INDEPENDENT PRICING AND REGULATORY TRIBUNAL

DRAFT REPORT - REVIEW OF PRICES FOR WATERNSW'S RURAL BULK WATER SERVICES

Tribunal Members
Dr Peter Boxall AO, Chair
Mr Ed Willett and Ms Deborah Cope, Members

Members of the Secretariat
Hugo Harmstorf, CEO, Matt Edgerton, Scott Chapman,
Elina Gilbourd, Chris Ihm, Shirley Dang and Jessica Forrest

SMC Conference Centre, 66 Goulburn Street, Sydney

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OPENING REMARKS

THE CHAIR: Welcome everybody and good morning. I would like to welcome you to this public hearing. We are conducting a review to determine the maximum prices that WaterNSW can charge for its monopoly rural bulk water services from 1 July 2017.

My name is Peter Boxall and I am Chair of the Independent Pricing and Regulatory Tribunal (IPART). I am joined today by my fellow tribunal members, Ed Willett and Deborah Cope. Assisting the tribunal today are members of the IPART secretariat, Hugo Harmstorf, who is IPART's Chief Executive Officer, Matt Edgerton, Scott Chapman, Elina Gilbourd, Chris Ihm, Shirley Dang and Jessica Forrest.

I would like to begin by acknowledging that we are meeting on the Gadigal land of the Eora people and wish to pay my respects to the traditional land owners, both past and present.

The purpose of today's hearing is to outline our key decisions from our draft report and draft determination which we released on 14 March. We seek your views on our draft decisions of the maximum prices that WaterNSW can charge for providing rural bulk water services. We have made draft decisions on:

WaterNSW's efficient costs of providing rural bulk water services;

The customer share of these costs; and

How the customer share of costs should be recovered through prices,

I would like to thank those who have participated in this review to date, particularly those who have provided a written submission in response to our issues paper which was released last September. WaterNSW's pricing proposal, our issues paper, the draft report and the draft determination are available on our website.

Today's public hearing will be webcast and questions may be submitted through the web to assist those who cannot make the public hearing in person.

This public hearing is an important part of our consultation process. In addition to the views expressed in written submissions, we will consider the views you provide today in making our final decisions on WaterNSW's prices for rural bulk water services.

We are seeking comments on all of our draft decisions. The closing date for written submissions is 17 April. Our final report and final determination are due for release in June 2017, which will set the maximum prices to apply from 1 July 2017.

Before we commence proceedings, I would like to say a few words about the process for this hearing. We will begin today's public hearing with a brief overview of the key decisions in this review to provide some context for the more detailed discussions to follow. Then, WaterNSW will give a brief overview of their proposal.

Following this, we will have four sessions, each focusing on particular key decisions, with a lunch break in between at about 12.00pm.

In the first session, we will consider the draft decisions on WaterNSW's expenditure, including operating expenditure, capital expenditure, and the approach used to allocate costs between customers and the government.

The second session will consider the costs of the Border Rivers Commission (BRC) and the Murray-Darling Basin Authority (MDBA) and our draft decisions on these costs.

The third session, after lunch, will consider our draft decisions on price structures and WaterNSW's approach to managing revenue volatility.

Finally, the fourth session will consider our draft decisions on valleys which are well below full cost recovery. At the commencement of this fourth session, I will invite stakeholders from the North Coast and South Coast valleys to join the roundtable.

Following the fourth session, there will also be an opportunity to hear your views on any other issues you wish to raise that are relevant to this review.

To begin each session, a member of IPART's secretariat will give a brief presentation introducing each topic. I will then invite participants at the table to provide comments on these topics. Following discussion by those around the table, I will then invite comments from those in the general audience.

As I mentioned, today's hearing will be webcast, recorded and transcribed. To assist the transcribers, I ask that on each occasion you speak to please identify yourself and, where applicable, your organisation before speaking. I also ask that you speak clearly and loudly. A copy of the transcript will be made available on our website.

I now call Scott Chapman from the IPART secretariat to give a brief overview of the key decisions and to provide some context for the more detailed discussions to follow.

OVERVIEW OF KEY DECISIONS

MR CHAPMAN: Thank you, Peter. My name is Scott Chapman. I am from the IPART secretariat. I am going to give a quick rundown and an overview of essentially the key issues that we will be talking about in more detail a little later on today and the tribunal's key draft decisions that led to our draft prices in out draft report and our draft determination.

The review started in June last year with WaterNSW's pricing proposal to us. We released an issues paper on 13 September last year and held a series of public hearings. There were three public hearings - one in Moree, one in Sydney, and one in Coleambally, in October and November. We took into account all stakeholder feedback between then and the draft report and we issued our draft report and our draft determination on 14 March 2017.

Today we are holding a public hearing here, simply in response to our draft decisions in our draft report and draft determination to allow stakeholders a further say on some of the draft decisions the tribunal has made.

Importantly, the closing date for written submissions, which we encourage all stakeholders to participate in, is 17 April - so a couple of weeks from today - and we intend to release our final report towards the middle of June 2017, following which our prices will take effect from 1 July.

Looking at our draft decisions, whilst there are a lot of nuances and many issues that we addressed in our draft report and draft determination, it really comes down to a story in three parts, and the first of those is expenditure and efficient costs.

The core costs of WaterNSW in operating this business are falling. That is largely, and primarily, a result of decreased and continually decreasing operating expenditure on WaterNSW's behalf. Our draft decisions will also result in further reductions in relation to revenue requirements, including return on capital, and these savings will flow through to most valleys, and most customers in most valleys will experience decreasing bills before inflation - not all customers, but most.

However, the Murray-Darling Basin costs, or the costs related to the Murray-Darling Basin Authority and, to a lesser extent, the Border Rivers Commission, are increasing significantly. This will put upward pressure on bills for the Murray and the Murrumbidgee and, to a lesser extent, the Border River and, in particular, to high security customers in the Murray.

Largely we have also made changes to price structures, and that is the third part of the story. We are considering making changes to tariff structures in the Lowbidgee Valley, the Fish River Water supply and, importantly, to the Border Rivers Commission and MDBA charges.

We have also updated the high security premium for the valleys, which is essentially the ratio in the fixed charges between the general security licence holder and the high security licence holder.

Our draft decisions on price structures would impact entitlement charges, particularly in the Gwydir, the Hunter and the Murray Valley, and, in particular, in the Murray to customers from the MDBA component of the bill and high security customers there.

In general, bills would increase at or below the rate of inflation in most valleys, both for high and for general security customers. But, of course, there are a few exceptions, the most notable of those are high security holders in the Murray Valley. The biggest reduction is for high security customers in the Hunter Valley, and that is largely as a result of both decreasing costs and greatly decreased high security premium in the Hunter Valley. For the high security customers in the Murray Valley, it is primarily about increases in the MDBA charge and how we have structured those costs. We will get to that later in sessions 2 and 3 today.

In comparison to WaterNSW's proposed prices, our bill impacts for most high security customers are generally lower. That is more often than not in most valleys a result of the changes to our high security premium and the draft decisions we made on that. However, as I mentioned a moment ago, the big stand-out here is the high security holders in the Murray Valley, and we will talk about that in much more detail later.

WaterNSW has proposed prices that remain largely constant, with a slight reduction for high security holders in the Murray. Our draft decisions lead to about a 35 per cent increase, including inflation, over the period of this determination.

For general security customers, it is a different story. Most of our general security bills are at or below the rate of inflation and are lower than WaterNSW's proposed prices, particularly in the Murray and the North Coast and South Coast, which we will talk about separately in the sessions here today.

General security customers in the Hunter will experience an increase rather than a decrease in bills, which were proposed by WaterNSW basically because we have made such a significant change in our draft decision on the high security premium in the Hunter.

That is essentially a summary in very broad terms of the key issues that we dealt with in the draft report and the draft determination and the key issues that we will be talking about in much more detail today and we are very keen to hear feedback from all stakeholders on those issues. Thank you.

THE CHAIR: Thank you very much, Scott. I now call on David Harris to give a short overview of WaterNSW's pricing proposal.

OVERVIEW OF WATERNSW'S PRICING PROPOSAL

MR HARRIS: Thanks very much, Peter, and good morning everyone.

Today's forum is being convened by IPART principally so that our customers can have the opportunity to be heard on the draft IPART determination. What I would like do in a couple of slides here, and not take too much time about it, is focus on the main features of our pricing proposal which we submitted to IPART a year ago.

I would also like to start by acknowledging the time and effort that our customers have put in to contributing to this process. It comes at a time when our customers are being dominated by other matters of water policy and water regulation, so we would particularly like to acknowledge and thank our customers for the effort that they have put in to this pricing determination process.

From our part, we believe that, during this process, in developing our pricing submission, we have demonstrated a huge improvement in our consultation process and, just as importantly, far more comprehensive information has been provided to our customers, in particular, a much improved transparency and knowledge sharing around tariff structure options and an increase in transparency and understanding as to WaterNSW's bills, including pass-through charges at other agencies, such as the Murray-Darling Basin Authority, over which WaterNSW has no control and that do have a material impact on our customer bills.

Our pricing proposal that we submitted to IPART contained a number of real positives for our customers. It demonstrated a business that is refreshed, customer responsive and, as acknowledged already by Scott in his opening remarks, a business that is efficient.

Our pricing proposal reflected a clear commitment to meet customer requirements and continued to drive efficiency gains. We have delivered, through that pricing proposal, some great outcomes for our customers in relation to our activities and costs. We have reduced operating expenditure over the period by 20 per cent compared to the current regulatory allowance, and a reduced revenue requirement over four years from our rural customers - that is 11 per cent lower than the revenue requirement under the current determination - resulting in reduced bills for WaterNSW customers. As Scott acknowledged in his opening comments, IPART has confirmed that WaterNSW's core costs are reducing.

We have also achieved a significant decrease in operating expenditure through a new lean and efficient organisation and through vigilance on the part of our new management team across all cost areas of our business.

Customer consultation outcomes: During the customer consultation process, we have agreed a number of things with our customers. We have agreed to further consult with them on issues they were concerned about that arose during the preparation or our pricing proposal. We have also agreed and committed with our customers to address a few complex issues, not in this pricing determination process but rather prior to our 20121 submission - those being: legacy asset issues; government water user share; our levels of service framework; and capital underspend holding costs.

We are also committed to provide our customers annually with more detailed information on the capital projects that we plan to undertake in each of the valleys and can I report on that, that we have just completed a roadshow across all customer service communities in relation to our FYA team capex plan and that has received broad support right across the state.

Just to recap, our proposal reflected customer choice. We included in our proposal that we supported customer service committee resolutions for retaining the overs and unders mechanism and nomination of preferred tariff structure by valley.

Other highlights of our proposal - we are committed to delivering products and services that meet customer preferences and requirements. Customers clearly indicated their preference for tariffs with a higher proportion of usage charges, as they value the correlation between income and outgoings.

We structured our pricing proposal on the basis of customer preference for continuing of the existing fixed variable tariff structure, except in the case of Fish River, and progressively delivered increased customer choice.

We also proposed the purchase of an insurance product to assist WaterNSW in managing revenue volatility arising from high variable tariffs. Customers responded positively to our refreshed consultation approach, overall efficiencies and services being delivered.

In summary, Mr Chairman, we are absolutely committed to being a customer responsive organisation and providing a range of choices to help meet the needs of our customers. We remain committed to maintaining real relationships with our customers through regular engagement and I think we have delivered on that over the last year in relation to this pricing proposal process.

Reduced operating expenditure of 20 per cent over the period has contributed to a reduced revenue requirement from customers of 11 per cent. On average, our proposal provided customers with a bill reduction of 4 per cent. Thank you very much.

THE CHAIR: Thank you very much, David.

SESSION 1: Draft decisions on expenditure and cost shares

THE CHAIR: We will now move on to session 1 of today's agenda and Elina from the IPART secretariat will introduce the discussion. Could I just remind you that this is a discussion on key draft decisions and analysis of WaterNSW operating costs, capital costs and proposed capital maintenance allowance, and we will also discuss our draft decisions on the share of these costs recovered from customers through prices. We are planning to discuss consideration of the BRC and MDBA costs in the next session, that's session 2. Elina.

MS GILBOURD: Thank you, Chair, and good morning everyone. I will start by talking about the notional revenue requirement, NRR, which reflects our decision of the efficient costs of delivering WaterNSW's monopoly bulk water services.

The NRR is built based on a number of draft decisions the Tribunal has made on expenditure and other allowances. The total NRR is allocated between customers and government through prices. Overall, our draft decision on WaterNSW's total NRR over the 2017 determination period is to set it at $426 million, 1.4 per cent below WaterNSW's proposal.

This graph shows the increases and decreases to WaterNSW's NRR resulting from our draft decisions. The main increases are due to an increase in the unders and overs mechanism - or UOM - allowance, because of our draft decision to discontinue the UOM and recover the remaining balance through prices in most valleys, and because of an increase in ICD rebates based on an adjustment to the calculation of the avoided cost to WaterNSW resulting from the activities of the irrigation corporations and districts.

The main decreases are a significant reduction in the volatility allowance. WaterNSW proposed purchasing a risk transfer product at a cost of $3 million per annum. Our draft decision was to reduce their revenue volatility allowance to less than $0.8 million per annum. We have also reduced their tax allowance.

This slide compares the annual notional revenue requirement based on our draft decisions to the annual notional revenue requirements set by the ACCC in its 2014 decision. The comparison is on an annual basis as the ACCC's decision was over three years and our draft determination would be for four years.

Our draft NRR is $5.1 million or 6.7 per cent per year lower than the NRR set by WaterNSW. As with the previous graph, some of our draft decisions have increased the NRR while others have decreased it. The main increases result from a higher UOM allowance and higher MDBA and BRC costs, and the main decreases result from WaterNSW's lower operating expenditure and lower ICD rebates compared to the ACCC's 2014 decision.

As already alluded to by Scott and David, operating expenditure has fallen significantly. We have only made two minor adjustments to WaterNSW's proposed opex based on advice from Aither, our expenditure review consultants. Both of these reductions relate to 100 per cent customer share activities.

First, WaterNSW proposed increasing its opex to develop a 20-year asset management strategy for each valley. This is the only material opex activity where WaterNSW forecast a significant increase in proposed operating expenditure. Aither recommended reducing the expenditure by $1.1 million, which was 30 per cent of the proposed expenditure on the item, as it found that the proposed costs were not efficient because they were based on preliminary estimates and did not incorporate potential synergies of undertaking similar tasks across valleys.

Second, Aither recommended a $0.4 million reduction in the allowance for supervisory control and data acquisition costs, which corresponded to a 25 per cent reduction it recommended for capex on the item.

Turning to capital expenditure - this was a slightly different story - WaterNSW proposed around $196 million for the 2017 determination period, which was a significant increase in expenditure from the current determination, particularly for renewals expenditure. Our draft decision sets WaterNSW's allowance for capital expenditure at just under $152 million, which is 23 per cent below WaterNSW's proposal. This reflects a reduction recommended by Aither of $21 million to WaterNSW's proposed general renewal expenditure and just over $12 million for sampled projects that did not fully satisfy prudence and efficiency tests.

It also reflects updated forecasts for Keepit Dam expenditure that were provided by WaterNSW.

Overall, our draft decisions have reduced the customer share of capital expenditure, compared to WaterNSW's proposal, by 21 per cent.

We also made a draft decision not to allow $3.2 million of fishway capex. The proposed expenditure was driven by dam safety works in the Namoi Valley which triggered a requirement under section 218 of the Fisheries Management Act. This regulatory requirement was initially to be met at the Gunidgera Weir in the Namoi Valley at an estimated cost of $9 million. However, WaterNSW proposed replacing the project with an offset in the Barwon Valley at a lower cost of $3.2 million. Aither found this to be prudent and efficient.

In principle, we support the offset approach as it seeks to discharge regulatory duties at least cost. While the project would be undertaken in the Barwon, the approach satisfies the "impactor pays" principle as the Fisheries Management Act requirement was triggered by works that benefit Namoi Valley customers.

However, our draft decision is not to allow the expenditure because WaterNSW had not consulted Namoi stakeholders before proposing the expenditure. This raises doubt about the timing of the project which was due to commence in the current financial year. IPART and the ACCC had also previously allowed fishway expenditure in the Namoi Valley, which was not spent.

We have, however, allowed $1.6 million in opex to fund planning, design and business case activities to develop a strategic fish passage program across a number of valleys.

I will now move on to how WaterNSW's costs have been allocated between WaterNSW customers and the New South Wales government.

Our draft decision is to maintain the current cost-share ratios shown in this table consistent with WaterNSW's proposal. These cost shares were established in IPART's 2006 determination and have remained constant since that time. The cost shares are based on a framework that allocates WaterNSW's costs between customers and the broader community based on an impactor pays principle. That means costs are allocated to different groups in proportion to their contribution to creating a need for WaterNSW to incur the costs.

