*** – State Water’s Interim Operating Licence first issued in July 2004, required State Water to develop and report against its Environmental Management Plan, with its first report required by July 1, 2005. Therefore the cost of the EMP must have been included in the last Determination, and therefore form part of the Baseline OPEX.

Recommendation 4: That EMP Implementation expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

- ii. ***Environmental and Heritage Assessment Procedures*** – While State Water may have recently developed a set of procedures to ensure the consistent application of environmental legislation, this does not mean that State Water was not obliged to comply with this legislation in the past, and therefore the cost of complying was built into the Baseline OPEX. State Water should

be congratulated for developing a consistent procedure, but this should lead to improved efficiency and reduced costs, rather than lead to additional costs to be borne by users.

Recommendation 5: That Environmental and Heritage Assessment Procedures expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

- iii. *Fish Passage Program* – By State Water’s own admission (3-12) this program integrates two existing programmes, and therefore should once again lead to efficiencies rather than additional costs.

Recommendation 6: That the Fish Passage Program expenditure be removed from new Thematic Expenditure, and be recognised as part of the baseline expenditure.

- iv. *Heritage Management Programme* – Heritage Management activities should be deemed to be a legacy cost and therefore a 100% Government Cost, given that the assets requiring protection were in place before the 1997 “line-in-the-sand”. In addition, the protection of heritage assets provide no benefits to users (and will potentially increase costs), and is been driven entirely by government, and therefore should be paid for by government.

Recommendation 7: Heritage Management Expenditure should be a 100% Government cost.

- v. *Water Quality Programme* – In all but the most extreme circumstances, water quality is a no-issue for irrigator users. The most common water quality issue that can be addressed to a greater or lesser degree through water storage management is blue-green algae.

Blue-green algae is not a commercial problem for irrigators, although it may impact on other paying customers such as town water supplies and domestic and stock customers, and non-paying users such as those that benefit from replenishment flows, riparian rights and recreation users.

Therefore, if this is genuinely new expenditure, and there must be some doubts about that as State Water has always had to manage its water quality, then the cost should either be borne directly by government as a transparent payment, or a differential pricing structure should be developed for urban water supplies, and domestic and stock customers.

Recommendation 8: That water quality program expenses be paid for directly by government, or a differential pricing structure be developed that levies this cost onto urban, and domestic and stock customers.

- c. ***Dam Safety Thematic Plan*** – GVIA believes this expenditure can be deferred as State Water will be fully committed to a whole range of Dam Safety upgrades over the next decade that have been dictated to it by the requirements of the Dam Safety Committee. It therefore appears unlikely that State Water will have any real demand for further updated assessments in the short to medium term.

In addition, if the expenditure is deemed by IPART to be justified, GVIA is concerned that a component of such work must already be included in the Baseline OPEX, and even if it is not, as the results of such studies is likely to be used in the assessment of Dam Safety Upgrade requirements, then any additional cost should be absorbed by the Dam Safety Upgrade Capital programme.

Recommendation 9: That the Dam Safety Thematic Plan expenditure should be deferred, but if not, IPART must first ensure that it is not already been accounted for in either OPEX or Dam Safety Capital, and if it is genuine new expenditure it should be applied to Dam Safety Upgrade Capital expenditure.

- d. ***Research*** - GVIA commends State Water for taking a pro-active approach to ensuring it has available to it the appropriate skill sets it will require into the future.

However, GVIA believes it would be more appropriate for this expenditure be deferred until after State Water returns to improved profitability, and it should be funded out of profits, rather than from operational expenditure, as the expenditure will have no immediate value to current State Water customers.

Recommendation 10: That the research expenditure be funded out of profits.

- e. ***Land Management Thematic Plan*** – Again it appears highly likely to GVIA that this expenditure has already been accounted for as part of the Baseline OPEX.

However, if IPART determines it is genuine new expenditure, then State Water should fund it through its unregulated business activities, as State Water recognises (3-14) the plan is likely to be used to drive new unregulated business activity such as increased grazing leases, wind farm developments and carbon sequestration opportunities.

Recommendation 11: That Land Management Thematic Plan Expenditure, if assessed by IPART to be genuine new expenditure, should be funded by State Water's unregulated business activities.

- f. ***Emergency and Security Thematic Plan*** – Given that State Water’s drivers for this planning is global terrorist activity as evidenced by the Bali bombings and the like (3-15), GVIA contends that this should be whole of government expenditure, funded by either State or Federal Government, in the same manner as airport or sea port security.

GVIA is aware that Federal money was available to local government to upgrade regional airport security, and believes this would be an appropriate funding source for State Water.

Recommendation 12: That the Emergency and Security Thematic Plan be viewed as a community cost, and funded directly by State or Federal Government.

g. Corporate

- i. ***Data Cleansing*** – GVIA contends that this is a standard cost of doing business, and therefore is an activity built into Baseline OPEX.

Recommendation 13: That data cleansing be recognised as part of Baseline OPEX.

- ii. ***Interstate Tagging*** – GVIA contends that this is being driven by National Water Reform, and therefore the costs should be recoverable through the Commonwealth National Water Market Systems programme.

Recommendation 14: That the cost of developing an interstate tagging system should be recovered through the National Water Market Systems programme.

- iii. ***Multiple Water Sources*** – GVIA supports State Water’s submission in this regards.
- iv. ***OH&S Audits*** – This is a core business function and therefore would have been included in Baseline OPEX.

Recommendation 15: That OH&S Audits be recognised as an ongoing requirement, and therefore accounted for in Baseline OPEX.

- h. ***Discretionary Service Levels*** – GVIA supports State Water’s position in regards to the discretionary services recommended by the Gwydir Valley Customer Services Committee.

3. Whether there is scope for State Water to achieve further efficiency gains over the 2010 determination period?

State Water has identified in its submission some scope for further efficiency savings, and the organisation should be congratulated for this. However, no

business in Australia can survive today without ongoing efficiency gains. There is no better example of this, than the industry State Water primarily serves – agriculture.