In our 2012 review of rural water charging systems, we recommended that cost-share ratios be reviewed every second determination period. WaterNSW proposed that such a review should be conducted after the conclusion of the determination process to allow sufficient resources to be allocated and ensure proper consideration and consultation.

While the cost-share ratios have been maintained since IPART's 2006 determination, the nature of WaterNSW's expenditure program, the mix of its expenditure activities, has meant the overall share of costs allocated to customers has increased over recent determinations.

The overall customer cost share based on our current draft decisions is 67 per cent. This represents a seven percentage point increase over the total customer share allowed in IPART's 2010 determination.

We considered the review of cost shares was important due to this change in the overall share being borne by customers, as well as the fact that cost shares have not been reviewed in some time and we received significant stakeholder comment about the appropriateness of the current cost shares.

We asked Frontier Economics to review the cost-sharing framework. Frontier recommended recasting the approach to determining cost shares in each valley. Rather than basing the cost-share categories on cost items or activities, Frontier recommended relating efficient costs to specific services provided by WaterNSW, subtracting legacy costs to determine efficient forward-looking costs that would be recovered from current and future impactors, and then recovering these costs through prices, the New South Wales government's contribution or other mechanisms.

Frontier considered its proposed approach would provide the right incentives to water users in WaterNSW, encourage consistency in the application of cost sharing over time and with other industries and increased transparency around the cost of providing specific services.

We consider that Frontier's recommendations may provide a more robust approach to cost sharing. However, Frontier has highlighted a number of preconditions for its approach. These include gathering detailed information on WaterNSW's services, shared assets and activities, and developing a clear and well-documented process for allocating the costs of shared assets and activities.

The proposed approach may also require changes to information collection and billing systems, as well as potential legislative and regulatory changes to allow costs to be allocated to impactors that are not billed by WaterNSW.

Given these preconditions, it is not feasible to implement Frontier's approach as part of our 2017 determination.

Our draft decision is therefore to maintain current cost shares, but implement an extensive review of the framework, including stakeholder consultation, before the 2021 determination. This will allow us time to address

Frontier's preconditions and properly consider the complex issues involved.

For this session we are interested in your views on whether our expenditure adjustments are reasonable, including whether there is any scope for further efficiency gains. We are also interested in whether Frontier Economics' proposed cost-sharing framework would lead to a better distribution of costs between impactors. Thank you.

THE CHAIR: Thank you very much Elina. Comments? We will start with some comments from the irrigators. Stefanie?

MS SCHULTE: Stefanie Schulte from the NSW Irrigators' Council.

Before going into the detail of what we have just discussed, I would like to thank the tribunal for providing us with another opportunity to appear at this hearing today and also taking this chance to have a second hearing, which is a first.

As IPART and WaterNSW concede, there is a large contingent of irrigators here today, really reflecting the importance that irrigators place on not only their water entitlement but also the importance of water charges, and the reason being is that it has a direct financial impact on irrigators' bottom line and, of course, the production of food and fibre in the state.

In terms of the aspects that we've just heard, regarding the notional revenue requirements, we acknowledge that IPART has proposed a reduction of $5.1 million per annum rather than as compared to the last determination. However, there is a point that we would like to make, in particular, around the additional cost that will be passed on to irrigators through their charges, including the proposed passing of MDBA charges at an average of $15.4 million in the year, the balance of the overs and unders mechanism of around $3 million a year and the proposed volatility allowance of another $0.8 million a year.

That is about $19.2 million a year of costs that are passed on to irrigators which are either not regulated, in the case of the MDBA charges, or in our view don't need to necessarily be there and we will go into those in a minute.

In respect to the operating allowances, we acknowledge that IPART has proposed a reduction of $11.2 million over the course of the next determination. However, what we are actually more concerned about is the allowed and actual operating expenditure over the course of this determination which we've heard was around $21.7 million.

It is our understanding that irrigators have already paid for that allowed operating expenditure, but in some instances that expenditure has never been met, so we do believe there should be consideration made by IPART that those efficiency savings that have been achieved by WaterNSW should be shared with its customers and we will be making a submission to that effect.

In relation to capital expenditures, we acknowledge that IPART has reduced WaterNSW's proposed capital expenditure by $44 million, but we're concerned that IPART's expenditure consultant has found that most of WaterNSW's proposed capex project had not undergone significant investigation and design, or were immature in their development and, in addition, Aither also stated in their report that there was little certainty over the need for the expenditure.

As per the previous determination, IPART outlined in its own draft report that there has been a significant underspend by WaterNSW on their capital allowances, $120 million compared to the $90.27 million of actuals, and as we outlined to the tribunal last time, through that, irrigators have paid a return of that underspent capital which we believe should be returned to irrigators in the course of or within the next determination.

In addition, we would also like to raise our concerns that IPART's proposal would see WaterNSW's capital expenditure allowance increase by $40 million in total, but also nearly tripling for the user share of that capex, and that being despite the reasonably poor track record of what we've seen of actual expenditure versus allowed expenditure for capital.

The reason why we consider this important, as a last point, is that we have seen a significant growth in the asset base of WaterNSW and we do believe that there will be a significant cost coming back to irrigators over the course or courses of the next determinations and despite the reduction in the proposed rate of return, that's going to be an ongoing cost factor that you will see coming back to irrigators.

THE CHAIR: Thank you very much, Stefanie. With so many irrigators here, I guess I can move down the table. Zara?

MS LOWIEN: Zara Lowien from Gwydir Valley Irrigators. I would probably support Stefanie's comments and just raise a couple of things around operational expenditure.

Obviously, I welcome the additional efficiency gains within the Gwydir Valley and continue to look forward to the efficiencies being realised as the mergers continue and the organisational restructure for capital expenditure overall.

In addition to Stefanie's comments, I think the issue for us is around the Aither review where they didn't look into individual projects, they looked at a higher level comparison, and so in that assessment they found $21 million dollars worth of savings or revised costs for renewals and almost $44 million over the entire capex program, and for me that questions if they've gone into individual projects, whether that capital review would be even less than it currently sits.

Second to that is a question around the fishway investment and the continued look at the project there. I note that Aither said that it would be a prudent and efficient business to be looking into that option and that is correct and I question whether there is a duplication with DPI Fisheries potentially and within DPI Water as part of the negotiations under the basin plan implementation, noting that most of the valleys, being the Gwydir, Lachlan and Macquarie, are also part of the northern basin which had a review to look at complementary measures. I would like that to be investigated before that cost is passed on to users.

Our major concern, one of our headline issues, with the pricing process, from our point of view, supporting Stefanie, is the continued growth of the RAB. The concern for us is that since 2013 to current forecasts at the end of this next determination period, we are looking at just under $250 million worth of additional regulatory asset base added on which customers are paying for.

I think the fact that it is nearly 70 per cent of notional revenue requirement is a big concern and that is something that into the long term we're going to see the RAB continue to grow and customers continue to pay on that, and that we might see a long-term erosion of customers supporting capital investment who may see a degradation in our assets, as customers are unwilling to continue to invest and add to that RAB. I think that's where we don't want to be, so we have to consider how we're continuing to calculate that going forward.

THE CHAIR: Thank you very much, Zara. Mary?

MS EWING: Thank you. Mary Ewing, Executive Officer with Lachlan Valley Water.

Endorsing the comments that have already been made, we welcome the reductions in opex. However, we do flag a concern that whether the reductions in opex are also contributing to a reduction in service levels and the lack of consultation that there has been with customers on levels of service going forward. In the Lachlan Valley, particularly, we've seen a loss of WaterNSW personnel from the valley and that has been something that people have valued in the past.

In terms of capex, we have similar concerns to Zara about the rigour of the examination of the capital maintenance and renewals program and the fact that it is considerably higher than what WaterNSW and its predecessors have submitted in the past for capital for those items, so we welcome an even closer look at that.

In terms of scope for further efficiency gains, again, in terms of opex, I flag that issue about levels of service and changes in level of service in achieving those gains. We are concerned about the continuing underspend in capital expenditure or delayed expenditure that has been typical of WaterNSW in the past and the fact that WaterNSW is therefore receiving an unearned rate of return on some of that capital which currently is not being adjusted and we believe that there's a capacity to adjust that through the annual reviews.

Finally, in terms of Frontier Economics' proposed cost sharing, while we welcome a look at cost sharing, we think that there needs to be a close examination of who the impactors really are, given the changes in community standards and community expectations about service that we have seen over the last five to 10 years, and whether those are now actually transforming some community expectations into impactors rather than extractive users being a primary impactor. Thank you.

THE CHAIR: Thank you very much, Mary. Perin?

MS DAVEY: Thank you. Perin Davey from Murray Irrigation.

Again, I support what my colleagues have said, particularly about the opex and the capex. However, I would like to commend IPART for applying scrutiny to the WaterNSW application and looking at the results of the IPART draft determination for WaterNSW charges would see our charges for New South Wales Murray general security entitlement holders go down and we applaud that decision.

I mainly want to focus my comments on the cost share issue. While I accept that the Frontier Economics review has led to a recommendation for valley-based cost share, I think that there needs to be an awful lot of stakeholder consultation, so I understand why that has been postponed.

However, in the absence of having a full review of the cost shares, given that the reality of the application of the cost shares that have been maintained since 2006 is that the customer share is actually increasing, having increased 7 per cent since the 2010 determination, I think that more scrutiny needs to be applied to certain of these areas.

As Mary indicated, perhaps we need to redefine impactors or consider whether impactors is now the right application, impactor pays or beneficiary pays. There are unbilled impactors. Increasingly, there are community standards that are being called for and need to be met that require river operators to actually manage the system which is not necessarily meeting the needs of the impactors.

Certain things on the user-share list, such as corrective maintenance, routine maintenance and asset management and planning, are now all being influenced by these other interest groups that are increasing in their demands on rivers. These include riparian landholders, recreational users, local governments and of course the environmental requirements that are being met. Some of these, including environmental water deliveries, are having adverse impacts on the rivers and therefore, again, impacting how the rivers operate.

We would really encourage IPART to have another look at the user-share framework as it stands and at the very least maybe apply more of a community service obligation on certain areas of river operations and management. Thank you.

THE CHAIR: Thank you very much, Perin. Shane?

MR GEE: Shane Gee, Hunter Valley Water Users Association. I don't think there is much more I can add to what has been said. I will just go back over capex and that is concerning the lack of detail in the submissions from WaterNSW in relation to capex expenditure. It is probably something we have been noticing through the CSCs lately, the conversation on and the details of the expansion of capital doesn't occur; we're not getting that information when we ask for it, verbally and in writing. Yes, it is concerning that there's not a proper business case done. They can't or haven't outlined specific projects in specific valleys. Yes, that's about it, thanks.

THE CHAIR: Thank you very much Shane. Louise?

MS BURGE: Louise Burge, Vice Chairman of Murray Valley Private Diverters.

I would like to make some comments, firstly, to thank WaterNSW for its attempts to reduce expenditure, so that is appreciated. I would also like to thank IPART for giving us the opportunity to have these ongoing discussions.

In the Murray Valley we face particular risks, particularly for Murray Valley Private Diverters. We tend to be smaller organisations and very much affected by some changes under the Basin Plan and also changes in relation to future decisions on operational matters including prerequisite policy measures and SDLs.

What we are finding is potential for reduced reliability and for increased costs, and we have a situation where the customers do not have this capacity to pay the increasing fees and prices. I draw particular attention in that comment to the MDBA pass-through costs. We believe there needs to be increased scrutiny and transparency on MDBA costs. Particularly, as was mentioned before, with some of the changing expectations through political processes where customers are being charged or potentially charged for some of these political decisions, we see the risks of cost shifting.

I will perhaps speak about some other issues later on, but my final commentary would be that the future processes for capital expenditure, even under SDL, sustainable diversion mechanism projects have already had one demonstrated effect where a business case, under the southern basin measuring project, has perhaps gone over budget or the budget has not met original expectations and those costs have been passed through on the metering charges which IPART has considered. The precedent is set. As that has already occurred once, we are very concerned that if the budgets on these future implementation decisions on the Basin Plan are not accurate, that will come through in fees and charges to us, thank you.

THE CHAIR: Thank you very much, Louise. Graeme?

MR PYLE: Thank you, Peter. Graeme Pyle, Southern Riverina Irrigators.

For some time I have been looking for a complete list of assets of New South Wales that we are charged for the use of. New South Wales should be proud of these assets. They do beautiful work and they produce a great deal of wealth to the state. This list of assets is one of the main drivers for our fees and charges. Was IPART given a complete list of assets and their value and the percentage of usage by New South Wales customers? If so, can I have a look at that list, because that seems to be a basic tenet to it all.

I know at Coleambally, I raised the issue of the Yarrawonga regulator, not a huge instrument, but it has a multiple of uses. We are wondering what percentage of that is charged to us, as the Hume Weir, and to various other instruments all the way down the river, and what is the likelihood of us being charged for this extravagant pipeline from the Murray to Broken Hill over time? That's so that we can rest peacefully in our beds at night knowing that we will not get run over by a bus some time later. Thank you.

I commend WaterNSW and IPART for organising this and driving the cost down. That is a fabulous thing. Thank you.

THE CHAIR: Thank you very much, Graeme. Jenny?

MS McLEOD: Jenny McLeod from Coleambally Irrigation.

I, like my colleagues, would like to congratulate WaterNSW on looking to reduce their operating costs and IPART for the scrutiny that they have imposed on WaterNSW's submission.

I have a couple of comments specifically in relation to the Murrumbidgee Valley and the question of whether adjustments to opex and capex are reasonable. I note that in the Murrumbidgee Valley, with the exception of metering and billing, WaterNSW's current expenditure is significantly below the allowance allowed by the ACCC. I think the adjustments that you have proposed are well within the reach of WaterNSW and are actually higher than what I project their current expenditure will be, so I think there is possibly some more stretch in that area.

In relation to capex, that is the next area that WaterNSW needs to focus on. I agree with the comments by Aither and the conclusions that IPART has made that their capital programs needs a lot more work to be robustly developed and to have a bottom-up instead of a top-down approach.

Coleambally Irrigation is used to managing capital programs, much smaller than WaterNSW obviously, but balancing capital investment in the long term to ensure your assets are not gold-plated but they are robust is really important. WaterNSW has some work to do in that space and irrigators look forward to working through those issues with them. So we support the capex adjustments.

In relation to cost shares, I have a couple of points. Perin has raised some very valid points about the potential for issues with valley-specific cost sharing. Coleambally Irrigation would like more information about how IPART intends to roll out that process going forward.

In relation to the current determination - I know we will discuss MDBA costs in the next session - comments have been made about the changing community standards and the impactors driving costs. When we see the MDBA costs, which are the costs which are increasing for Murrumbidgee and Murray irrigators, I think there is a case to look at whether or not the cost-sharing arrangements between government and water users, or that component of costs, should be potentially adjusted with a greater government share paid through this determination. Thank you.

THE CHAIR: Thank you very much, Jenny. Ildu?

MR MONTICONE: Thank you. Ildu Monticone from the Peel Valley Water Users Association. Thank you for the opportunity to say a few words.

I think our situation in the Peel is quite different from most of the other irrigators here because as long as we continue to pay three times more than the next highest water usage charges in the Murray-Darling Basin, really, we do not have much interest in focusing on the split of opex and capex and user shares. Our major focus is trying to get the usage charges down to somewhere near a reasonable figure.

It is interesting that around the time the draft decision was delivered, WaterNSW came to us with a proposition to adopt an 80:20 split in the field. If that was approved by IPART, it would have a dramatic effect in the reduction of water usage charges in the Peel. I guess our question is: would IPART consider the adoption of that?

THE CHAIR: Thank you, Ildu. We will consider that and every other issue which is raised as a part of this process. You have now raised that. That is now on the public record. We will consider it and we will consider submissions on that and other matters. Thank you.

I am going to call on David, from the MDBA, and Gavin, from DPI Water, to see whether they have anything they want to say now. I will then give WaterNSW a chance to respond to some of the issues and will also call on any further comments from the secretariat before we open it up to the floor.

David, would you like to say anything now?

MR DREVERMAN: David Dreverman, MDBA. I think I will let Gavin go now. It is better that I do it at the next session.

THE CHAIR: That's fine, thanks. Gavin?

MR HANLON: Gavin Hanlon, DPI Water. I was going to say the same thing.

THE CHAIR: All right. David, would WaterNSW like to make any comments at this stage?

MR HARRIS: Yes, thank you, Peter, and thank you to those who have acknowledged the cost reductions that we have achieved, which are due to management's approach to running an efficient business for our customers.

I will comment very briefly on opex, capex, cost shares and fishways. In relation to opex, through its draft decision, IPART, correctly, recognised the significance of the large reductions that we have proposed and included only minor adjustments to our requested opex allowance. We are pleased to see that those reductions have been accepted to enable WaterNSW to better provide services to our customers at lower cost over the forthcoming period. We do consider that the amount we ask for is reasonable, particularly in relation to the 20-year infrastructure strategy, and we will be making written submissions to IPART on that point.

In relation to capex, firstly, a number of comments have been made, and they have been made at earlier forums, around the historical capex underspend. We have undertaken with our customers to look at holding costs over the course of the next determination. I referred to that in my opening comments and we stand by that commitment.

We also detailed at previous hearings the different methodology that we are now using, which has been endorsed by Aither and IPART, in relation to calculating our capex, and, in particular, the different methodology that we are adopting for delivering capex. I will not go through that again because I have spoken about that at all of the public forums convened by IPART. Suffice to say we have changed that methodology in an attempt to address the historical underspend. So we are aware of that problem and we have taken steps to address that.

In relation to capex and our pricing proposal, we included a request for a capital expenditure allowance of $186 million. $115 million or 60 per cent of our request related to our maintenance capital program of around about $28.8 million per annum. Yes, this was a step increase over the last determination which provided $19 million for capital maintenance capex. This amount was designed to ensure that WaterNSW does not consume assets faster than we are able to reinvest to maintain their capability. It includes necessary catch-up maintenance capex from years of under investment.

WaterNSW uses a model of actual asset condition and risk data with investment values benchmarked against a depreciated modern engineering equivalent replacement asset value to determine a cost-efficient profile of reinvestment for our assets.

In its draft report, IPART accepted in full the recommendations of Aither, the consultants engaged by IPART to undertake a review of the prudency and efficiency of operational and capital expenditure set out in our pricing proposal. We are disappointed that IPART did not allow the amount we requested for maintenance capex. We will be arguing for a smaller reduction than IPART proposed and we will be making a written submission to IPART in that regard.

I want to touch, lastly, on capex and on a point that Louise Burge made today, which has been made in previous forums, around the cost risk of government-funded projects or specifically SDL projects. This is a matter that we have raised now several times with Gavin Hanlon from DPI Water. That risk will be addressed when the government decides projects to be funded by either the New South Wales government or the Commonwealth and then implemented by WaterNSW.

In terms of cost shares, as noted in my introduction and consistent with the position put by the NSW Irrigators' Council in relation to the pricing determination, we have supported and we have committed to our customers to conduct an in-depth review of the issues of cost shares and, I might stress, legacy asset issues during the next determination period to enable those issues to be fully ventilated.

Finally, I will just touch on Namoi fishways. We are currently working with our customers in the Namoi Valley in relation to the best options to complete fishway obligations. The Commonwealth has recently advised that the obligation in Gunidgera Weir, at Namoi, will not be funded through complementary measures, and we have communicated that overnight to the chair of the CSC. We are continuing to meet with the CSC and NSW Fisheries prior to our submission to IPART on this issue. Thank you.

THE CHAIR: Thank you very much, David. Scott, do you want to say anything at this juncture?

MR CHAPMAN: No, thank you.

THE CHAIR: Matt?

MR EDGERTON: Matt Edgerton, from the IPART secretariat

Mary, Perin and, I think, Jenny mentioned the fact that community expectations are increasingly driving expenditure. I was wondering if you are able to elaborate a bit more on that and perhaps provide us with a specific example or two.

MS DAVEY: There are several examples. Certainly the example of impacts and negative damage can be seen with the incidences of bank slumping. In the case of the Barmah Choke, which is near our valley, there has been silting of the Barmah Choke due to the necessary delivery of flows downstream. For example, last year, the river was kept at bankfull for much of the year, which has been said to contribute to the silting. That is an impact of river management.

As an example of increased community expectations just last week in the Pastoral Times, there was an article whereby the business development manager of the Edward River Council was calling on the MDBA to operate the river at higher levels for Easter so that the tourists could enjoy a good ski season, for the end of the season. These tourists do not contribute at all to river management costs, and the water has to come from somewhere. There is an expectation by the community and by businesses, and I understand these river towns are dependent on tourist dollars, and increasingly so, as irrigation dollars fall away with the water recovery that has occurred in our region. They are increasingly looking at tourism dollars to make up the shortfall; however, the tourism dollars are not paying for the river operations and management. That is a very recent example.

THE CHAIR; Jenny or Mary?

MS EWING: One example is in extreme conditions, for example, severe drought, there is a very high demand from the public to continue operating a river for as long as possible as far as possible. That is understandable, but that is delivering water to people who are exercising their basic landholder rights. They do not pay for services. It takes a lot of cost for WaterNSW and water to operate the river. In that circumstance, I think that demand for a high level of service through a whole range of extreme conditions is an impactor that currently is not being charged. Thank you.

THE CHAIR: Jenny?

MS McLEOD: The only other thing I would add to that would be that we the environmental water management and the demands of society to shift the balance between irrigated agriculture and the environment and the environmental water manager is placing a different set of demands on its use. Also, that can then extend to environmental works and measures which generate a cost in the provision of environmental benefits. That is the only other point I would add as an example.

THE CHAIR: Thank you very much, Jenny. Questions from the floor or comments? Anybody? Yes?

MR SALARDINI: Ash Salardini from the NSW Farmers Association.

I would like to, firstly, endorse all the comments from the irrigators. I would like to focus on one comment that seems to have been made once but not reiterated again, and that is the capacity to pay, particularly in the North Coast and South Coast but also the Peel Valley. There is a big issue here around capacity to pay. Regardless of the pricing determination, we are seeing a decline in users and that will increase costs for future determinations if you go with full cost recovery.

I note that from the North Coast and South Coast, there seems to be an acknowledgment of this, but there was not any explicit acknowledgment from the Peel Valley and that is a big concern.

THE CHAIR: Thank you, Ash. Would anybody else like to make a comment?

MS TONGE: Fleur Tonge, from Toonumbar Dam. With regard to examples of the capex and operational expenditures, one example that we have seen up in our area is where severe damage occurred a couple of years ago due to flooding at the dam. This year some operational expenses have been done there which have been termed capex - $250,000 worth of road maintenance.

I see that as an example where changing between operational expenditures and capex can cause us longer term expenses. It also just questions the reliability that we can give to the decisions on capex versus operational expenditures.

I suppose the other point on that is that it would be largely done there for tourism and other people visiting the dam rather than for the irrigators.

THE CHAIR: Thanks you, Fleur. Yes?

MR WOOLASTON: Tom Woolaston, Peel Valley Water Users Association.

I would like to support Ildu and let you know that we are hurting as irrigators. It is very hard to meet the costs that are coming in, and irrigators are gradually stopping irrigating because of the costs. We hope that you can consider closely the change from 60:40 to 80:20.

THE CHAIR: Thank you, Tom. Is there anybody else? Yes, down the front?

MR COUROUPIS: Anthony Couroupis, from Western Murray Irrigation. I am appreciative of both the opportunity to sit here today and to provide feedback. I also commend WaterNSW for the significant improvements they have made in the organisation's operations. I would note significant historic underspends on both capex and opex. I think some of that is incorporated, but I do not see any certainty around that that is not going to remain the way for the future, so I encourage IPART to continue to scrutinise forecast expenditure as you have. I encourage that.

The proposal before us would see no net change in WaterNSW's costs, but a 70 per cent increase in MDBA costs and an overall increase in our bill of 50 per cent for New South Wales Murray high security users. We consider that unacceptable. Wrapped up within that, there is a range of issues around the fixed to variable cost share and the increase in MDBA costs but also the high security premium change as well. We again commend WaterNSW for the reductions in costs, but look forward to seeing that continue along with maintaining service delivery. Thank you.

THE CHAIR: Thank you, Anthony. Yes?

MR DOYLE: Bob Doyle. I am representing the Paterson River here today. I was chair of Coastal Valleys from 1999 through until January this year, except for a small stint of about four years. I have resigned as chair out of frustration with the process.

As a Paterson irrigator, I am quite happy with the process and I think the consultation process has been very good. While I was chair, I felt very differently about the situation for the North Coast and South Coast. The consultation through the CSC reference panel, through the development and our contribution to the WaterNSW submission has been very difficult to the point where I have a lot of problem with trust of the capex and trust of the opex.

The problem stems back to asking basic questions and getting a response. As much as David says that there has been better consultation, and overall for the Hunter, I would say that is okay, the problem for the North Coast and South Coast is that it has been nowhere near that transparent. The process to get to 23 February, when we were told that the preference for Toonumbar Dam is the sale of that dam as an outcome, or the future direction of the dam, has been very, very frustrating.

It comes back to the process of the CSC - I know this is not relevant to this actual hearing and it comes more into the operation licence hearing when we come to that stage and when we talk about CAG - but for the North Coast and South Coast, the consultation has just not been up to scratch. It comes back, and it means we have to very, very seriously look at every one of these capex expenditures. We ask questions as to what they are about. We get very, very little response. As much as David says that the consultation has improved, while that might be true for the Hunter and it might be true for the rest of state, it is not true for the North Coast and South Coast.

THE CHAIR: Thank you very much, Bob. Anybody else? Yes?

MR GRAY: Peter Gray for EnergyAustralia New South Wales.

We would like to agree with the previous speaker in respect of price concerns. The capex expenditure within our scheme has always been underspent and that leaves us with some concern. The changing in the setting up to an 80:20 pricing regime not in line with other valleys is also of concern to EnergyAustralia. We find that the raw water run of river chlorinated water that is delivered to us at a price in excess of $800 per megalitre is purely extreme.

We would also like to highlight the fact that the 80:20 determination does not encourage any water savings. As an organisation, and previously as Delta Electricity, millions of dollars were spent on reducing our take from river, particularly in times of drought. Although I can recognise why WaterNSW wants to actually change this for their cash flow, it does cause other issues for other users. Thank you.

THE CHAIR: Thank you very much, Peter.

SESSION 2: Draft decisions on MDBA and BRC costs

THE CHAIR: I think now is probably a good time to move into session 2, which is a discussion on the Murray-Darling Basin and the Border Rivers Commission, and I ask Shirley Dang to introduce the topic

MS DANG: Thank you, Peter.

The MDBA and the BRC are cross-jurisdictional bodies that coordinate and manage water resource management and bulk water activities from a "whole of system" perspective. The BRC activities, and hence the contributions to them, apply in the Border Valley, while the MDBA activities are undertaken in the Murray and Murrumbidgee valleys.

WaterNSW has proposed recovering BRC and MDBA costs via an annual 100 per cent fixed entitlement charge and an adjustment to the high security premium applied to MDBA and BRC costs.

Our draft decisions on BRC and MDBA charges are outlined on the current slide. In this session, I will go over what our decisions are and why we made our decisions.

WaterNSW's proposed to pass through BRC and MDBA costs to users of around $61.65 million over the four years of the 2017 determination period.

Our expenditure consultants, Aither, conducted a high level review of MDBA costs and found that the MDBA was generally able to explain its processes for promoting prudence and efficiency and no glaring issues were identified. Aither did not review BRC costs as detailed information was not available.

While Aither did not have sufficient information to identify any specific reductions in MDBA costs, we share similar concerns with customers about the lack of independent scrutiny in the development of MDBA costs. We appreciate the concerns raised by users that insufficient transparency means there is no assurance that only prudent and efficient costs are pass-through. Indeed, while Aither's review found the processes was generally sound, it was unable to verify that these costs are efficient. Therefore, our draft decision is to apply an efficiency adjustment of 1.25 per cent compounded per annum to both BRC and MDBA costs.

Here you can see the impact of our efficiency factor on both BRC and MDBA costs over the four years of the 2017 determination period. Our efficiency factor would reduce BRC and MDBA costs by $2.4 million and this represents a reduction in the customer share by approximately $1.9 million over the 2017 determination period.

In its 2014 decision, the ACCC introduced an unders and overs mechanism to address WaterNSW's revenue volatility risk that arises from the mismatch between WaterNSW's tariff structure and its cost structure.

In this session we will be discussing about the UOM established for MDBA and BRC revenue. The UOM for each individual MDB valley will be discussed in session 3. Currently, WaterNSW faces an under-recovery of around $2 million for MDBA and BRC revenue. In its pricing proposal it estimated that the under-recovery will increase to $3 million.

WaterNSW has also proposed to recover the outstanding amount by adding the UOM balance to MDBA and BRC charges, smoothed over each of the four years of the 2017 determination period.

Our draft decision is to accept this proposal, as the ACCC passed through the MDBA and BRC costs in its 2014 decision on the basis that these costs represent a regulatory obligation that WaterNSW cannot control. Also, smoothing the recovery of the balance over the four years will reduce customer bill impacts.

We have also made the draft decision to discontinue UOM for BRC and MDBA costs as we consider that the UOM does not materially reduce WaterNSW's revenue volatility. We will have a further discussion about the discontinuation of the UOM for each individual MDB valley in session 3.

As mentioned earlier, WaterNSW has proposed to recover BRC and MDBA costs via an annual 100 per cent fixed entitlement charge. From WaterNSW's perspective, its BRC and MDBA costs are 100 per cent fixed which means that the current 40:60 fixed to variable tariff structure is not cost reflective. However, adopting WaterNSW's proposal and moving to a 100 per cent fixed entitlement charge would create substantial bill impacts for high security customers in these valleys. It would also mean that WaterNSW is transferring all of its revenue risk to customers.

We consider that, ideally, fixed costs should be recovered through fixed charges and variable costs should be recovered through variable charges. As such, we consider the current 40:60 fixed to variable tariff structure to not be cost reflective. A higher fixed proportion would be appropriate.

However, we consider it unreasonable to shift to a 100 per cent fixed tariff structure and shift all the risk to customers. We consider it more appropriate for WaterNSW to bear some revenue volatility risk as business revenues are not guaranteed in competitive markets. As such, our draft decision is to adopt an 80:20 fixed to variable price structure for BRC and MDBA charges. This tariff structure would achieve a reasonable balance between matching WaterNSW's largely fixed cost structure and distributing volume risk between WaterNSW and its customers.

In line with its proposed 100 per cent tariff structure, WaterNSW has also proposed adjusting the high security premium for BRC and MDBA charges, recognising that shifting to 100 per cent fixed entitlement charge would disproportionately impact high security customers. Specifically, WaterNSW proposed to adjust the high security premium down to mitigate bill impacts on high security entitlement holders.

However, to reduce bill impacts on high security customers, WaterNSW has adjusted the premium to shift the cost burden to general security customers through higher prices per entitlement. This means that general security entitlement holders with relatively low usage could face large bill impacts.

We acknowledge that without an adjustment to the premium, the bill impact on high security customers would be larger. However, we consider that it is not appropriate, in principle, to reduce the bill impact of high security entitlement holders by manipulating the high security premium and shifting costs on to general security customers.

The high security premium serves to reflect the relative security and reliability of supply afforded to high security entitlements over general security entitlements and the parameters used to calculate the high security premium reflects each of these benefits to high security entitlement holders.

As such, our draft decision is to not apply a different high security premium for BRC and MDBA charges but to maintain the same high security premium we calculated for WaterNSW's bulk water. We will discuss about the high security premium further in session 3.

Despite our efficiency factor, bills from BRC and MDBA costs will impact customers in the Murray and Murrumbidgee valleys. This is due to the combination of an increase in MDBA costs and our draft decisions on BRC and MDBA price structures.

The current slide demonstrates the bill impacts for BRC and MDBA costs alone. As you can see, high security customers in the Murray and Murrumbidgee valleys will be largely impacted. This is primarily due to our draft decision to switch from a 40:60 to an 80:20 tariff structure, which means that the fixed component of the tariff structure is larger. This change in tariff structure, combined with our draft decision to use the higher non-adjusted high security premium, means that high security customers bear larger costs of the now larger fixed component of the BRC and MDBA charges.

In addition, our draft decisions on BRC and MDBA tariff structures will impact overall bills in the Murray and Murrumbidgee valleys. This slide shows bill impacts excluding BRC and MDBA charges. As you can see, bill impacts from WaterNSW's bulk water charges will be decreasing in real terms.

However, our draft decisions on BRC and MDBA will negate this decrease and, in particular, substantially increase bill impacts on high security customers in the Murray Valley.

We have the following questions for stakeholders:

Is the efficiency factor of 1.25 per cent compounded per annum applied to WaterNSW's proposed BRC and MDBA costs reasonable and sufficient; and

What are your views of adopting an 80:20 tariff structure?

THE CHAIR: Thank you very much, Shirley. WaterNSW would just like to make a couple of quick points and then I was planning to move to David and Gavin before moving to other stakeholders. David Harris?

MR HARRIS: Thanks, Peter. I just want to make the point that these are not WaterNSW's bulk water charges. WaterNSW is simply providing a billing service to the New South Wales government. We should not be at risk for these charges. They are not ours, they are not WaterNSW's bulk water charges.

THE CHAIR: Thank you, David. Who would like to go first? Gavin?

MR HANLON: I might provide a general overview, if that's all right. The Murray-Darling Basin costs are built up from each of the states and the shares between the states is something like New South Wales 47 per cent, Victoria 43, South Australia 8, and the balance in surrounding areas, and ACT end up with 1 per cent of that for the southern system.