Agricultures terms of trade have continually declined over many decades, and the only way agricultural industries survive is through the continuous achievement of efficiency gains through the adoption of new technology and techniques.

It is up to management to identify where and how the savings should be made. But IPART should be dictating a 3% annual efficiency savings, which should lead to a gradual decrease in real prices, and maintain actual prices at close to the opening levels.

To some extent IPART needs to be cautious that State Water does not replace efficiency savings made on OPEX, by simply increasing capital expenditure, and therefore increasing the RAB and the consequential return flowing through to prices.

GVIA would suspect that there are significant efficiency gains that can be made on hydrometric services, routine maintenance, flood operations and river operations.

4. The information provided by State Water on its past and forecast capital expenditure, and the prudence and efficiency of this expenditure?

As with operational expenditure, it is outside of GVIA's expertise, to be able to provide detailed commentary on the efficiency of capital expenditure. However, as the table below details, State Water is planning an ambitious capital expenditure programme in the Gwydir Valley over the next Determination period.

GVIA believes IPART would be warranted in commissioning a study on the efficiency of these budgeted project costs. As a close observer of State Water's operations GVIA is concerned that State Water is inclined to invest in "gold-plated" capital projects, rather than more commercially engineered projects and as users we must shoulder our share of those costs.

With regards to prudence, GVIA does not believe the Dam Safety Upgrade is in anyway commercially justified. However, GVIA does concede that State Water is largely subject to the directions of the Dam Safety Committee in this matter.

GVIA notes significant expenditure has been flagged under the Environmental Planning and Protection line-item, and can only assume this may be work associated with cold water pollution control.

If this is the case, GVIA strongly questions whether State Water is capable of carrying out this work during this Determination Period as it has not been discussed at any more than a very general level at the Gwydir Valley Customer Service Committee, to GVIA's knowledge no significant planning or design work has been

carried out, and State Water will be very heavily committed to carrying out its Dam Safety Upgrade work over the Determination Period.

Therefore, GVIA believes IPART needs to pay particular attention to the prudence and likelihood of this work being carried out, with the view to removing it from State Water's capital expenditure programme for this Determination Period.

Recommendation 16: IPART closely assess the prudence, and likelihood of State Water carrying out its budgeted for Environmental Planning and Protection work, with the view to removing it from State Water's regulated capital expenditure budget.

As raised later in this submission, GVIA is concerned about the cost sharing of the fish passage works which will be triggered by this upgrade

Table 3: Forecast Capital Expenditure (\$09/10) \$M

Activity	2010/11	2011/12	2012/13	2013/14	Total
	11.90	25	15	10.1	62.1
Dam Safety (pre 1997) 100% Govt	11.19	22.57	6.83	0	40.59
Structural and other Enhancements 100% User	.03	0	0	0	.03
Environmental Planning and Protection 50% User	.10	2.2	8	10	20.3
Flood Operations 50% User	.08	0	0	0	.08
Water Delivery & Other Operations 100% User	.55	.28	.15	.14	1.12

Recommendation 17: That IPART commission a study of the efficiency and prudence of State Water's capital expenditure, and this study includes a benchmarking component against similar efficient organisation.

5. An appropriate rate of return to apply on State Water's RAB and the means of estimating this rate?

There is a very real argument as to whether any rate of return should be applied to the State Water RAB.

NSW Irrigators are competing against irrigators in South Australia who do not pay any bulk water charges at all.

As businesses, NSW irrigators are competing against other NSW businesses that enjoy the advantages of significant public transport infrastructure that are provided to them and their employees at a price that fails to even fully recover operational expenditure, let alone provide a return on assets.

However, GVIA concedes that there is a political reality that means IPART must include a rate of return on the regulatory asset base. In the last Determination IPART chose to apply the same rate of return (6.5%) as was applied to Sydney Water.

GVIA notes that State Water in its submission has called for a higher rate of return (7.9%), on the basis that it believes its business is inherently more risky than a business like State Water.

GVIA does not have the technical skills to enter into an economic debate on the relevant Weighted Average Cost of Capital (WACC) parameters, but it does believe the following deserves noting by IPART.

State Water points to its delivery volumes over the past Determination period as evidence to the riskiness of its business.

GVIA concedes that the State Water business is more volatile than Sydney Water, but does not agree that it is intrinsically more risky.

While Sydney Water has a stable customer demand pattern, not varying widely from the average, State Water has both upside and downside volatility, effectively cancelling out a lot of State Water's perceived revenue risk.

IPART would be wise not to focus too closely on the past Determination period in regards to volume of water sales, but must consider the long-term volatility that provides State Water with just as much opportunity for over-recovery as under-recovery.

Continuous accounting and carry-over provisions protect State Water from any risk that maybe imagined from over-supply. Should there in any one year be a surplus of water available, it will be held over to future years, preserving that revenue for State Water.

State Water also puts forward a of nonsense type argument with regards to its risks.

It claims that not only is it subject to supply-side risks (more correctly put as both upside and downside volatility), but it is also subject to demand-side risk (5-10).

State Water argues that global financial conditions impact on irrigators decisions. GVIA contends that there is no evidence that global financial conditions lead to any reduction in demand. Irrigators may adjust cropping mixes due to global market fluctuations, but they will still use whatever water is available to them.

GVIA is concerned that one of State Water's drivers for a higher WACC is that it believes its credit rating is at risk, but this appears to be a self-perpetuating issue.

As GVIA understands it; State Water largely funds its capital program through State Government borrowings, as these borrowings increase, further pressure is placed on State Water's credit rating; to help protect its credit rating State Water

wishes to apply a higher WACC; while the capital expenditure has been largely driven by the Dam Safety Committee that requires a level of safety well and truly above what a commercial business would require.