In around 2012, the New South Wales government substantially reduced its contribution to the Murray-Darling Basin Authority at the time. It felt that for all the reasons explained here around funding and efficiency, that it would substantially reduce that on the basis that a number of reviews were then completed. Those reviews have since been completed, so I might go through what they were.

Firstly, there was a request for a review of the cost shares between the states, an efficiency review, which has since been done by Synergy and Cardno, a review of cost spikes, so the Murray-Darling Basin Authority's cost profile shows some quite chunky expenditure with their infrastructure in the out years, so we asked for a review on ways of mitigating the risk for induced price shocks and we also asked for a review on institutional arrangements for the best way to be able to manage any future cost spikes that might hit the states as a result of changes in the cost spike review.

Finally, what has happened in the last 12 months. The basin officials also requested that the MDBA - in fact, I think it was the Commonwealth department that ended up commissioning it - do a review on the regulation approaches to the MDBA's corporate plan. Each state has its own economic regulators and the ACCC ultimately oversees each of them in turn, but it was clear that each state was potentially doing its own thing with economic regulation and some of this stuff was falling through, even though all the states had asked for an efficiency review over the top of the MDBA's cost structures.

That review is yet to fully conclude. I think the report has been submitted. I am not sure we made a decision at the last one. We were going to enter into discussions with the ACCC on the best way of doing that because the last thing we want to do is have the New South Wales regulator look at the costs and determine one thing and then submit the corporate plan to a regulator in another jurisdiction and end up with two different numbers, so we will have to have a discussion with the ACCC on the best way of getting a consistent approach across the basin on that.

In terms of the way the corporate plan is built up by the MDBA, New South Wales and WaterNSW have members on I think it is the River Operations Committee, which is one of the committees that looks at both river operations and ongoing capital requirements for the infrastructure operated across the basin and that corporate plan goes through another level of scrutiny, then submitted to basin officials, which I represent our state on, and then ultimately on to the ministers for sign-off for I think it is a three-year rolling period, from memory.

I think the next step for government is that, as per the last determination, we are anticipating that there will be a direction issued to WaterNSW at some point very soon for being able to pass through those costs. That hasn't been issued yet, although we're anticipating it will be soon while different parts of government work through the best mechanisms for doing that.

I think it is fair to say that as a result of some of those reviews that have been rolling since 2012, the costs in the MDBA have actually remained relatively flat. I think that New South Wales share is around $30 million in total. I think four or five years ago it was $32 million. What has changed is the user shares contribution to that and, as flagged, the government is yet to decide or issue a direction as to what it might like to see roll out there into the future.

As for the ultimate user share and broader community share, I acknowledge the comments made around the changes in customers - I will call them customers - or water users profile within the basin. More than 30 per cent of the water has been taken out of the consumptive pool and now sits with other users who have very different needs to other customers and I think it is fair to say that has been pretty actively debated at a basin level about ongoing appropriate cost shares between environmental water holders and normal customers and that will have to play out in the next 12 months or so.

I was going to leave it at that for general comments, Peter. David knows the intimate detail of the MDBA corporate plan.

THE CHAIR: Thank you very much for that, Gavin. David?

MR DREVERMAN: Thank you. In the presentations that have been made and in the draft determination there is a lot of confusion between the term MDBA costs are rising and MDBA charges are rising. As Gavin said, the cost to governments of the joint program, New South Wales's share in 2006 was about $32 million. This year it is less than that and even next year it's about $30 million, so it hasn't risen.

What has changed is you're doing a comparison back to 2014, which Gavin has explained was a period during which New South Wales had chosen not to meet its historic share and effectively was receiving a subsidy from other governments to make the program continue to happen at a slightly lower rate, and to the extent there has been any growth in expenditure in the last couple of years, we have had to re-bring into the program some particular major plan maintenance and asset renewal projects that were deferred during that period 2012 to mid 2016. They were deferred during that time to allow the program to continue without the full historic share by New South Wales.

Gavin did mention one of those reviews that was done was a review of cost shares. That review found that the historic shares was as good an approach as any and has been endorsed by all partner governments to continue into the future.

Gavin also mentioned an efficiency review that was done a few years ago by Synergy and with support on the engineering side by Cardno. In that review, they got to the end and they could find that the program was efficient, but as regulators all over the country were putting in efficiency dividends of the order of 1 per cent, they recommended that there be a 1 per cent efficiency dividend in the MDB river management program going forward and that is actually included in the total charge that has been levied on New South Wales share this year. When you then apply another 1.25 per cent on top of that, you're actually doubling the efficiency review and because the corporate plan going forward has been signed off by the four governments at ministerial council level, effectively, New South Wales share has been agreed, so when you take a 1.25 per cent dividend, you're actually just doing an additional transfer in your cost share, the efficiency dividend has already been met. We will come back in our written submission and explain that to you.

There are a couple of other elements. The high security change probably reflects the climate sequence we have been in for the last 20 years where you actually see that high security entitlements in the Murray are taking a bigger share of total water availability as the total water availability has reduced.

The other thing that we have seen is that within that high security share the urban supplies, through the changes to the Water Act in 2008 and the introduction of the concept of critical human water needs, the urban water supply component of that high security water has actually become more secure than the share that is available to irrigators and that is not reflected at any stage in any of the pricing arrangements around the country, but it was pretty clear in the millennium drought that towns got water when even high security irrigators weren't getting water. It is something that you might want to contemplate going forward, particularly in a drying world.

With the 80:20 fixed variable, our costs are basically fixed. If anything, I have explained to the different IPART hearings previously that in drought when water use is down our costs actually go up, not down, and that's pretty well understood. I think it is a step in the right direction, your 80:20 tariff, but it is actually not fully reflective of our costs, our costs actually do go up.

The final one I wanted to mention was you're talking about, in relation to the rest of the program, a return of underspent capital. The River Murray Operations Joint Venture, which is the joint venture between the four governments, is a not-for-profit entity and if it doesn't spend the capital that was provided for this year, it will spend it in due course. It does that through adjusting future contributions.

If you look at the whole time I've been there, 17 years, the only under-expenditure in relation to that that as a New South Wales share will be the under-expenditures that happen this year. Every other dollar of under-expenditure in that last 17 years that had a New South Wales tag on it has been spent to provide a program from which New South Wales is benefiting.

There was a little bit of impact through that four-year period where there is some element of under-expenditure that is owing to Victoria and South Australia, but it doesn't affect New South Wales. It has proven a little bit more challenging as to how we return that, but we're working on that. I think that's probably enough from me.

THE CHAIR: All right. Thank you very much for that David, that's very helpful. Other comments from stakeholders around the table? Stefanie?

MS SCHULTE: I will make a start and then I will hand over to our members in the Murray and also the Murrumbidgee to fill in the body of the detail. First of all, I would like to pick out the point made by Gavin and also David.

What we care about as water licence holders is the amount that we actually pay as part of our bulk water charges and I do appreciate that decisions are made without irrigators being at the table, but because of the rigidity of the pricing determination being made every four years, or in the last case every three years, we have never had the transparency of being able to meet up between what is being determined for the four-year pricing period versus what we actually pay and so instead of just having two sets of figures, every single year we have sets of figures and if there was a decision made, or a decision that was made in the past, of reducing New South Wales share or contributions to the authority, it should still be raised as a point that irrigators through that period still paid the contributions that were determined by IPART. It is not our shares or our costs that have actually decreased in that period.

In terms of overall, we continue to be frustrated that from our perspective there's very little regulatory oversight of those costs that have been passed through and that there's very little transparency and it was quite evident even in the Aither report where there seemed to be some confusion by the consultant of the MDBA costs that are passed through as part of WaterNSW's charges versus those that are passed through to other regulator charges through the water administration, the ministerial corporation or the DPI Water charges. It wasn't quite clear to us in the report that the consultant understood the differences of those charges that came through.

In terms of the overall MDBA pass-throughs, in terms of our costs, those increases are significant. We are talking about $61 million over the course of the next determinationthat will be recovered from our water licence holders in both the Murray and the Murrumbidgee and that is not to take into account the efficiency dividends.

We do commend IPART to have a look at both sharing of costs between the New South Wales government and water licence holders in that respect and we also commend them for imposing an efficiency dividend of 1.25 per cent.

We do believe that in light of the lack of transparency around those costs from the perspective of water licence holders, that efficiency dividend could be greater going forward, and secondly, in terms of aiding that transparency from the perspective of licence holders, we do strongly recommend IPART to have a review or have a look at the submissions that the council will make in respect to the review of WaterNSW's operating licence, as we do believe IPART could impose some form of transparency and disclosure requirements on WaterNSW, at least as a constructing authority, to be able to give licence holders some form of transparency around the actual works and projects that are being conducted.

Finally, we did note with interest the underspend of capital expenditure identified by IPART and do acknowledge what David has said, that this was the first time that there was an underspend in capex from the New South Wales perspective. We have concerns that as part again of this pricing determination, those costs have been paid for by licence holders and, effectively, we just want to make sure that the capital will be spent, that it is not going to be asked for again, and if it is not spent then it is also returned to licence holders in the form of an offset between actual MDBA costs.

THE CHAIR: Thank you very much, Stefanie. Perin?

MS DAVEY: Thank you very much.

I hear what Mr Dreverman says, that you can't compare the cost now as to what it was in 2008 or even 2014. However, as Stefanie said, in 2008, when the New South Wales government determined to drastically reduce their contribution to the MDBA, our component remained the same to such an extent that the user share component was virtually 100 per cent of what was being paid for the New South Wales contribution to the MDBA. Irrigators or water users have never been recompensed for that skew in the government user cost shares at the time.

We commend IPART for contracting Aither to review the efficiencies of the MDBA. However, I do find the Aither report a bit lacking in terms of a lot of the comments from Aither concern the limited scope of their review, so they couldn't fully have a look. While they found that it appears the MDBA charges are efficient, they have said that that's within the limited scope of their review.

I note, too, that they have identified that the MDBA planned costs are returning to historical levels. I also note that when the New South Wales government reduced their contributions, the MDBA also reduced some of the joint programs, such as the Sustainable Rivers Audit. While costs are returning to historical levels, some of those programs have not been re-instigated, so there is a bit of a mismatch there.

Aither did find that given the nature of the River Murray operations assets and expenditure, there are a few reasons as to why it shouldn't be treated like any other regulated business or utility and that has been the position of certainly Murray Irrigation over a number of years, that the same scrutiny and transparent process should be applied.

There have been a series of reviews that Mr Hanlon referred to. However, there has been no public submission component to those reviews. We have not had the public scrutiny that is applied through something like the IPART process.

The government user cost share component of the MDBA is probably even more of a factor when it comes to the MDBA charges than with WaterNSW. Certainly, a lot more of the infrastructure that the MDBA is responsible for has that cross-interest component to it. It is being used a lot more for environmental purposes. Community expectations with delivering for environment river management has changed over the years and that has not been reflected in the way the government user cost shares are applied, so I would really endorse IPART having another look at how the cost shares are applied.

I just want to note in the Aither report - and it is in the executive summary on page (x) - they identify the Murray user share of the WaterNSW contribution and that is actually 15 per cent of the total MDBA planned expenditure. That is just users in the one valley through one component because we also have an MDBA component through our DPI Water charges, so that would bring our percentage of what we are contributing to the MDBA up even further.

When you view that and then look at it in the context of the southern connected system in which we operate, where we are in a competing marketplace, the way the MDBA charges are collected from the other states is also not that transparent, but our understanding is it is not all through water users either. I think that that needs to be taken into consideration in the context of who is paying for what services. I am sure my colleagues have further to say.

THE CHAIR: Thank you very much, Perin. Louise?

MS BURGE: Yes, thank you very much.

I think one of the greatest things comes back to the users capacity to pay and confidence in the process. We won't have that confidence until we get transparency. It is not clear where the transparency lies. We have information or general overviews on what DPI and MDBA charges are and what WaterNSW pass through MDBA charges are, but we are actually not getting a breakdown on the MDBA charges themselves.

There are a lot of implementation costs with the basin plan. The Water Act 2007 was meant to be done at no cost to state governments, but we can't sit back and say that that is correct because, quite simply, we don't know. We don't know what Commonwealth funding was given to New South Wales in relation to implementing the Water Act 2007. We don't know what component of it is appropriately segregated in the cost structure to ensure that there is not double-dipping or information is being smudged between cost structures or indeed charges. I think to build confidence we certainly need that transparency.

The MDBA has about 300 staff and we are not clear where those staffing responsibilities lie and one of the major things that we have found right through water policy is that there still seems to be this component where charges are applied without the capacity of the customer to have input into how to achieve projects or capital works with the appropriate level of scrutiny by those who actually pay the most. There needs to be in any future discussion about pricing impositions, the capacity of those customers to scrutinise.

I suppose I will leave it at that, but there are a lot of risks in the various factors.

THE CHAIR: Thank you, Louise. Graeme, and then Jenny.

MR PYLE: Thanks, Peter, I don't think the efficiency factor is anywhere near high enough. I think it should be 12.5 per cent compounded and that would take the MDBA and the BRC off the planet much quicker than it will take it at 1.25.

The greatest threat to irrigated agriculture in New South Wales is the MDBA, other than droughts and floods - they are the only thing that beats you. In South Australia everyone pays for the MDBA, but here we are in the Murray Valley paying a vast amount for a lacklustre performance by the MDBA.

If we do not pay the MDBA fees, I am wondering at what stage will David Harris cease sending us water? Also, what amount of money is received by WaterNSW for collecting these fees for the MDBA? I smell a conspiracy and I am thinking collusion with monopolies here. I am frightened for my irrigators. Please help me.

THE CHAIR: Thanks you very much, Graeme. David?

MR HARRIS: I could clear that up right now. We recover nothing --

MR PYLE: Thank you.

MR HARRIS: -- for the billing service we provide - nothing, not a cent.

MR PYLE: And will you supply us water if we do not pay the MDBA?

THE CHAIR: Thank you, David. Jenny?

MR DREVERMAN: Sorry, could I reply?

THE CHAIR: Yes, David.

MR DREVERMAN: Can I clarify that when WaterNSW collects money from irrigators to meet MDBA charges, the charges are a matter for New South Wales and that money is passed from WaterNSW to New South Wales treasury. The New South Wales government has agreed to make a contribution to the MDBA.

Despite what you are saying, Graeme, it is not a direct path. We do not tell them what to collect; that is a matter for the New South Wales government. It is a sovereign matter within New South Wales. What they collect comes out of the determinations of IPART. It reflects our cost, but the whole of what they pay is a matter for New South Wales processes to determine.

THE CHAIR: Thank you, David. Jenny?

MS McLEOD: I am from Colleambally Irrigation, which is in the Murrumbidgee Valley. I think the point David has made is at the crux of this issue and that is that MDBA costs are an agreement between the New South Wales government, or of the New South Wales government, to contribute to MDBA functions. Irrigators as water users have no line of sight to the decision-making process or the services that are provided.

The key issue for irrigators in the Murrumbidgee Valley, who are contributing about 18 per cent of the MDBA costs, which are costs incurred outside of the Murrumbidgee Valley, is the transparency for the decision-making around the decision that they pay 18 per cent and the Murray Valley pays the balance. That is our key issue in terms of the costs.

I agree with the comments - particularly the comments Perin has made - about the MDBA costs. When you are looking at moving on - the under and overs mechanism and recovering the outstanding amounts - I think you also need to look backwards to the former determination where irrigators paid 100 per cent of the costs, when you consider that issue.

My two other points are that it would appear that with the state constructing authority costs that the MDBA pays for, there is actually little scrutiny of those costs and whether there are opportunities within the state constructing authorities in Victoria, South Australia and New South Wales to actually effectively - to use simple terms - load up costs that are charged through the MDBA versus other costs that might have a more rigorous process around them.

In relation to the high security irrigators and the premium or the impact on those high security irrigators, I would argue that if IPART is concerned about that, they should not look to a solution that general security pay more. They should look at price caps as a mechanism to alleviate that rather than shift it to general security irrigators. Thank you.

THE CHAIRM: Thank you very much, Jenny. Are there any other comments around the table before I open to the floor?

Questions or comments from the floor? Yes, Anthony.

MR COUROUPIS: Thank you. As you have heard from various speakers beforehand this is a story of transparency, scrutiny and rigour. I think, to a person, everyone says that is absolutely missing from the New South Wales irrigators' perspective, being those that are responsible for paying these charges.

In terms of your questions with the efficiency factor, we are not sure because we do not know what we are paying for and that is the expression of this frustration.

The impact of adopting an 80:20 tariff is significant, particularly on Western Murray, arising again from a range of changes. Also building on Jenny's point about the constructing authority arrangements, David made very clear that WaterNSW makes no gain from collecting the revenue and passing it on to the MDBA. But I regard WaterNSW as so conflicted in that constructing authority arrangement, where it is the beneficiary of the payments from the MDBA to WaterNSW for those construction activities, that I would perhaps regard it as unable to comment, again because of the conflict of interest that arises from that source of income, and again around which there is next to no scrutiny.