GVIA does not believe its members should be burdened with a higher WACC, to protect a credit rating, that is being put at risk by Dam Safety Committee recommendations and the State Government's borrowing policies.

GVIA is also very concerned that the State Government is getting a double return out of State Water; borrowing money at the Government risk free rate, then on-lending it to State Water, which has to pay a return-on capital based on the commercial interest rate.

GVIA believes IPART needs to consider State Water's WACC in the context of it being just one asset in a portfolio of assets controlled by the State Government.

While State Water may experience revenue volatility as a stand-alone organisation, its impact on the State Government's bundle of assets is very minor.

Just as individual investors are encouraged to minimise risk by having diverse portfolios, the State Government minimises its risk by its diversity, and therefore can afford a lower, but overall stable rate of return.

GVIA also wishes to make it very clear to IPART that it does not like State Water's implied threat that if it is not awarded a higher WACC, it will implement a 90% fixed 10% usage charging regime.

The 40% fixed / 60% usage regime allows State Water to share the economic cycles of its customer base, and is a critical reminder to it of the position of its customers.

IPART needs to also consider the significantly lower global interest rate regime that is in place now, compared to 2006, which should lead to a lower WACC being applied.

Recommendation 18: That IPART apply a WACC no greater than 6.5%, and prevents any attempt by State Water to move away from its 40%Fixed / 60% Usage tariff system.

6. Whether it is appropriate to address State Water's revenue risk by adjusting the WACC?

This issue has been largely dealt with in the previous response. However, to summarise, GVIA contends that State Water has made no argument that justifies that it faces sustained revenue risk, and therefore revenue risk does not represent a sound reason for increasing the WACC.

7. *The implications of transferring pricing responsibility from IPART to the ACCC for the Murray Darling Basin and any transitional arrangements that IPART might put in place to ensure a smooth transition?*

GVIA remains committed to the IPART process, and believes that if the ACCC remains responsible for future price determination processes, then IPART should seek to carry-out the Determinations under licencing from the ACCC.

GVIA notes that the Federal Minister for Water Penny Wong has called on the ACCC to provide her with more advice on this and related matters.

8. *The appropriateness of State Water's proposed approach to depreciation, asset classes and lives?*

GVIA is surprised that State Water has decided to adopt a single depreciation life-span for all its assets. It believes it would have been more appropriate to depreciate assets in accordance with their actual useful lives.

However, GVIA is aware of State Water's assurances that its proposal will have no net impact, and therefore calls on IPART to independently verify State Water's claim, and if found valid, GVIA will accept State Water's position.

Recommendation 19: That IPART independently assess State Water's claim that its proposed adjustment to asset lives for depreciation purposes will have no net affect.

9. *Appropriate output measures for the 2010 determination period. These should be aligned to projects or activities that State Water plans to undertake over the forthcoming determination period.*

GVIA believes that it is critically important that State Water reports to IPART on an annual basis, and that IPART has the ability to revise down State Water's prices if State Water fails to make the expenditure allowed for under the IPART process.

GVIA is particularly concerned about capital expenditure. While State Water believes it will meet or slightly exceed its total allowed-for capital expenditure for the current Determination period, it has demonstrated in its submission (4-2) that it has experienced a very high degree of annual variation from forecast.

This is an issue for GVIA, as the annual RAB, and consequentially pricing, is determined by the forecasted expenditure, and over the past Determination irrigators have been paying prices that were in part based on proposed capital expenditure that did not occur in the year it was meant to occur in.

GVIA is particularly interested in this issue, given the very significant safety upgrade, fish passage and cold-water pollution remediation works that have been budgeted for in the Gwydir over the next Determination period.

The reporting should be broken down to a valley-level, with valley-level adjustment of prices.

Recommendation 20: That IPART receive an annual report from State Water on expenditure, and any under expenditure of capital should result in a RAB adjustment and a consequential adjustment to the following year's prices.

In addition GVIA believes IPART should closely monitor State Water's performance indicators, to ascertain whether any OPEX savings are being made at the expense of service delivery. GVIA would recommend using the performance indicators currently used internally by State Water.

Recommendation 21: That IPART receive an annual report based State Water's internal performance indicators, and monitor the results against State Water's operational expenditure.

10. The usefulness of valley based reports.

GVIA values the valley-based business reports, and is confident that their value will increase overtime as GVIA gains a better understanding of the financial aspects of the State Water business in the Gwydir Valley.

11. Whether the cost sharing approach used in the 2006 Determination remains appropriate.

GVIA is confused by State Water's approach to cost shares in its submission. It proposes no changes to cost shares (7-3), but then strongly suggests that IPART revisit the rationale for the allocation of cost shares (7-5).

GVIA believes that cost shares have been vigorously debated over the past few Determinations, and that they should be largely maintained. However, should IPART choose to re-examine Cost Shares GVIA will be putting forward vigorous arguments for changes to the following; hydrometric monitoring, public liability insurance, flood control and asset management and replacement.

With regards to the present cost shares, GVIA requests that IPART recognise Environmental Planning and Protection activities involving Fish Passage works be a 100% Government charge, if those works are required because they have been triggered by Pre-1997 Dam Safety Compliance works.

For example, in the Gwydir Valley pre-1997 Dam Safety Compliance work over the new Determination period will see \$47.2m (100%) of expenditure, but it will also trigger \$5m (50% User) worth of fish passage works.

The fish passage works are only required because of the Dam Safety works; works which will provide no commercial benefits to users; therefore GVIA strongly argues that such works should be seen as part of the total the Dam Safety upgrade and allocated accordingly.

Recommendation 22: That when fish passage work requirements are triggered by Pre-1997 Dam Safety Upgrades, the fish passage costs should be included as part of the Upgrade costs and allocated accordingly (100% Govt).