The impact of the proposed change on Western Murray's bill is that the MDBA costs would increase from twice WaterNSW's costs to almost triple MDBA costs year on year, this year versus next year. We regard the need to consider tools like price caps or other things like that as essential as our customers recover from the drought and look to continue to invest in irrigated horticulture.

THE CHAIR: Thank you very much, Anthony. Are there any other questions or comments from the floor?

Are there any wrap-up comments? Gavin or David?

MR HANLON: As a way of general comment, earlier I made the comment about economic regulation of the MDBA and that there are three or four states as joint venture members there. Each of them in turn, except for the ACT, has their own economic regulator. We are currently thinking through the process of what would make sense here so we do not have regulators regulating more regulators.

As I mentioned, we are thinking the best way of doing that is to ask the ACCC to provide some guidance to the states on how to deal with MDBA inputs into their corporate plan. Coming with that would be the transparency and rigour that I think people are asking for here, but that discussion still has a way to go.

THE CHAIR: Thank you Gavin. David?

MR DREVERMAN: I have been in the program 17 years and I have heard this accusation of lack of transparency. The New South Wales government has available to it, all of our cost information. It has a complete set of every budget over that period - all 65 pages with every single project set out in that. We are very happy to provide whatever support to meet the transparency needs that you are looking for. Through Gavin and David, all you have to do is say, "This is what we need", and we will provide it for you.

People are talking about Aither and Aither not being able to do things. We provided Aither with the full support for the budget that they had to do their review. They spent a very, very small fraction of the time that Synergy and Cardno spent with us when they did a complete and comprehensive review. So the fact they put that comment is more a reflection not of our costs and not of our efficiency but of the budget that they had to do the task, so I am a little bit frustrated.

If I can share, in terms of customer oversight, what we do, there is a Murray customer service committee. I have attended it three times this 17 years. I have gone every time I have been invited. I have been prepared to stay all day if necessary to answer the questions, but they have a whole lot more pressing issues and I normally stay for an hour or an hour and a half, maybe two hours, for discussion.

Although you all come here and say you want transparency, you know where we are - we never knock back an invitation when we go to those meetings and we turn up as requested - if you want to have a further detailed discussion.

When we do turn up, one of the interesting observations I would make is that WaterNSW will turn up. They will talk about the part of our program that they are delivering on behalf of four governments, but they do not actually then address the other parts of our program that are being delivered by the other two governments and they probably do not even address the parts of government that are being delivered by DPI Water. If you are really fair dinkum about improving the transparency, then you need to look at the engagement process. But we are very, very happy to participate in that improvement.

THE CHAIR: Thank you, David. Louise?

MS BURGE: Thank you. Could I highlight, as a member of the Murray Valley customer service committee, that we are unable to ask detailed questions about the broader MDBA costs because they are deemed to be outside WaterNSW's core business. They will only deal with questions in relation to WaterNSW's operational costs. That has been made very, very clear.

Coming back to the point of what customers need, we need some transparency about the different components of the MDBA structure right across the system. That is important because then we can determine what level of costing is actually for the river operational matters as opposed to other core business of the MDBA of which irrigators are not meant to be liable for. That is what we are seeking. We seem to be going round and round and round in this circle where nobody can provide us with an answer. I believe, on behalf of the irrigators in our valley, that we need those answers. If we are being required as a user pays, it should be our right to get that information.

THE CHAIR: Thanks, Louise. Perin, and then David from WaterNSW.

MS DAVEY: Thank you.

David, with all due respect, I hear what you say. Like you, I have heard it before, that the MDBA makes this information available to the New South Wales government. This is by no means a sort of direct assault on any one agency. It is clearly a failing, however, of the process that irrigators, year after year, keep coming back with the same complaint that they have no line of sight on how these costs are determined, how they are then broken up and how they are applied to user charges. That is the key thing.

I do agree entirely with Louise's statement that one of the concerns, particularly in the modern era of the MDBA, as opposed to the Murray-Darling Basin Commission, is that it reports in the federal budget sphere as one entity across all of its tasks - the River Murray operations, implementing the Basin Plan and so forth. As water users, we cannot see the breakdown of what is being paid for and how. So it is not any singular agency; it is a failure of the process.

THE CHAIR: Thank you, Perin. David Harris?

MR HARRIS: Thanks, Peter. I want to make a couple of points.

First in relation to Anthony Couroupis's comments about our costs, it is those costs as constructing authority that were, in fact, scrutinised by IPART in its review for prudency and efficiency. As Louise has indicated, at our CSCs we provide information on our business's costs, which, relevantly, are the constructing authority costs for New South Wales.

Obviously the New South Wales share of MDBA costs includes other costs that are nothing to do with WaterNSW and we cannot provide those details because we do not have them. Secondly, Gavin referred to a request of the ACCC. Stefanie, supported by others, referred to regulatory oversight of these costs. I simply point out to people that we made a recommendation in that regard in our pricing proposal - we commend that; I have spoken about that at previous forums - but I would strongly urge that we not set up another layer of pricing regulation in relation to this. It would be a matter of very minor incremental cost for each of the constructing authorities. In fact, we have just done it; we have just gone through a prudency and efficiency review for our element of the joint venture costs at the state level through IPART, Goulburn-Murray Water and SA Water could do exactly the same thing at a very marginal cost. You bring another layer in on top of that and you will have to pay for it.

There is a third issue I want to raise. I appreciate that for our customers the main issue obviously is the amount that they are paying here, so I appreciate that the issue I am about to raise is a second-order issue against the primary issue that our customers have raised, but that second order issue is this: we previously have been subject to a direction from the New South Wales government to pay a fixed amount. That has previously been dealt with as a mere pass-through under our prior pricing determinations.

It was decided that, in fact, in this pricing review, IPART would do a prudency and efficiency review of the New South Wales government's share of MDBA costs that we pass through to our customers. That was done and, amongst other things, IPART recommended an 80:20 split in relation to those charges and the abolition of UOM.

As Gavin has indicated today, we are expecting that, in fact, the New South Wales government will now issue a direction to WaterNSW, in exactly the same way as it has done previously. Given the process that we have gone through with IPART in looking at the prudency and efficiency of these costs, I find it a little bit strange that the New South Wales government would then lob in a direction.

From our perspective, the issue that that creates is a gap between a fixed amount required under this imminent direction from the New South Wales government versus the split fixed variable tariff charge that IPART have recommended. We simply point out that IPART's issues paper states categorically that IPART itself must allow WaterNSW to recover an amount equal to the cost that it has to pass through from the New South Wales government. We highlight that to IPART because we see ourselves getting caught between these two approaches and having to make up that gap out of charges that other customers outside of Murray and Murrumbidgee pay us.

We think that is not what should be done. We have gone through this whole exercise for a reason, but I just make that point that we must be able to recover whatever charge we are required to pass through to the New South Wales government.

THE CHAIR: Thank you, David. Are there any comments? Gavin?

MR HANLON: Just to comment further to David's point on the direction, it is anticipated the government will issue a direction of some sort. The final details of that are for discussion with another government that is a much bigger one than ours and that will happen over the next few weeks.

THE CHAIR: Thank you, Gavin. Anybody else? Louise? .

MS BURGE: Thank you.

After this determination review, I would hope that we could actually get to a point where that transparency that we have been requesting and, indeed, the regulatory oversight on the MDBA charges will be similar to other charging regimes that are subject to regulation. What approach or what direction does this discussion need to go in to achieve that objective? I would hate to be in this situation in the next determination where nothing has changed. Is there something that we, as customers, can go towards to get the objectives completed that we need?

THE CHAIR: David, why don't you make a comment and then I will make a comment.

MR HARRIS: Okay, thanks. What we have all just been saying is that the New South Wales government contribution to the Murray-Darling joint venture is an amount of money that comprises in part, costs that WaterNSW incurs, and in fact DPI, as well as constructing authorities, exactly the same as Goulburn-Murray Water and SA Water. That New South Wales government contribution, though, covers other costs as well that are not related to the asset services, if I can call them that, that we provide to the joint venture.

What has just occurred is that IPART has actually conducted - and this is exactly, Louise, what you and others have asked for - a prudency and efficiency review of our costs, as constructing authority, being a portion of those MDBA charges.

What IPART cannot do through the WaterNSW pricing determination is have a view of or review other components of the New South Wales government contribution to the joint venture. They cannot do that. They are not part of our cost base. They are not part of the costs that we can show Aither and take Aither through, and so on. This is the whole problem we have in that our costs are only a portion of that total joint venture payment and this pricing determination, therefore, is not the vehicle for the sort of transparency across the entire joint venture - the New South Wales government joint venture contribution.

THE CHAIR: Thank you, David. Gavin, do you want to say something now?

MR HANLON: No, thank you.

THE CHAIR: To comment on the questions that you have raised, Louise, and that others have raised, based on my experience, long before IPART when I worked in government, this is actually a New South Wales government issue.

The Murray-Darling Basin Authority is a joint venture of four governments, if you include the ACT. There is a decision as to what each state should contribute - X. Then the question is how does the New South Wales government propose to pay X? Where will it get the money from? What has happened is that they have said, "Well, irrigators, for example, that receive services from WaterNSW and from DPI Water should make a contribution", and the last time, the New South Wales government issued a direction which said that the irrigators should make a contribution of a proportion of X, which the ACCC passed through as a direction.

This time, we did not have a direction before we started this pricing process, so we took a look at the prudency of the costs that were being imposed through MDBA by the New South Wales government potentially on the regulators and we formed a draft view. That is what we are discussing, and the draft view is on the slide.

The issue then is if the New South Wales government issues a direction sometime in the next few weeks, then that will be taken on board. If not, the tribunal will have to make a final decision on what should be passed through. That is where we are at.

In terms of going forward, we can take on board the comments that have been made today. You are quite right that they have been made in the past, but I think today's discussion has actually opened up a few other areas. The contributions in particular of David and Gavin have been most helpful, at least from an IPART perspective, and, I would argue, from the perspective of other stakeholders.

Maybe going forward what needs to be done is that the government - I should imagine this would be very much in Gavin's bailiwick - would need to look at the total cost, look at how that is divvied up amongst the different stakeholders, including what should be passed through, and then make it transparent and clear why certain amounts are being passed through to whom and whether those costs are prudent and efficient, as we got Aither to do a relatively high-level review because we didn't have the time to go through and do a bottom-up review.

If previous consultants like Synergy and Cardno have done that, I am not sure whether that information was made available to Aither, and whether that type of information or that sort of updated information was available, whereby people would feel more comfortable that the expenditure that they are being asked to pay by the MDBA is indeed efficient. Thank you.

Is there anything else? We are now 10 minutes after the planned lunch break. Why don't we break for lunch now. We were planning to come back at 12.45. Maybe we should still try to come back by 12.45 for session 3. Thank you very much.

LUNCHEON ADJOURNMENT

THE CHAIR: Welcome back, everybody. Just in case there is somebody who was not here this morning, could I just remind you that today's hearing is being webcast and recorded by our transcribers.

SESSION 3: Draft decisions on price structures and managing volatility

THE CHAIR: I now call on Chris Ihm from the IPART secretariat to introduce discussion on price structures and managing volatility. That is session 3. Thank you.

MR IHM: Thank you, Peter.

Our draft decision is to discontinue the unders and overs mechanism, the UOM. This mechanism was introduced by the ACCC in its 2014 decision to address WaterNSW's revenue volatility risk. The UOM operated such that variations in actual versus expected sales would accumulate in an account and then the holding costs on that account balance would be reflected in prices, not the actual balance itself.

The holding cost adjustment only varies prices by a small amount, hence, we consider that the UOM does not materially ameliorate volatility risk. The total UOM balance as at 1 July 2016 is $19.5 million and that represents a shortfall to WaterNSW. Prior to making final decisions, we would update this balance for actual sales in this current financial year.

Given that our draft decision is to discontinue the UOM, there lies an issue with the existing balances. In our draft decision is that customers would return these balances to WaterNSW via an uplift to entitlement charges and this uplift would be applied to both general security and high security entitlement charges in accordance with how much they contributed to the existing balance.

To address revenue volatility, WaterNSW propose a risk transfer product of about $3.6 million per year to be included in its prices. It argued that its current tariff structure exposes it to an unreasonable amount of volatility risk and so this risk transfer product would mean that it would swap two-thirds of actual usage revenue with two-thirds of expected usage revenue with a third party provider, hence, replicating an 80:20 fixed to variable tariff structure.

We agree with WaterNSW that its existing tariff structures do expose it to revenue volatility and hence, some financial risk. However, our calculations indicate that self-insurance may potentially be a more cost-effective option than purchasing an RTP.

Hence, we are introducing a volatility allowance which is a premium that will be included in prices to reflect WaterNSW's exposure to undue revenue volatility risk and this premium would be applied to all values that are at cost recovery and have a fixed proportion that is less than 80 per cent.

The amount that we have included in prices is $0.765 million per year and this is applied to general security and high security to the extent that they do contribute to revenue volatility. In most valleys the source is general security, but in some valleys, like the Lachlan, there is some from high security and this was based on examining the percentage allocations over the past 20 years to both high security and general security entitlements.

Turning to our draft decision on price structures, we are maintaining tariff structures for the valleys, except for Lowbidgee and the Fish River water supply scheme. For Lowbidgee we have reduced the 100 per cent fixed charge that is currently in place to an 80:20 fixed and variable split. We consider that 80:20 would be a reasonable balance between matching WaterNSW's cost structure and distributing risk between WaterNSW and its customers.

For the Fish River water supply scheme we have increased the current fixed proportion that's 55 per cent to an 80:20 fixed to variable tariff structure. This restructure was done as part of a package deal in conjunction with addressing the one-off structural change in demand due to the closure of EnergyAustralia's Wallerawang power station where we have set the UOM balance attributable to its closure to be zero.

The 80:20 fixed to variable structure would mean that going forward a greater reliance is placed on fixed charges and means that EnergyAustralia contributes an appropriate share of costs incurred in providing infrastructure related to its contractual arrangement with WaterNSW.

A key component in setting prices once a tariff structure has been decided are the high security premiums. This determines how much more high security entitlement holders pay compared with general security entitlement holders and this is due to the greater security and reliability of water that high security customers enjoy.

We have maintained the existing approach but have updated the inputs. The security factors are calculated using high security entitlement and general security entitlement information, along with long-term extraction limits in each valley's water sharing plan, to signify the relativity security between high security and general security entitlements.

These factors haven't been updated since the 2006 determination and also back in 2006 for certain valleys their water sharing plans were not yet in place and so estimates were made.

We have also updated the reliability ratio to reflect the latest 20-year period. Something to note is that changes to these high security premiums don't mean a change in the overall revenue that WaterNSW receives, but rather, redistribution of the revenue received between high security and general security entitlement charges.

As a result of the update, most valleys would experience a modest reduction in the high security premium. The reduction would be larger for the Gwydir, but particularly so for the Hunter. With the Hunter, back in the 2006 determination, rather than using the information available in its water sharing plan regarding high security, general security and long-term extraction limits, given that there was a conversion factor of three specified under its plan, that number was directly used to denote the relative security between high security and general security entitlements.

However, subsequently, this number has been removed from this plan and no longer holds, therefore, we have re-calculated its security factor using the information in this pilot water sharing plan, consistent with how the security factor is calculated for all the other valleys.

In contrast, the high security premium in the Murray Valley would increase. Information in its current water sharing plan indicates that a lower long-term extraction limit is available compared with the information that was used in the 2006 determination. Hence, if there's a lower long-term extraction limit and high security customers are given priority water allocations, then they enjoy greater security of supply.

That is the impact on high security and general security entitlement charges over the four years. This excludes the impact of the MDBA charges. We are looking at about a 5 per cent nominal increase over four years for high security, including inflation.

We have some questions for discussion:

What are your views on discontinuing the UOM and recovering the outstanding balance directly from entitlement charges?

Is it reasonable for WaterNSW to face 20 per cent business risk?

What are your views on the introduction of the volatility allowance for WaterNSW to engage in "self-insurance"?

Are there other ways WaterNSW can manage its revenue volatility risk efficiently?

Are the changes in tariff structures for Lowbidgee Valley and the Fish River water supply scheme

reasonable?
What are your views on updating the parameters in the high security premium?

THE CHAIR: Thank you very much, Chris.

Comments or questions at the table? Stefanie?

MS SCHULTE: We would like to comment on the first three questions, in particular, the proposal by IPART to remove the unders and overs mechanism. New South Wales is quite concerned that IPART's draft determination suggests the phasing out of the unders and overs mechanism and the repayment of the balance, including interest, over the course of the next determination, the reason being that such a change in approach is, in our view, quite contrary to what the ACCC's intent of that process was in the 2014 determination which was designed to enable the recovery of WaterNSW's or back then State Water's notional revenue allowance over the long term and to phase out their unders and overs mechanism and recovery of the remaining unders and overs balance over the next determination will significantly distort prices and lead to less transparency for WaterNSW's customers.