12. State Water's consumption forecasts, as outlined in its submission.

GVIA emphatically rejects State water's proposed new water consumption model which would result in a 10.9% fall in the Gwydir forecasted consumption, and a consequential and significant increase in the usage component of the Gwydir charges.

Despite State Water commissioning the Centre for International Economics (CIE) to provide a report documenting justification for change and the proposed alternative model, it has gone way beyond accepted science in recommending this model.

If IPART accepts State Water's proposal, it is in effect accepting that climate change is here and now, and it has already had a 10% impact on river water availability.

This flies in the face of the most comprehensive study of climate change implications for the Murray-Darling Basin that was conducted by the CSIRO, on behalf of the Federal Government.

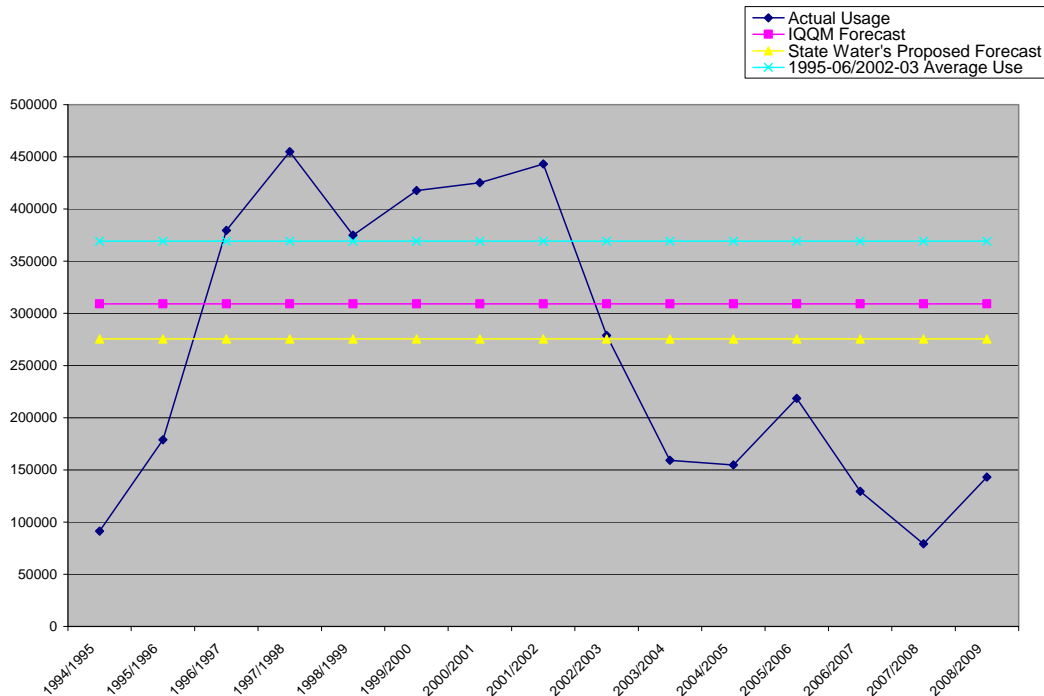
The CSIRO study, "Water Availability in the Gwydir – A report to the Australian Government from the CSIRO Murray-Darling Basin Sustainable Yields Project" considered a range of likely climate scenarios for 2030, and used 15 different climate change models. While GVIA has some well documented reservations about the CSIRO report, it has been widely accepted by government as the best information available on the likely affect of climate change in the Murray-Darling Basin.

The report concluded that in the Gwydir future surface water availability could increase by 34%, reduce by 29%, but using statistical analysis it was most likely to decrease by 10%.

Given the wide variance in CSIRO's predictions, and remembering that the predications are based on likely climate scenarios in 2030, it is very hard accept State Water's and CIE's conclusion that it can confidently expect a 10% decrease in expected consumption in 2010-2014.

GVIA and its members can well appreciate that during this current drought cycle it is hard for State Water to be bullish about future consumption, however, one does not have to look too far into the Gwydir past when average consumption was well above the current IQQM Forecast model, as demonstrated in the chart below.

Figure 1: Gwydir Water Use 1994-2009



While GVIA concedes that since 2003/04 consumption has been significantly below both the long-term IQQM forecast and the proposed State Water forecast, likewise the period from 1996/97 to 2002/03 was well above both forecast lines.

What this graph clearly demonstrates is the volatile nature of water availability/consumption in the Gwydir Valley, and if the period from 2004 represents a step change down in availability, then it must be equally valid that the period from 1996 to 2002/03 represented a step change up.

The truth of the matter is that State Water's business is a long-term business, that is affected by natural climatic cycles, and the only fair average measure of that variation is the long-term IQQM model.

Should IPART accept State Water's proposed model, there would be a very real risk of State Water over recovering both through additional sales, and inflated usage charges brought about by the adoption of its model.

Climate change may be real, and, if so, it will be picked up by changes to the IQQM over time, at a rate that will roughly match any actual changes.

The State Water proposal tries to superimpose what might be 2030 climate conditions onto 2010, and in doing so dramatically reducing its revenue risk, not by magically eliminating it, but by passing it on to its customers, and that would fundamentally change the accepted risk sharing equity between State Water and its customers.

Recommendation 23: That IPART continue to use the long-run IQQM data as the basis of its consumption forecast model.

13. The implications for prices and for State Water's financial viability of continued reduced water availability.

This question should equally ask - what is the impact on State Water's financial viability of increased water availability?

As discussed in the previous section, there is no evidence to suggest the consumption patterns of the past four years will be repeated over the next four years.

State Water is concerned with under recovery of revenue and its customers, including members of GVIA, are concerned with over recovery.

It is worthwhile considering which of the two parties is in the better position to wear the risk – irrigators who are effectively small to medium business, or the shareholders of State Water who are effectively the NSW Government.

State Water's clear policy is that 70% of its profits are returned to Government in the form of dividends. Should State Water over recover, irrigators are in no doubt that the vast majority of that money will not be either returned to them, or at the very least retained by State Water to fund revenue shortfalls in future years.