We have a preference to continue the unders and overs mechanism, instead of a volatility allowance, for the pure reason that at least the unders and overs mechanism throws up actual consumption versus forecast rather than artificially inflating prices in the first instance.

Therefore, coming to the volatility allowance, we are quite puzzled that we're going back to an approach that we had in 2010. As I said, not only do we feel that irrespective of what actual consumption figures will be over the next determination, we provide a very marginal sort of risk protection mechanism for WaterNSW through the VA and, at the same time, the current way of how the rate of return is being calculated, we have a feeling that the volatility allowance kind of doubles up on what the risk premium in the calculation of the weighted average cost of capital really should be and hence, we sort of questioned why we would have a volatility allowance and a risk premium for WaterNSW.

The final one in terms of the insurance overall, we wanted to reiterate that even under very severe drought conditions, a significant proportion of WaterNSW's revenue is actually guaranteed just the way that we have the current structure and the way that IPART has proposed to continue the cost-sharing framework. Even under the current figures and assuming that the current government and unit share is continued, 33 per cent or $141 million would be guaranteed through the proposed government user share and then of the remaining 67 per cent, 40 per cent of that is recovered through the entitlement fixed charges, which would then constitute another 20 per cent of WaterNSW's notional revenue requirement.

That leaves about 40 per cent of WaterNSW's total revenue at risk, in our view, but even during the worst year of the drought, when there were consumption figures as low as 30 per cent, that would then still, through the variable charge component, add another 12 per cent. So we are talking over 70 per cent of WaterNSW's revenue that is actually recovered. Therefore, to have not only a rate of return that includes a risk premium, the phasing out of the overs and unders mechanism and the volatility allowance is coming to that third question. It is a significant amount of protection that is being allowed to WaterNSW that is not in any way, shape or form accessible to any of its customers.

Just to reiterate, we would prefer the continuation of the overs and unders mechanism, because it is much more transparent, and not the volatility allowance and definitely not the repayment of the balance of the UOM over the course of the next determination.

THE CHAIR: Thank you, Stefanie. Other irrigators? Zara?

MS LOWIEN: Thank you very much. Obviously, I will be reiterating Stefanie's comments there, but I'll talk particularly about some of the analysis we've done as well. The question, again, we were quite obviously vocal through the previous hearing and also the issues paper about WaterNSW's actual volatility in terms of their business and so what we have seen as part of this draft determination is actually some actual expenditure over the last determination and we've noted some significant savings in operational expenditure.

For example, in the last determination we had $21.7 million not actually spent by WaterNSW. We have a current UOM balance, by the presentation we have had here, of 19. When you add it up in the report, it is actually 14.9 and that is what you are requesting users to pay back in the next period.

14.9 hasn't been recovered from customers over the determination, but they have saved 21.7, so we've actually paid more than what we’ve received in terms of actual expenditure. For us there's a real issue with the way IPART has suddenly changed the UOM, as well as the requirement to pay that back.

It is the one significant driver, together with the high security premium, of prices in our valley and is unacceptable. We don't see that the balance needs to be recovered based on actual costs and if it does, if a volatility management structure needs to be in place, we would prefer that, based on the analysis that the ACCC provided us some time ago which said that it does provide chances over the long term, and I think what we're missing here is a very short snapshot of price volatility which we'll need to consider over the long term.

Some other points for us on this section, unless people want to talk about UOM? No? There is the consideration around the payback of that. As I said before, we don't believe it needs to be done, we would prefer the UOM to be in place, but if it does have to be paid back, I question the split between high security and general security. It is based on water allocations and not actual water usage and I think that needs to be reflected in the pay back opportunity.

The major component of prices for us is this high security premium and the update. We did ask for an update of that premium and used the current figures. The concern I've got is linked to forecasting and the basis of the 20-year rolling average being used rather than the IQQM outputs. I do note that in some cases you're using the water sharing plan factors, which is actually an IQQM output, but in our case you use a 20-year rolling average. We believe it needs to be consistent and, as we have provided in the past, a preference for IQQM as a long-term representation of access and usage in our valley is much more applicable. Thank you.

THE CHAIR: Thank you, Zara. I might ask Jenny, would you like to go now?

MS McLEOD: Yes. We don't have a lot of comments on these issues. I agree with Zara's point about the difference between allowed expenditure versus actual expenditure and the validity of the argument for recovery of that cost.

I have a question in relation to the proposed annual adjustment of pricing within valleys that's in your proposed structure for MDBA valleys, as to how that actually links with the volatility because the annual adjustment is to take into account variability in water sales, so we need to be sure there's no double-dipping in that respect.

In terms of the long-term yield on different entitlements, it is important that we use a long series path and I think it's also important that we don't seek to manipulate and change that. We have the MDBA looking to change the long-term cap factors through the basin plan decision making process and we don't support that and I think IPART need to give consideration to rather than looking at the short term for the high security premium, they look over the longer term, noting that it is more of an issue in the Murray Valley than in the Murrumbidgee Valley.

Those are all of the comments I have on these points, thank you.

THE CHAIR: Thank you, Jenny. Ildu, do you have any comments?

MR MONTICONE: Thank you.

In the Peel we don't have unders and overs, so it's a pretty simple response to that part of it, and if IPART approved the 80:20 proposed cost-sharing ratio in the Peel then volatility and the risk transfer approach, and all of that, is out of the window anyway. Thank you.

THE CHAIR: Thank you, Ildu. Mary?

MS EWING: Thank you.

Our views are similar to what Zara and my colleagues have said in terms of the unders and overs mechanism. We don't believe that there has been much opportunity to really be tested yet over a longer period of usage data. We felt that it was actually a more responsive mechanism to the volatility than a fixed volatility allowance.

The proposed volatility allowance is charged to a valley regardless of the actual volatility in income that occurs during that pricing period. It reflects a volatility in the previous period, so you are potentially having a situation where you're over-recovering from a valley that is not experiencing much volatility in that pricing period.

In terms of whether it is reasonable for WaterNSW to face 20 per cent business risk, we feel that it is not unreasonable. Stefanie highlighted the proportion of WaterNSW's revenue that actually is at risk and a fair bit of the revenue that is at risk is actually the share that represents the return on equity, so it is about the shareholders' return rather than the actual funding costs for the capital expenditure, rather than depreciation, rather than tax, rather than operating expenditure, and for a monopoly business we don't actually believe it is reasonable that they should receive a totally risk free revenue. I think I've covered that, thank you.

THE CHAIR: Thanks, Mary. Perin?

MS DAVEY: Thank you, and I concur with what my colleagues have said. Murray Irrigation supported the continuation of the unders and overs mechanism, mainly because it is reflective of what actually happens from year to year, whereas the volatility allowance is a constant and it doesn't reflect that in some years WaterNSW will over-recover, whereas in other years it will under-recover. I agree with my colleagues.

However, I do thank IPART for considering the issue and not going with WaterNSW's original application to have both a volatility risk transfer product and the unders and overs mechanism, and I also congratulate IPART on viewing a self-insurance model as a cheaper alternative to the risk transfer product.

The only other issue that I would like to raise in this session is the issue of irrigation corporation discounts because I am not sure where it fits in the scheduling. It is an issue that I would like to raise. Firstly, I thank IPART for not cutting the rebates by 50 per cent, as was requested by WaterNSW. I believe the proposal to look at actual sites rather than the number of customers is the right way to go.

However, I do note that the proposed reductions from IPART are greater than our actual reductions in site numbers. Since the 2014 determination, our actual delivery site numbers have only been reduced by 8 per cent, as opposed to I think it is 19 per cent proposed reduction in the rebate. In saying that, some of our sites we've changed, we've got new technology coming in, our costs are actually greater and we have a higher proportion of extra large outlets now which have greater costs. That is not reflective.

Also, the other way of looking at it is some people have said to look at entitlements, but our entitlement numbers of what is on our bulk water licence for general security has not changed since 2014, even though there is a greater proportion held on our licence held by government departments or government agencies. However, we still have to deliver those, so it hasn't changed our delivery at all.

I would like to highlight those areas and ask IPART to have another look and consider whether there is room to increase those rebates given those facts and I will be making a written submission as to that.

THE CHAIR: Thank you very much, Perin. We will take all that on board, thank you. Shane?

MR GEE: Hunter Valley water users sort of take those same stances as with NSW Irrigators, so yes, we would be guided by them on those matters. Thanks.

THE CHAIR: Thank you, Shane. Louise?

MS BURGE: One of the issues that continually comes up is we are talking about government risk, but I think, clearly, the people at the most risk are the actual customers. The customers are facing numerous risks in water availability, the volumes of water left in the district, and particularly smaller schemes and indeed larger schemes, but I will speak about smaller schemes, is the capacity for people to pay in those smaller schemes, as a lot of water reform - and

I will use that in inverted commas - decisions are being applied and implemented and the capacity of these people within their schemes to keep paying higher and higher charges with less and less people and less volumes in the schemes is reaching breaking point.

I acknowledge and support Stefanie's comments, and Perin's as well, but with the self-insurance, I think that is a product that WaterNSW should consider, but as long as the risk or the costs associated with that product, if it is just passed through in a different format then how do we, again, make sure that these products and charges are equitable.

I suppose, at that, point I probably will not make much more comment, but in the Murray Valley general security is subject to increasing volatility in terms of security and reliability on the resource and yet, we are being asked to pay for other components that don't share those risks. Thank you.

THE CHAIR: Thank you, Louise. Graeme?

MR PYLE: Thank you, Peter. I think WaterNSW facing a 20 per cent business risk certainly gives clarity to its business. I know it does to mine. There is nothing greater than the fear of failure, and risk does that, or it introduces that into the process.

Now, with the self-insurance thing, I am unclear here. The money is stacked in a self-insurance scheme for later use and I am wondering how you do that safely and then there is its cost over borrowing the money. Now, WaterNSW should be able to borrow money at much lower interest rates than the average punter, so I do not know where you put your money to create extra wealth to cover the charge and the risks. I need clarity there. I raised that at Coleambally as well. Thank you.

THE CHAIR: Thanks, Graeme.

MS McLEOD: Mr Chairman?

THE CHAIR: Yes, Jenny?

MS McLEOD: I would like to thank Perin for raising the question of the large customer discount.

CICL thanks IPART for adjusting the proposed rebate based on the customer site information provided by us. However, we still find that the methodology that you are using to establish the large customer discount is quite unclear.

If you look at the irrigation businesses - Murrumbidgee Irrigation's business and Coleambally Irrigation's business - they have not really changed very much since the last determination, but their large customer discount has decreased by a greater proportion than the Murray large customer discount.

I also note that the one area where WaterNSW's costs exceed the ACCC allowed cost is in metering and compliance. From a logic point of view, we are really questioning the scale of the reduction and the evidence base behind that, if you are using metered sites and avoided costs as the basis for reduction. Likewise, we will be making a submission on that to you.

THE CHAIR: Thanks, Jenny. Scott, are you able to clarify on the discounts?

MR CHAPMAN: I would probably have to go back and have a look in your submission at the numbers on that, but we will take your submission into account on the issue about the numbers of sites and we will reconsider that before we issue our final report.

THE CHAIR: WaterNSW, David?

MR HARRIS: Thanks, Peter. I will comment on the UOM, the RTP and the irrigation corporation discounts.

Firstly, on the UOM, WaterNSW supported customer preference to maintain the UOM in our pricing proposal. We also showed, however, that the UOM does not address our business's volatility risk. IPART's draft determination was not to support continuation of the UOM. If that is to be the case, then WaterNSW supports the balance being returned to WaterNSW as that is part of our revenue requirement.

We see no rationale, I might add, for treating EnergyAustralia differently to other customers. In our view, EnergyAustralia should have to pay the UOM balance attributable to them.

In relation to the risk transfer product or RTP, again WaterNSW supports customer choice on tariff structure, but the consequence of high variable tariffs is that you get revenue volatility for WaterNSW. We showed throughout the process that the UOM did not address that issue at all.

WaterNSW welcomes IPART's recognition that we should receive our revenue in relative alignment to our largely fixed cost base and to support, to replicate an 80:20 price structure. We received a competitive market quote of $1.3 million for an insurance product to manage this revenue volatility. That is down from the original quote in the draft prices of $3.6 million, or a difference of $2.3 million. However IPART is proposing $0.765 million for the purposes of self-insuring our own volatility revenue. We do not accept that the $0.8 million per annum allowance for volatility self-insurance to replicate an 80:20 from the current price structures reflects the efficient costs of providing customer choice on tariff structure. This amount is not sufficient either to self-insure - if indeed we can self-insure, which I question - or to purchase the insurance product, and we believe that IPART should provide us with the $1.3 million.

In addition to that, we actually think that procurement of this volatility insurance is both an efficient and innovative solution to providing customer choice of tariff structure while at the same time providing WaterNSW with the revenue structure more appropriate to our cost structure. The insurance product will be a relatively new development for the Australian water industry.

Lastly, Mr Chairman, in relation to irrigation corporation discounts, due to the building block model, any discount provided to irrigation corporations is added to the bills of other customers who are not irrigation corporations. Accordingly, we believe strongly that it is imperative that the correct discount is applied to irrigation corporations so that other customers are not subsidising irrigation corporations.

We set out in section 16.1.2 of our pricing proposal our new risk-based approach to metering reading. The restructure in the metering reading program was noted to reduce cost and provide savings to customers over the coming determination period. The improved meter reading program is one of the key drivers in the reduction of the metering and compliance budget and, therefore, the reduction of the ICD rebate.

We have identified a number of issues with IPART's methodology in calculating the discount. These include overestimating telemetry costs and the method of estimating customer numbers. We will provide details of these methodological issues to IPART in our written submission. Thank you.

THE CHAIR: Thank you, David.

Are there any questions or comments from the floor? Peter?

MR GRAY: Thank you, Chairman and tribunal members. I am from EnergyAustralia, but I would also like to highlight that I am the chair of the CSC for the Fish River scheme, although I do not speak on behalf of the other three major users. However, I think it is appropriate to emphasise that EnergyAustralia consumes more than half and has a major share of the sustainable yield of Oberon Dam that WaterNSW operates and, subsequently, our opinion, I think, is appropriately weighted.

I do recognise that WaterNSW has considerably improved its communication strategies with customers and I applaud them for that. Let's hope that, in the future, that customer representation process does not substantially change in its current format.

As to the questions above, with regard to question number 2 - "Is it reasonable for WaterNSW to face a 20 per cent business risk?" - in reality most businesses face a 100 per cent business risk in their dealings and the way in which they conduct their operations. They do not have the fortunate position of being a monopoly supplier.

Do I think that the 80:20 change is appropriate - which is question 5 - surprise! No, I don't think it is appropriate. We are dealing with a monopoly supplier here. For EnergyAustralia there is no chance of contractual change to our current arrangement. We are exposed to business risk. We cannot alter our current arrangements with WaterNSW for approximately 30 years. Most people would say that that is not sensible in a business environment, but yet we are contracted to a monopoly supplier.

Being the second highest user in the scheme, I believe that WaterNSW has a conflict of interest in representing itself, as the second biggest user of the scheme, and indeed being the supplier. I imply nothing more than that, and I just note that I believe there is a conflict of interest there.

In closing, the 80:20 shift is a substantial increase from the present levels. As WaterNSW is a monopoly supplier, it would have seemed appropriate that this would have been at least a phased-in arrangement to be fairer to the other businesses involved in the catchment. Thank you.

THE CHAIR: Thank you, Peter. Anthony?

MR COUROUPIS: Answering question 6, we are concerned about the review of the high security premium based on the 20-year window. We agree with others' comments or questions about the use of the longer term IQQM data, which I think, provides a better long-term view as to the relative mix of the availability of high and general security allocation. Thank you.

THE CHAIR: Thank you, Anthony. Are there any other questions or comments?

MR SALARDINI: I think this has already been raised, but there is a bit of a misunderstanding as to what the market risk premium is in the WACC calculations and whether that is doubling up on the volatility allowance. Potentially someone from IPART might want to go through what is included in that market risk premium and that might actually clear that issue up.

THE CHAIR: Thank you, Ash. Matt?

MR EDGERTON: The short answer is there is no doubling up between what is included in the WACC and effectively the volatility allowance that we have proposed in the draft determination.

The volatility allowance we have proposed in the draft determination really recognises that under our 40:60 price structure - 40 fixed, 60 variable - WaterNSW is subject to significant volatility or risk given that, first of all, it has largely a fixed cost structure, and, secondly, there is inherent uncertainty associated in forecasting sales. So that volatility allowance recognises the risk that is unique to WaterNSW.

With the market risk premium in the WACC, that represents more, I guess, general systematic risk associated with a water utility.

MR SALARDINI: But it has no forecasting risk calculated into the risk premium.

MR EDGERTON: In the?

MR SALARDINI: In the market risk, the premium.

MR EDGERTON: It is not addressing that risk.

MR SALARDINI: No.