Should State Water under recover, then it has the backing of the substantial earning and borrowing power of the NSW government, including access to finance at a rate significantly below that available to irrigators.

State Water does face revenue volatility, as does its customers, but by any assessment State Water is in the stronger position to manage that volatility.

14. The appropriate approach to translate user's share of the revenue requirement into State Water's prices.

GVIA believes the user shares revenue requirement should be reflected in State Water's prices by the appropriate application of a formula that includes the following components:

- a. A maximum revenue recovery of 40% fixed from fixed charges.
- b. A appropriate High Security/General Security ratio which accurately reflects the costs involved in delivering High Security water (Further detail on a proposed model is provided later in this submission)
- c. A minimum recovery of 60% through usage charges
- d. The consumption forecast component of the Usage charge to be based on the long-run IQQM model (Gwydir 309,164 megalitres)

Recommendation 24: State Water prices should reflect the following factors in terms of how to equitably recoup user shares:

- a. ***Maximum 40% fixed component***
- b. ***Minimum 60% usage component***
- c. ***An equitable High Security/General Security ratio (As proposed by GVIA later in this submission)***
- d. ***The use of the long-term IQQM Consumption forecast***

15. What transitional path and rate of increase is reasonable for prices in valleys where prices are not yet at full cost recovery.

GVIA suggests that those valleys not at full cost recover should be subject to price rises equal to, in percentage terms, to the highest price rises being applied to those valleys already deemed to be at full cost recovery. Any transitional path at levels lower than this would be inequitable to those valleys already at full cost recovery.

Recommendation 25: Valleys not at full price recovery should be subject to price rises equal to the maximum price rise being faced by a valley deemed to be at full cost recovery.

16. Options for meeting the cost of providing water in valleys in which cost reflective prices may not be practical.

GVIA is strongly opposed to any cross-subsidisation across valleys, and therefore suggest the only way of meeting the cost of providing water to those valleys where cost reflective pricing is not practical is through a clearly identified Community Service Obligation (CSO) payment made by the NSW Government.

Any action that would see State Water denied revenue from a particular valley on the basis of non-cost reflective pricing, and not supported by a CSO payment would in effect be cross-subsidisation by the other valleys serviced by State Water.

Recommendation 26: That any planned shortfall in revenue from a valley, because cost reflective pricing is deemed impractical, should be compensated by a fully funded government CSO payment to State Water.

17. The appropriate balance between fixed and usage charges.

As stated earlier, GVIA is strongly supportive of a minimum usage charge component of 60%. The correct fixed:usage balance allows State Water and its customers to share both upside and downside business risk, and this has been long recognised by State Water and IPART.

Over the past 4 year's irrigators have been faced with very low and even zero allocations, meaning farm activity and consequential profit performance has been severely impacted, and yet irrigators have had to meet their fixed water pricing charges.

The following tables demonstrate Gwydir Valley allocations (including supplementary access) over the past 4 years, and the impact the 40% / 60% tariff has on the price per actual megalitre received, compared to the alternative structure 90% / 10% tariff proposed by State Water if it does not get awarded its preferred WACC of 7.9%.

Table 4: The real cost per megalitre for each megalitre delivered in the Gwydir Valley (Proposed 2010/11 Prices - 40% Fixed / 60% Usage) *

Year	GS Security Usage	Supplementary Usage	Total Usage	Effective Allocation	Total Fixed Charge	Total Usage Charge	Total Charges	Cost per megalitre of real water
2006/07	114,038	434	114,472	22%	\$1,793,440	\$1,274,595	\$3,068,035	\$26.80
2007/08	26,268	42,725	68,993	13.5%	\$1,793,440	\$766,512	\$2,559,952	\$37.10
2008/09	81,549	52,449	133,998	26%	\$1,793,440	\$1,488,718	\$3,282,159	\$24.49
60% Allocation/Usage			305,700	60%	\$1,793,440	\$3,396,327	\$5,189,767	\$16.97
100% allocation/usage			509,500	100%	\$1,793,440	\$5,660,545	\$7,453,985	\$14.63

* Assumptions – Fixed GS Charge \$3.52/meg Usage Charge \$11.11/meg

Table 5: The real cost per megalitre for each megalitre delivered in the Gwydir Valley (Proposed 2010/11 Prices – 90% Fixed / 10% usage) *

Year	GS Security Usage	Supplementary Usage	Total Usage	Effective Allocation	Total Fixed Charge	Usage Charge	Total Charges	Cost per megalitre of real water
2006/07	114,038	434	114,472	22%	\$4,035,240	\$211,773	\$4,247,013	\$37.10
2007/08	26,268	42,725	68,993	13.5%	\$4,035,240	\$127,637	\$4,162,877	\$60.33
2008/09	81,549	52,449	133,998	26%	\$4,035,240	\$247,896	\$4,283,136	\$31.96
60% allocation/ usage			305,700	60%	\$4,035,240	\$565,545	\$4,600,785	\$15.05
100% allocation/usage			509,500	100%	\$4,035,240	\$942,575	\$4,977,815	\$9.77

* Assumptions – Fixed GS Charge \$7.92/meg

Usage Charge \$1.85/meg

It is clear from the above tables that the 40% Fixed / 60% Usage tariff structure gives irrigators some protection during periods of low allocation, when their capacity to pay is also at the lowest, and offers considerably revenue upside for State Water when consumption is high, while the 90% Fixed / 10% Usage tariff has the opposite effect.

The 40% fixed / 60 % usage tariff shares the risk as equitably as possible, and recognises that irrigators are more susceptible to the risks associated with low allocation years, but have the capacity to pay a revenue premium to State Water in high allocation years.

Recommendation 27: That at the very minimum IPART maintain a maximum Fixed Charges revenue component of 40%.