THE CHAIR: The risk premium in the WACC addresses the risk that WaterNSW faces or other water companies face. In the case of WaterNSW, it is the risk that they face if they were able to price something at 80:20 which is more reflective of their costs.

The issue of the variability that we are talking about, as Matt pointed out, is an effort to transform the 40:60 into the 80:20 because that is more reflective of their costs.

Any other questions or comments? Mary?

MS EWING: I would like to make a brief comment on the tariff structure as it relates to the Lachlan. We are still interested in the 80:20 tariff structure as one that manages risk for users in the Lachlan. However, as an organisation, we are still in the process of consulting our wider membership, and I would like to respond to a couple of the questions you asked in your draft report about what level of support is needed for a valley to move to that.

THE CHAIR: Sure.

MS EWING: I think 100 per cent support is unrealistic and would suggest possibly that majority support from a customer service committee, which is generally people that are reasonably well informed about the issues and are up-to-date with what is happening, is probably an appropriate method. Thank you.

THE CHAIR: Thank you, Mary. Zara?

MS LOWIEN: To follow on from Mary, I agree with that proposal to have a discussion. I think we are obviously seeing a continuation of, in our view, embellished risk to the business and, even with this draft determination, a movement towards an 80:20. We need to sit down with some facts and have a discussion at the CSC, as Mary indicated, with those informed members.

Our view within the Gwydir Valley would be that we would survey our members first and ask every individual member and then present that back to the CSC. The difference with that is that it covers a range of other users especially going forward with the operating licence change. In particular the Commonwealth and New South Wales governments would have a say.

What I would also like to do is continue to touch on - I think Anthony touched on this earlier - forecasting, as I did, and part of the analysis on the draft determination on page 102, which refers to a comparison of IQQM over a 20-year rolling average. It is a little bit clever of IPART to cherry-pick data in a comparison by using IQQM during the millennium drought, which was a very unique climate situation which no-one had predicted. I don't think a 20-year rolling average would have been able to handle the millennium drought and the lack of water throughout that period.

Most water users have been very consistent in understanding the basis of IQQM - its robustness, the fact this is used for assessment, compliance to the SDL into the future and a whole range of assessments for the New South Wales government. It is very interesting that the regulator continues to go for a different process again as opposed to the one that the state government has already accounted for as IQQM.

I think the main thing that we are all facing here is long-term volatility. Yes, things change and, as we pointed out, our water availability changes very, very quickly. We had the last hearing in Moree, and I think we had significant water allocation that year. We have used over our forecast this year and we have more in carry-over to use next year of the same amount.

Situations can turn very quickly. As Mary, I think, pointed out, the volatility allowance request as opposed to a long-term management, whether it is forecasting or UOM, does not take account of change and how quickly it can occur in some of these valleys. I suppose I am reiterating our concern in going against IQQM and also a longer term assessment for volatility in the long run.

THE CHAIR: Thank you, Zara. Are there any other questions or comments?

MR MAGNER: Yes. Chris Magner from the Richmond River, in the far North Coast. The 80:20 proposal that was bandied around a bit originally was not really accepted back through the coastal CSC. However, the more we look at it, we are not all that concerned about whether or not WaterNSW has any security by having that ratio. What we are concerned about is whether or not we have viability available back to the farmers and the licence holders.

On the Toonumbar, when you calculate out of the current 60:40, it is $7.60, or whatever it is, on a usage charge of $45. That is worked out on the 60:40. That does not seem to add up until you work out that there is only 10 per cent of the allocated licence being used in the last average of 20 years and all of the weighting of the usage charge gets then weighted down on to that 10 per cent. That is what forces up the prices of Toonumbar and Peel and Bega. These prices get forced up because using that ratio, whatever one they have locked in on, does not give a satisfactory result. What we should be looking at is what is viable back to the farmers, back to the users.

When you start to look at just Toonumbar, using 10 per cent, for every dollar that we moved over on to the fixed charge, it takes $10 off the usage charge. If you look at how we can start to get viability back to our licence holders, forget about 10, 20, 30 per cent, 60:40, forget about all your percentages and start to work out viability.

What is the viable price that you can charge? If you have to push up the fixed charge a little bit more to bring down those dams that are on the high usage charge, bring them down, change it, chuck the ratios out the window and just work out on viability. Don't get your hat hung up on a ratio formula that you think we all have to abide by.

Once we have viability back into the usage, then we can get our low active dams active again. We can create new use. We can bring in new users and we can get the current users using more. We have gone into a spiral on some of these dams. Let's bring the spiral down, let's get creative and let's get production going again.

THE CHAIR: Thank you, Chris. Stefanie?

MS SCHULTE: I just have a very quick follow-up comment regarding the fixed cost structure of WaterNSW. I think it is still important to note that, even over the course of this current determination, we have seen significant opex savings that have been talked about previously - in the magnitude of $20 million. Also I think the underspend in capex should be taken into consideration when we talk about the fixed cost structure, what the determination does and, as we faced last time, revenue versus allowed revenue. It is very important to go back to what is actually the expenditure role of WaterNSW and then how much it is actually a fixed cost business.

THE CHAIR: Thanks, Stefanie. Anything else on this session? No?

SESSION 4: Draft decisions on price structures and managing volatility

THE CHAIR: Let's move on to the fourth and final session. This is on the draft decisions on valleys below full cost recovery.

I was going to suggest that the stakeholders from the North and South Coast valleys might like to come up to the table. That's Steve Guthrey, Melissa Balas, Fleur Tonge and Chris Magner. The rest of you do not have to leave, as long as there are four seats. Jessica will introduce the topic.

MS FORREST: Thank you, Peter. When possible, we aim to set prices that will fully recover customer share of WaterNSW's efficient costs to ensure that customers receive efficient price signals, resources are used and allocated efficiently and the customers and taxpayers share the costs of services fairly.

As you can see in the figure here, there are two valleys where prices are currently set well below full cost recovery. The North Coast valley recovers only about 20 per cent of operating costs and only 12 per cent of operating costs; and the South Coast valley recovers about 71 per cent of operating costs, but only 42 per cent of total costs.

Previously, prices in these valleys have been transitioning towards full cost recovery, with price increases tapped at 10 per cent per year. However, we consider that full cost recovery is likely to be unattainable in these valleys over the 2017 determination period and beyond.

Full cost recovery prices in North Coast and South Coast valleys are substantially higher compared to other valleys. As with the previous figure, you can see here that this is an issue for the North Coast valley in particular.

There are a number of factors that contribute to the low levels of cost recovery in these valleys, including that these valleys have:

The least number of customers of all valleys;

The lowest volume of entitlement and average annual water usage of all valleys;

Under-utilisation of entitlements by licence holders, particularly in the North Coast valley; and,

Relatively small dams, with higher cost per unit of capacity.

Rather than continuing the current 10 per cent glide path towards full cost recovery, our draft decision is to set prices using a new approach to valleys well below full cost recovery.

In making this decision, we considered a number of broad approaches for establishing a long-term pricing strategy for these valleys and engaged consultants - Aither - to undertake a review to establish key principles for setting prices in valleys where full cost recovery is unattainable.

In Aither's final report, which has been published on our website, it is recommended that for valleys below full cost recovery, prices should be set to align with those that would prevail in a reasonably competitive market and within the efficient pricing band such that the overall revenue that WaterNSW recovers from a customer lies between the lesser of a customer's capacity to pay for WaterNSW's services and the stand-alone cost, and the costs that WaterNSW would avoid if it did not have to supply those services to that customer.

For the South Coast valley, we have set draft prices at the estimated midpoint of the efficient pricing band, which is slightly above the current level of prices. For the North Coast valley, we have frozen prices at the current level, which is slightly below the estimated midpoint of the efficient pricing band, given the particularly low and declining customers numbers and average annual water usage, and the substantially lower levels of water cost recovery, particularly with regard to operating expenditure in this valley.

So just to give a bit of a visual representation of the efficient price band for a valley below full cost recovery, you can see in this figure that the efficient pricing band is located below the level of full cost recovery, which is represented by the black line at the top. The efficient pricing band is represented by the blue shaded area, with capacity to pay, which is the blue line, as the upper limit, and WaterNSW's avoided costs, the green line, as the lower limit. Under our new approach, prices would be set within this band.

In terms of how we estimated the efficient pricing band, we engaged consultants - Agripath - to investigate capacity to pay for rural bulk water services in the North Coast and South Coast valleys. Agripath's study aimed to assess customers' estimated capacity to pay for bulk water in the dairy industry by comparing the cost of irrigation pasture production, to which water costs are a substantial input, to the cost of dry matter bought-in feed as a substitute for pasture.

We used Agripath's cost estimates to approximate the bulk water prices at which the cost of irrigation pasture production would be equal to the cost of bought-in feed for a reasonably efficient farm with an efficient irrigation system. We determined the upper limit of the efficient pricing band, based on these prices, as a proxy for the prices of which a customer's estimated capacity to pay for bulk water would be reached.

We estimated the lower limit of the efficient pricing band as 1 per cent of WaterNSW's total cost of supplying bulk water services, reflecting the high fixed cost nature of WaterNSW's rural bulk water services business and the low avoided cost of supplying an additional customer.

We recognise that our upper and lower limit estimates are likely to require refinement over the medium term. However, we consider that our new approach, rather than continuing the transition towards full cost recovery, is likely to be the best way forward given the declining customer numbers and average water sales in the North Coast and South Coast valleys, which indicate that prices may be approaching customers' capacity to pay in these valleys.

At prices above a customer's capacity to pay the customer would no longer purchase water, so demand for rural bulk water services would fall, further reducing the number of customers usage and entitlement volumes, revenue and the level of cost recovery. This would result in further full cost recovery price increases to recover costs, as costs would need to be recovered from a smaller number of customers. Setting prices based on full cost recovery is therefore unlikely to be achieved in the North Coast and South Coast valleys, as customers are likely to be priced out of the market before full cost recovery is achieved in these valleys.

Under our approach, determining an efficient pricing band with an upper limit based on capacity to pay rather than full cost recovery prices should provide price stability and certainty for customers, which should provide customers with greater confidence when making longer term investment decisions, and it also provides a clear signal that transitioning to full cost recovery in these valleys is likely to be unattainable going forward.

We have the following questions for stakeholders, including:

What are your views on how we have set draft prices in the North Coast and South Coast valleys?
How could this new approach be refined?
Are there other ways that prices could be set in these valleys?

THE CHAIR: Thank you very much, Jess. Okay, comments or questions from around the table? Who would like to start off? Stefanie?

MS SCHULTE: I seem to be doing it for every session. First of all, we acknowledge that IPART has stated in its draft determination and draft report that there will be valleys where full cost recovery is not attainable and we welcome that draft report and draft decision.

We also acknowledge that IPART has dedicated a whole chapter in its issues paper around the issues of coastal valley prices and commissioned two separate studies to look at the willingness to pay in those valleys, so we congratulate IPART on doing that.

In terms of the actual draft decision that IPART has reached in its report, we had great hopes that there would be more price reductions for the coastal valleys. We have a concern that with the draft decision to freeze prices in the North Coast and having a once-off uplift and then a freeze, effectively, in the South Coast, will simply not solve the problem, and what Chris has mentioned previously, the need to really increase or incentivise greater usage on the coast is very important and it would be a win-win for all involved, but under the current prices and the prices that have been in place for the last six years, that has not occurred, so we did think that there is a re-think necessary to reactivate and incentivise greater usage on the coast. I will hand over to my colleagues.

THE CHAIR: Steve?

MR GUTHREY: Steve Guthrey, Bega Valley Water Users Association.

Basically, I endorse Stefanie's comments. I think that we really need to go back and have a really big think about pricing on these coastal rivers. I congratulate IPART in coming part of the way towards that and I think my other colleagues have got some issues that they want to raise and some figures they want to raise in regard to this, so I'll hand it on to them.

THE CHAIR: Thanks, Steve. Who wants to go? Is it Chris or Fleur?

MR MAGNER: Let Fleur go first and I'll follow.

THE CHAIR: You wanted to talk about Bega, Melissa?

MS BALAS: I'll catch up.

THE CHAIR: No, let's do Chris or Fleur. We've got time to go around.

MS TONGE: Fleur Tonge from Toonumbar Water Users Group. On behalf of the Toonumbar Water Users Group, we thank you for the opportunity to provide feedback on this draft report. We are very pleased that it has been recognised that the full cost recovery is not attainable and that this new approach has been proposed.

We commend the support of Aither's report. The critical issue here is how the capacity to pay is calculated. Agripath provided a comprehensive report on the cost of irrigated pasture production and the cost of bought-in feed. We commend this work done. However, we do not agree that this alone can be used to estimate capacity to pay for bulk water. Economic survival depends upon profitability, not just the ability to find an alternative source of feed.

A common mistake is that a business should continue to increase production to a point where marginal revenue equals marginal costs; that is, the marginal profit will be zero. I have done some figures using the reports that you've already documented. Would you allow me to pass these figures around so that I can talk through the figures, Mr Chair; is that all right?

THE CHAIR: Sure.

MS TONGE: My apologies for that paper not being better presented. That was the best I could do early this morning. Using the figures from Agripath's report and the Dairy Farm Monitor project, the marginal revenue per megalitre of water is $270 and the marginal cost at our current rates of irrigation water is $250 to $290. Therefore, the marginal profit at the moment is zero, which means that is the upper limit to which a farmer can pay for this water. It is no surprise that there has been a massive reduction in the water used out of Toonumbar.

I would just like to give you details of how these figures are arrived at. They're not figures plucked out of the air; each of these figures comes from those reports. The details of the calculation are: one megalitre of irrigation provides one tonne of dry matter, that is directly out of the Agripath report; one tonne of dry matter produces 75 kilograms of milk solids, that's from the Dairy Farm Monitor project.

In our area, where price is fairly good, that's $7.65 per kilogram of milk solids, therefore, the marginal revenue of that one megalitre of water is $574. The variable cost to work out our marginal costs, initially, the costs, the variable costs, not including irrigation from Dairy Farm Monitor project, is $4.05 per kilogram of milk solids times by the 75, because there were 75 kilograms of milk solids in that megalitre, gives us $303 of variable costs. Then add in the cost of that megalitre of irrigation water from the Agripath report, it's between $250 and $290 per tonne. They quoted it in kilos of dry matter, so I have converted the 25 to 29 cents to a tonne, so take the average of that and you've got $270.

The total of those marginal costs is $270 plus the $303, so our marginal cost is a total of $573, giving us a marginal profit of zero, which is exactly where farmers should stop using the water. At that point they are making no money to continue to use it.

This shows that there is no incentive at that price to irrigate. We totally agree with the actual process to work out the efficient price. The upper limit of the capacity to pay should be the current price and the avoided costs should be close to zero, as suggested, so we can work the midpoint out. Current usage - and these would be the costs that Agripath used when they were working out irrigation costs - is the 45 plus the $5.54, that's the DPI costs in there, so usage costs are currently $50. Add in our fixed costs, which are $12.83, giving us a total current cost of

$63 a megalitre.

If we go for the midpoint, which has been suggested, half of this price is $31.70. Subtract from that the fixed costs that we are paying anyway, we come up with a price for the water of $18.87.

I was very pleased when I came up with this price because I realised immediately that it was a price that we have been suggesting is one that we would pay for. It is the price that when WaterNSW modelled the merger price of all regulated coastal valleys, they suggested that model price as $18.65. It is a price that matches very closely to what I would call a price that is effective for all of us and it compares well with the Hunter Valley irrigator's price and we know it there. We did some figures on the dairy farmers in that area. They had more effective irrigation facilities and because of their confidence with the irrigation water price, they are producing their feed at $115 a tonne compared to in our area it is much closer to $200, because of their use of efficient water at an efficient price.

For all those reasons, it really does match in that that is the appropriate price that we should be getting charged. We commend the approach that IPART has adopted. We believe that with the correct analysis of the capacity to pay, it will provide the price stability and certainty for the customers, giving us a confidence that we need to make appropriate long-term decisions.

THE CHAIR: Thank you very much, Fleur. Are you going to put this in a written submission?

MS TONGE: Yes.

THE CHAIR: Good. Chris?

MR MAGNER: With your permission, can Melissa go next and then I can follow up?

THE CHAIR: Certainly.

MR PARBERY: Chris, don't forget me.

THE CHAIR: Melissa?

MS BALAS: Thank you for that. Again, I reiterate what Fleur said. We do commend IPART for what they have done. The reports that have been done we agree with. We agree with the methodology. It is a good report. We actually looked at some Dairy Farm Monitor data that we did for our farms for 2012-13 and it shows that the cost of purchased feed came in at $0.32 a kilogram of dry matter. Agripath came up with 0.33 which I think it justifies that they are pretty close in terms of their purchased feed costs.