18. The impact of State Water’s proposed prices on its customers.

GVIA members recognise that it is appropriate that they pay for the fair and reasonable costs incurred by State Water of capturing and delivering water.

However, they are becoming increasingly perplexed at how State Water can continue to demand real price rises when the valley has been deemed to be at full cost recovery.

State Water’s attitude that it should be immune from business risk, and utilise its monopoly position is not acceptable to the GVIA membership.

That State Water has managed to deliver a profit during the past four years is not only a testament to the rebuilt State Water management team, but it also demonstrates that State Water is not a fundamentally risky business, and it is extremely hard to accept any argument for price increases that exceed CPI. Indeed, IPART should be setting prices of CPI – Efficiency Gains.

The following tables identify the extent of the prices rises being sought by State Water for the Gwydir Valley.

Table 6: State Water's Proposed Gwydir Prices

	2009/10	2010/11	2011/12	2012/13	2013/14
High Security Entitlement Charge					
Charge (\$ 09/10)/meg	6.08	11.54	11.70	12.17	13.16
Actual Change		5.46	.16	.47	.99
% Change		90%	3%	4%	8%
Cumulative Change %		90%	92%	100%	116%

	2009/10	2010/11	2011/12	2012/13	2013/14
General Security Entitlement Charge					
Charge (\$ 09/10)/meg	3.37	3.52	3.57	3.71	4.01
Actual Change		.15	.05	.14	.30
% Change		4%	1%	4%	8%
Cumulative Change %		4%	6%	10%	19%

	2009/10	2010/11	2011/12	2012/13	2013/14
Usage Charge					
Charge (\$ 09/10)/meg	8.96	11.11	11.27	11.71	12.67
Actual Change		2.15	.16	.44	.96
% Change		24%	1%	4%	8%
Cumulative Change %		24%	26%	31%	41%

All prices will be adjusted annually for CPI.

The impact of these proposed prices can be best demonstrated by looking at the impact they will have on a customer's annual bill, based on a 1000 megalitre General Security entitlement and varying levels of allocation/usage.

Table 7: High Security Water Bill (\$) - 1000 megs Entitlement / 90% usage

	2009/10	2010/11	2011/12	2012/13	2013/14
Annual Water Bill	14,144	21,539	21,843	22,709	24,563
Actual Change		7,395	304	866	1854
% Change		52%	1%	4%	8%
Cumulative Change		52%	54%	60%	74%

Total bills will also have to be adjusted for CPI

Table 8: General Security Water Bill (\$) – 1000 megs Entitlement / 90% usage

	2009/10	2010/11	2011/12	2012/13	2013/14
Annual Water Bill	11,434	13,519	13,713	14,249	15,413
Actual Change		2085	194	536	1164
% Change		18%	1%	4%	8%
Cumulative Change		18%	20%	25%	35%

Total bills will also have to be adjusted for CPI

Table 9: General Security Water Bill (\$) – 1000 megs Entitlement / 60% usage

	2009/10	2010/11	2011/12	2012/13	2013/14
Annual Water Bill	8,746	10,186	10,332	10,736	11,612
Actual Change		1140	146	404	876
% Change		16%	1%	4%	8%
Cumulative Change		16%	18%	23%	33%

Total bills will also have to be adjusted for CPI

Table 10: General Security Water Bill (\$) – 1000 megs Entitlement / 30% usage

	2009/10	2010/11	2011/12	2012/13	2013/14
Annual Water Bill	6,058	6,853	6,951	7,223	7,811
Actual Change		795	98	272	588
% Change		13%	1%	4%	8%
Cumulative Change		13%	15%	19%	30%

Total bills will also have to be adjusted for CPI

Table 11: General Security Water Bill (\$) – 1000 megs Entitlement / 10% usage

	2009/10	2010/11	2011/12	2012/13	2013/14
Annual Water Bill	4,266	4,631	4,697	4,881	5,277
Actual Change		365	66	184	396
% Change		9%	1%	4%	8%
Cumulative Change		9%	10%	14%	24%

Total bills will also have to be adjusted for CPI

The above tables clearly indicate the impact on customer bills. The impact does vary on allocation levels, but at an average Gwydir Valley usage of 60% of entitlement (based on GS and supplementary usage) irrigators will be facing a massive 33% real increase in their water bills over the four year Determination period, including an 18% shock in the first year, in a valley that IPART has declared to be at full cost recovery.

Regardless of irrigators capacity to pay as either individuals, or as a group, such increases should not be granted simply on the basis that they cannot be justified, when a valley is already at full cost recovery, and State Water has not been able to identify any

significant extra costs, even though it has attempted to do so through its dubious thematic expenditure.

However, State Water has stated in its submission that the proposed prices rise will have relatively little impact on the profitability of Gwydir irrigators, and has used a very flawed argument that there should be some sort of relationship between the temporary price of water and the capacity of an irrigator to pay fixed charges - “the huge difference between State Water charges and the market price for water suggests that State Water charges are immaterial to the market value of water” (12-3). Not only is this argue flawed, it borders on being dishonest. It almost suggests that income derived from water is without cost, and completely ignores the opportunity cost of holding a water entitlement.

For example, consider the situation in the Gwydir where a megalitre of general security licence has been valued recently by the market at \$2411; has a long-term average allocation of 36%; and an average allocation in recent years of 10%; an average interest cost of 7%; and an average temporary assignment price of \$260 per megalitre.

The following table will demonstrate the average cost of owning megalitre of allocation.

Table 12: The average annual cost of a megalitre of GS in the Gwydir and profit from the annual assignment market

Allocation	Opportunity Cost @ 7% For entitlement Values at \$2400	Opportunity cost per meg of allocation	Annual State Water Charge per meg of allocation	Annual Cost of Ownership	Average price of an megalitre of assignment	Average profit
10%	\$168	\$1680	\$46.31	\$1726.31	\$260	-\$1,466.31
60%	\$168	\$280	\$16.97	\$296.96	\$260	-\$36.96
100%	\$168	\$168	\$14.63	\$182.63	\$260	\$77.37

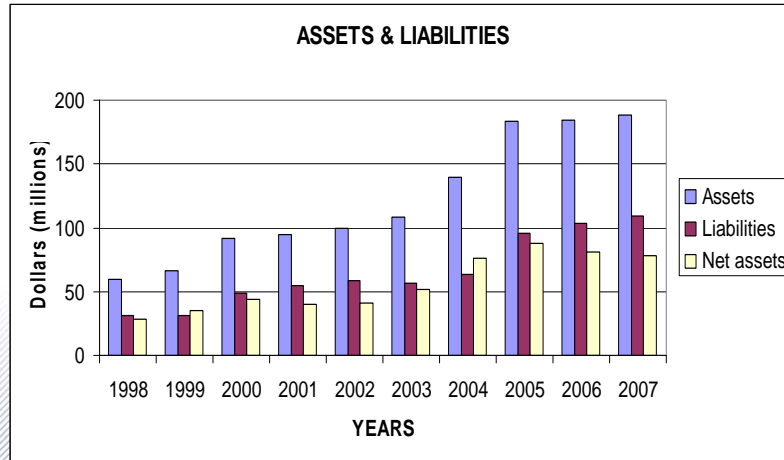
As the table clearly demonstrates when the opportunity cost of holding a licences is combined with the State Water charges, the annual costs in most years exceeds returns.

IPART should also consider the profitability of Gwydir Valley irrigation enterprise when assessing the impact of the increased prices may have on them.

The following charts have been prepared by independent accountants Boyce and Co Chartered Accountants and track the financial performance (in aggregate) over recent years of six of their medium to large size Gwydir Valley irrigator clients.

Figure 2: Aggregate of six Gwydir Valley Irrigated Cotton Growers Asset and Liabilities Performance

What have our growers done?



12

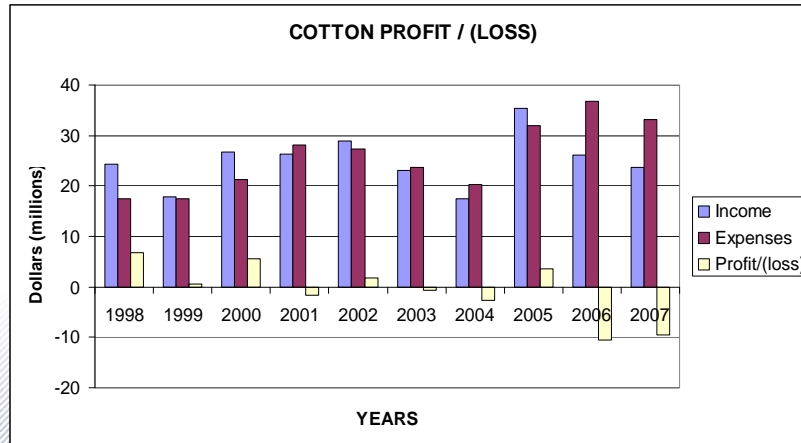
This chart clearly demonstrates that since the drought really started to bite in 2005 asset growth has stopped, while liabilities have increased significantly as growers have had to borrow because of profit shortfalls.

The next chart demonstrates the falling profitability of the cotton industry, not so much because of general lack of gross margin profitability, but because limited water availability has severely restricted growers’ abilities to plant enough area, to generate enough profit to cover overheads including fixed charges.

It is clear that any increase in charges, no matter how small, will only exacerbate Gwydir Valley irrigators already poor financial performance, which is being driven by the same factor impacting on State Water – a period of low water availability.

Figure 3: Aggregate of six Gwydir Valley Irrigated Cotton Growers profit performance

What have our growers done?



14

Recommendation 28: That IPART recognises the Gwydir Valley’s customer’s reduced capacity to pay, before approving any increase in State Water’s charges.

19. The appropriateness of introducing a mechanism, such as scarcity pricing, to address State Water’s revenue volatility; and a different sharing of revenue risks between irrigators and State Water.

GVIA is totally opposed to the introduction of any form of scarcity pricing, as it would be in effect a double application of scarcity principles, and would be outside of State Water’s charter to capture, store and deliver water, and the pricing principles laid down by the National Water Initiative.

While scarcity pricing may be an appropriate tool in urban water situations, where (outside water restrictions) there is no limit on how much water a consumer may choose to use, an irrigator is restricted by the entitlement he/she holds.

It is the entitlement that controls use, and scarcity pricing is already built into the value of the water entitlement, as demonstrated earlier in this submission.

As previously discussed GVIA believes the current 40% Fixed / 60% Usage tariff structure best shares the revenue risk between State Water and customers.

20. Whether there are any practical limitations that would need to be considered if a form of scarcity pricing was introduced.

Given GVIA's response to the previous question GVIA rejects any need to further discuss this issue.

21. The appropriateness of State Water's proposal to recover the cost of meter service provision.

GVIA supports in principle State Water's proposal to recover the cost of meter service provisions should the project proceed, but IPART should note that GVIA has not been convinced of the validity of the project, and nor is it confident that the project will proceed during the next Determination period.

However, should it proceed, GVIA believes the efficiency of the proposed costs needs to be carefully examined, and there needs to be some mechanism to ensure there is no "double collection" of metering charges, given the cost of providing metering services is already built into OPEX.

Recommendation 29: That IPART should examine the cost efficiency of State Water's proposed method of recovering cost associated with the servicing of meters rolled out under the possible metering project.

Recommendation 30: IPART should develop a framework to ensure no "double payment" metering fees, should the proposed metering project roll out during the next Determination period.

22. Whether consumers support the continuation of the Yanco Creek levy.

GVIA has no position or interest in this question.

23. Whether the consumers support the introduction of other levies.

GVIA has not considered, or been asked to consider any addition levies that would impact on its membership, and nor is it aware of any proposed levies.

24. Whether it is appropriate to maintain rebates to irrigation companies and districts (ICDs).

GVIA has no irrigation corporations or districts within its membership, nor is there any operating within the Gwydir Valley. On that basis, provide State Water and IPART

adhere strictly to a policy of no cross valley subsidisation then it has no position on the issue.

25. The level of these rebates, if appropriate, and the justification for this position.

GVIA has no comment on this question.

26. The appropriate balance between high security and general security entitlement prices.

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 13: 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 14: 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 Forecast	7.44	3.69	11.11	\$398,112	\$4,705,888	\$5,104,000
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.

Recommendation 31: 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).

27. The appropriate length for the 2010 determination period.

GVIA concurs with the State Water submission that the appropriate period for the 2010 Determination period is four years, providing irrigators with some price path certainty, without unreasonably locking customers into an extended price path.

Other Matters

User Definition

As raised in previous Determination submissions, GVIA remains very concerned about the narrow definition of “user”, and therefore the limited application of fixed and usage charges.

There is a whole range of government, commercial and recreational users of State Water’s services that do not contribute to meeting State Water’s revenue requirements.

GVIA understands and accepts that some of these users are hard to identify at an individual level, but others are not.

For example, apart from holding a large parcel of general security licencing as adaptive environmental water, the NSW government controls the 45,000 megalitre Environmental Contingency Allowance (ECA) which is captured and stored in Copeton Dam.

IPART needs to clearly understand that this allowance is not “owned” or “controlled” by State Water, but is in the control of the NSW Government, through the Department of Environment, Climate Change and Water (DECCW) an organisation completely independent from State Water.

State Water is obliged to capture, store and deliver that allowance, in accordance with DECCW’s instructions (just like any other customer).

DECCW’s objectives are not aligned with the objectives of State Water, so there can no longer be an argument that this allowance should be exempt from fixed and usage charges.

Recommendation 32: That IPART oblige State Water to charge DECCW fixed and usage charges on the ECA.

Similarly, State Water captures, stores and release up to 21,000 megalitres per year of replenishment flow water for landholders’ stock and domestic needs.

The release of this water is co-ordinated through local landholder groups, and is authorised by the NSW Office of Water.

This drought has clearly demonstrated that the Replenishment Water is providing landholders with a reliable supply, at a time when the rivers and creeks would normally have ceased to flow.

These landholders can be identified, or alternatively the NSW office of Water should be billed fixed and usage charges for these supplies.

IPART should clearly appreciate that these replenishment flows have the same security as high security and therefore the charge should be determined accordingly.

Recommendation 33: IPART should develop a price regime that recovers fixed and usage charges (at the high security rate) for replenishment flows water, and the charge should be levied either directly on the landholder beneficiaries or to NOW.

GVIA appreciates that it is harder and impractical to identify individual recreational users, and therefore suggest that a charge equivalent to 5% of the user revenue contributions for the Gwydir Valley be paid by the NSW Government as a clearly identified CSO payment on behalf of recreational users.

Recommendation 34: That the NSW Government be obliged to pay a CSO to State Water, equivalent to 5% of the Gwydir's user revenue share, on behalf of recreational users.

Government's responsibility to meet fix and usage charges on adaptive environmental water

GVIA understood that both the Australian and NSW Government had accepted its responsibility to pay fixed and usage charges on all Adaptive Environmental water. It was therefore when it read in State Water's submission (10-12) that the NSW Government was yet to finalise its position, but was thought to be supportive of paying the charges.

Since the government started to enter the permanent entitlement market for water for environmental use two years ago, industry has always understood that Government would pay its share of fixed and usage charges. Any move away from this would not only be a fundamental breach of trust, but would severely impact on the equity of irrigators, and the fundamentals of the water market.

Government water holdings should be viewed as no different to irrigator holdings, and the obligation on State Water to capture, store and release remain the same.

Therefore it is very important that in making its Determination IPART make a definitive statement that adaptive environmental water will be subject to the same charging regime as other entitlements.

Recommendation 35: That IPART in making its Determination make definitive statement that the holders of environmental adaptive water are subject to the same water charging regime as other water entitlement holders.

MDBA and BRC Pass Through Costs

GVIA notes that State Water intends to apply MDBA pass through costs to the Gwydir of between \$52,000 and \$66,000 per year.

As GVIA understands it State Water and the NSW Office of Water has come to an agreement to try and separate MDBA river operation costs from water management costs, and the MDBA costs allowed for in the State Water submission should only be river operational in nature.

GVIA contends that the Gwydir Valley should not be responsible for any of the MDBA operational costs and therefore they should not be considered when determine the prices for State Water's charges in the Gwydir Valley.

Recommendation 36: That IPART remove any allowance for MDBA pass through cost, when calculating State Water's total costs for the Gwydir Valley.

Supplementary Water

GVIA wishes to place an issue on notice for IPART to consider in future Determinations, if it continues to have such a role.

Currently, there is no fixed charge component on supplementary licences.

GVIA believes there is merit in closely examining this issue in future Determinations for the following reasons:

- i. There is a fixed cost component in managing supplementary licences.
- ii. There is no longer a direct linkage between supplementary licence and general security licences, which previously ensured access to supplementary/off-allocation/high flow was tied to levels of general security entitlement.
- iii. As trade continues, any historical link between general security and supplementary licences will diminish.
- iv. There are supplementary water entitlement holders who hold no High Security or General Security entitlement and are therefore not making any contribution to the fixed cost charging component of the current pricing regime.

GVIA is not proposing any increase in total charging, but believes an assessment of revenue neutral options could identify a more equitable balance between user revenue contributions.

Recommendation 37: That in the next Determination IPART fully consider the merits of establishing a fixed charge component for supplementary water.

Submission Concludes