The fact that the irrigated costs are within 8 cents of that indicates that the current price is at our capacity to pay in terms of if it has been at 8 cents, then my recommendation to farmers would be that given the risk that irrigation comes with, you potentially have the price of water increasing, you also have the electricity prices increasing. If you would rather invest in irrigation, you invest in purchasing feed, you can purchase a hayshed and purchase equipment to implement that and have better tax advantages and have actually lower risk of managing a farm, and certainly given the Agripath report, it is something that our farmers desperately have to consider because the price of water is just so high that to upgrade their systems that have actually been in decline for so many years, a lot of them have not actually invested in the irrigation infrastructure for quite some time; the only ones who have invested in the irrigation infrastructure are the ones that have actually had damage associated with flood events that they've claimed on their insurance. It is a case of we really need to invest some energy into improving irrigation infrastructure, but it is not worth it at the current price.

Certainly, when we look at the 2012-13 data that we looked at, the percentage of home-grown feed and the percentage of energy consumed is around 55 per cent, so 45 per cent of energy requirements of feeding cows is already coming in from purchased feed.

Our efficiency in terms of raised pasture, in that year we got 4.65 tonnes of dry matter per hectare, which is dismal, and not all that data was from irrigators on this regulated river, but it shows the efficiency of our grazed pasture. Growing our grazed pasture is fairly low and it is nearing where we need to actually do a fair bit of work, but to get farmers to do that you need to actually get them to invest in irrigation infrastructure and work on that.

I think the efficiency data that you are looking at, if we take a step back, we are only talking about 18 dairy farmers that have active licences on the Bega system, the regulated system. Of those 18 farmers, not all of them are using irrigation. Some of them have already stopped and are using bought-in feed systems. Those 18 farmers produce 37 per cent of Bega Cheese's milk supply for our factory in at Bega.

There are two factories at Bega and they employ 700 people in our community. We need to secure water supply in order to secure milk supply for the factory to support our regional economy; it is critical to us.

In terms of this report, we commend IPART in terms of coming up with this efficient pricing band and we just really ask you to look at that capacity to pay in that upper limit, in that we have the opportunity here to actually make a significant change and revitalise, actually, the irrigation and our communities in the Bega region and also the North Coast. Please take this opportunity to make a significant difference to us.

THE CHAIR: Thank you very much, Melissa. I can't read your name card from here.

MR PARBERY: Richard Parbery.

THE CHAIR: You are from the North Coast?

MR PARBERY: No, I wouldn't live up there, no - from the South Coast - it's too wet.

THE CHAIR: From Victoria?

MR PARBERY: Mr Chairman, my name is Richard Parbery. I am director of Bega Cheese and have been on the board for 26 years. I am also a practising tax accountant in Bega and many of these clients on the Brogo River are my clients.

Like the others, I commend IPART on taking a different approach to full cost recovery. David seems to have the attitude that we just keep going 10 per cent, 10 per cent, 10 per cent and then there is no problems because there is no water coming into the Brogo, so we don't need to have any more of these hearings.

The bottom line is that many of my clients have infrastructure at the moment. As Mel was saying, it is old, we have pivots, we have underground irrigation, we have travellers, and none of them would be in a position to make a decision to upgrade the infrastructure.

As you all would have known, on Friday night, at 6.30, the Senate actually passed the tax bill. It was amazing. What that has done is previously, in May 2015, small businesses under $2 million, including farmers, got very substantial tax relief: 100 per cent write-off on your water, three year write-off on your haysheds, et cetera.

This change on Friday night has given our bigger farmers, of which many are on the Brogo, some very good options. If your turnover is under $10 million you can now have a 100 per cent write-off on water, which is very attractive, if David's price is right, or you can now buy haysheds and that sort of infrastructure in and get a three year write-off. What people are going to be doing in Bega now, because the infrastructure is so bad and so rundown, they have to go down a track from which it will to be very hard to turn back.

I think in the majority of cases it will be both. Infrastructure will not be upgraded much unless they get the security on this pricing, which Mel has gone through and we will resubmit that to you in writing. In terms of haysheds, the tax effect on a $100,000 hayshed is $30,000, which is very effective, immediate and gives some very, very good options of buying at the right time. These are big changes on that Senate vote. I am delighted to see it came through at 6.30 on Friday - 27 votes to 30; quite extraordinary. Obviously, it was relating back to the tax changes as well on 10, 25 and 50 million.

Thank you, Mr Chairman. Thank you IPART for getting involved on this level, but I hope we can convince you that our price now is the upper level; as Fleur very effectively said, a non-productive level and a non-profit level.

THE CHAIR: Thank you very much, Richard. Who is next? Chris?

MR MAGNER: Thank you, Mr Chairman. Chris Magner from the

Richmond River.

We have heard what Fleur has presented and just in a supporting mechanism, I suppose, the document that was presented to the Casino meeting from WaterNSW only a couple of weeks ago, within the pilot process that they're going through to try and find a workable situation for Toonumbar Dam, in that presentation they gave us a pricing in the event that we merged all the coastal valleys' prices together and if we did that, we would have a fixed charge of $9.22 and a usage charge of $18.65.

Fleur's figures have come down just about to that, accidentally or by chance or good measurement I don't know. What Fleur's figures came down to are basically the same as that. As I said earlier, if we were to move $1 off that usage charge and take it to the fixed charge, it would bring you to, basically, the current charge for Hunter River. What we are saying, and again, in the presentation, in your paper, the current proposed price is $7.40 and $45.94, plus CPI. Again, as I said earlier, for every dollar moved from one bucket to the other, if we took the North Coast, the Hunter price of $10, it brings the North Coast usage price down to very similar to the Hunter price.

There are three examples of documentation, using your figures, that show it can be done. Our original attitude was, "Well, we're going to go down and fight for an amalgamated price on the coast", and we were told, "Oh, look, there's all sorts of barriers to doing that." You've got to go through all sorts of legal loopholes and duck and dive and it could take you years to get that through. We don't believe we even have to do that now. We believe that you could make that decision here now. You can look at these figures, juggle the figures whichever way you like, but if you look at these figures that we present to you, we believe that you could come up with a workable solution for Toonumbar, for Brogo, and, for my friend over across the table here, for the Peel.

I believe that we could do all of that now not affecting one dollar of income to New South Wales Water and we could get these dams active, viable and that would then encourage new use, either from the existing licence holders or from new licence holders, but we're going through the pilot process up on the Toonumbar and we are looking at all sorts of avenues of how we can bring in new users.

We want to continue with that process. If we get this pricing resolved here today, it's going to make it a whole heap easier to get that process working and go out to organisations like councils, meatworks and other industries that we want to try to attract into that area, if we've got a reasonable price, something could be used to bring them in. If we have to stay with these prices for the next four years and come back and argue it again, there won't be any users there; it will be all over.

THE CHAIR: Thanks, Chris. Broadly speaking, the North Coast and the South Coast think that the approach that IPART suggested in their draft report is right; you're just concerned about where you land within the band.

MR MAGNER: We are concerned about one figure.

THE CHAIR: Yes, the figure where you land in the band, yes. Good. Other comments? Shane and then Ildu.

MR GEE: Shane Gee, Hunter Valley Water Users, and I am also chair of the Coastal Valleys CRC.

Looking at the three coastal valleys as one, with the current prices IPART has announced that they're proposing for the North Coast, South Coast and Hunter, with just modifying the prices for the Hunter by, what was it, say $10.50 fixed and to $12 usage, it would actually become another 300,000 extra for the entire coast, and that is dropping the usage from the North Coast and South Coast from $40 down to that $12, $13. Yes, that should encourage extra use at that lower usage fee.

THE CHAIR: We look forward to your submissions on those issues.

Do you want to say anything more, Steve?

MR GUTHREY: No.

THE CHAIR: Ildu?

MR MONTICONE: Thank you, Mr Chairman. Ildu Monticone, representing the Peel Valley.

Mr Chairman, I sympathise with our colleagues in the North Coast and South Coast. I understand IPART is doing very well in trying to strike a price that is within their capacity to pay and is at a productive level and a profitable level. However, I would just like to point out that in the Peel, IPART is proposing 54 bucks a meg; North Coast, $45; and South Coast $42. Although we are full cost recovery, we are already way above those other two valleys, so when it comes to capacity to pay, the same argument applies to the Peel.

If the proposed 80:20 ratio is adopted in the Peel, the general security usage charge in the Peel would be $18.69, which is the same sort of ballpark as these guys are talking about. Without it, it will be 55 bucks, so the 80:20 ratio is very attractive to the Peel.

I also have a document I would like to hand out to the IPART members, if I may.

THE CHAIRM: Sure.

MR MONTICONE: In the capacity to pay section of the IPART draft report, in appendix D, there is a whole spiel about capacity to pay and the fact that if irrigators could not pay, they would return their licences, surrender their licences, and usage would drop.

That section in the IPART report is not correct, for two reasons: surrender and return of licences would only occur if the entitlement charge is excessive. In the Peel Valley, the entitlement charge is reasonable. It is the usage charge that is 55 bucks. People will not return their licences if the entitlement charge is reasonable, because they can trade it in to another valley, and that has happened.

The other reason why it is wrong is that the figures - I have some figures on the third page of this handout - show that the water usage in the Peel Valley has definitely decreased for the irrigators, as a result of significant price increases by IPART. So you already have your observable downward trend in usage and you already have your broad change in customer behaviour, and it reflects the capacity to pay.

Our argument is that we have already broken through the very regulations that you have set for irrigators being able to afford the prices that you set. We are saying if you do not adopt the 80:20, there is a real need for you to go back to square one for pricing in the Peel.

THE CHAIR: Thank you very much, Ildu. Deborah has a question.

MS COPE: My question is probably more to the South Coast. Given that both the Peel and the North Coast have sort of said very strongly that they support shifting the price structure so that the usage charge drops and there is slightly more on the fixed part of the charge, has the South Coast thought about that in your context? Is it something that is also attractive to you?

MR PARBERY: Quite honestly, we have not, but we are prepared to review anything to end up with a result that will encourage our farmers to use more water. What is happening at the moment is that people are consciously not irrigating - and that is showing in our graphs; we are down to about 30 per cent. In talking to clients the other day, there are several already now looking at alternatives once this tax review that has gone through.

If water is well priced, it will cover a lot of day-to-day costs because the water is there. Water on pasture is the most effective way to produce milk. There is no doubt about that, no-one argues about that. How you guys pay that price I have no idea, but our guys are resisting that price and not using the water. We are prepared to look at anything to come up with a result.

THE CHAIR: Thank you, Richard. David from WaterNSW

MR STOCKLER: Thanks, Mr Chairman.

First of all, I would like to commend the tremendous effort from our customers. It has been a year-long journey and I am really encouraged that the discussion is at this point, albeit quite late in the determination process. It is amazing what is possible when WaterNSW, our customers and the regulator have a better understanding of the rules, and that is really when innovation starts to come to the table, so I would like to thank you for your tremendous efforts.

We are encouraged that today we have heard the Lachlan Peel, North, most recently, and the South being open, and Gwydir, all having a better understanding and wanting to look further at possibilities around fixed to variable usage. As WaterNSW, we have spent a year having this discussion with our customers and we very much remain committed to this ongoing discussion.

THE CHAIR: Thank you, David. Are there questions or comments? We have a question from Matt.

MR EDGERTON: I have a follow-up question for Chris Magner. If I understand it correctly, your proposal is that the usage charge be reduced and, to accommodate that, we would have to increase the fixed charge.

MS MAGNER: That is one of the options. Our preferred option is to look at the figures first that Fleur has presented. If we go through your process - and we think that is a jolly good process that you have developed there - we have only one concern about that process and that is that the upper limit, we believe, is not the correct figure. We have tried to demonstrate that in the presentation and we will do that in our written submission.

Bega has also been looking at the same thing and has come up with the same conclusion. We all believe that the upper limit is not set at the right point. We should be looking then for that middle limit being much, much lower.

What we are saying is that all of these three different ways of looking at it give us the same answer. If we come to the reduction of the upper limit and go through your process, we get a figure that comes to somewhere around $18 a meg on usage charge, still retaining around $7.20 on fixed. If you were to move that a little bit by even raising the fixed by $1, it would bring the usage roughly down to where the Hunter is now.

With all of the figures that you have presented to us, we are not questioning any of these charts or any of these documents; the only one we are questioning is the upper limit of the usage. Therefore, what I was trying to demonstrate in rejigging the current proposals is that you can quite easily bring down that price by moving from one bucket to the other.

THE CHAIR: I think there are two issues here. One is the width of the band. What you are saying is that you think that the top of the band, as we have calculated, is too high.

MS MAGNER: Yes.

THE CHAIR: That means your band is lower than our band; right?

MS MAGNER: Yes.

THE CHAIR: That's point one, so that is a reduced cost.

Then the second point is once you have fixed on the appropriate point within the band - even your point - there is then an issue about whether the pricing would be 80:20 or 40:60; right? With 80:20, as you know, the bulk of the price is on the fixed charge and the price on the usage is lower and vice versa.

I think it would be helpful, and I think this goes to Matt's question in part at least, if you were to give us some indication - you do not have to give it now; you can give it in your written submission - on where you guys would land once we chose the right figure. Let's say, for argument's sake, we chose your figure, your point, would you then be likely to prefer 80:20 or the current 40:60?

MS MAGNER: That question is probably the concerning question that we have out of the whole process because, as I said earlier, getting your head around a ratio is not the answer. Getting your head around viability is more the answer. Therefore, if we got that figure down to similar to the Hunter, the ratio for North Coast could be closer to 80:20 and, using the same prices, the Hunter would be probably on 60:40 because of the way that the thing works out. Rather than what the ratio ends up as, we are more concerned about getting the price right without affecting the income of WaterNSW. The ratio to us is really irrelevant; it is the affordable price.

THE CHAIR: We get that, Chris, and we look forward to your submission on that.

Now to questions or comments. Fleur do you have a follow-up?

MS TONGE: No, not a follow up, but I just have one last comment unless there is someone else who wants to speak.

THE CHAIR: There is somebody in the audience who wants to say something. Yes, Bob?

MR DOYLE: I have just a few comments. On the Hunter, we elected to go 60:40 as a ratio quite a few years ago. That has proved very successful for the Hunter. Amongst the customer base, if you look at the Hunter, the biggest water user is Macquarie Generation, now AGL. Their preferred position is 60:40. A lot of people thought they would have wanted 80:20. The reason they went to 60:40 was they would get better water security with 60:40 over 80:20. Coalmines' preference is 40:60. With irrigators, there is a range, but irrigators have settled on 60:40 on the Hunter. Irrigators on the Paterson have also accepted 60:40, and that has worked very well. We achieved cost recovery a few years ago using that system.

Just to take Chris' point, instead of looking at the ratios, a better way of explaining it is that we actually set the fixed component of what we are looking at calculating. You determine the amount of revenue that WaterNSW wants. You then set the usage price and work backwards off that to determine the fixed price. That way, what ratio you actually finish up with does not matter.

The critical thing is that by setting the usage price, you are sending the right signal to use water. At the moment, with the existing usage price, the signal is do not pump. If we can find that number - that midpoint, whatever that number is - you then calculate your other numbers backwards off that and don't give two hoots about what the actual ratio is. See where the ratio falls out and that is just what it is.

THE CHAIR: Thank you very much, Bob. Any other questions or comments? Yes, up the back?

MR PATMORE: Newman Patmore. I am an irrigator on the Barrington River. I am here on the wrong day because it is an unregulated river, but I think what I have to say is relevant.

I am pleased to see some of the people up at the front table here, with what has been said today, are finally starting to get the idea of what we are up against on the land. I have been to a number of these meetings. We just hear people talking around this hypothetical type setting of charges that goes on here, but we do not see anything in our river valley that DPI Water is doing. We pay a lot of money. When we want to find out what the actual charges are, we get the run-around.

A number of years ago these prices really blew out, I used to pay $540 for a five-year irrigation licence. In recent years our charge has been just under $2,000 a year. You can go on with all this stuff about full cost recovery, but we have to try to pay our bills. We have water flowing past our door, running out to the sea, and you extract all this money from us.

When we want to find out what the actual costs are in our valley, nobody will give an answer. The bill comes from State Water, so we get on to State Water and are told, "Oh, no, we're just the billing authority. You have to talk to" - when I first started, it was the NSW Office of Water; it is now DPI Water - "DPI Water". When we go to DPI Water, we are told, "Oh, no these prices are set by IPART". So you go to IPART and they say, "Oh, these prices have been set for X number of years and that's that". We cannot find out what your actual costs are.

IPART claim that they look at the work that DPI Water is doing. Well, you must know what the costs - actual costs - are. I am not talking about generalities; I am talking about what we can see going on on the ground, what affects us, what we are actually paying for.

In our valley, MidCoast Water does all the investigating sort of work and the experimental work and everything else. We did not ever see anybody from DPI Water. I would just like to know or I would like to ask that you publish what the actual costs are, and what those costs are for in each valley, because if you don't have those costs, then this whole thing is a complete waste.

As to what has been going on here with these discussions on the North Coast, have you considered broadening your view and looking past making irrigators pay for this bureaucracy at DPI Water? Why is a small part of the community expected to pay when everybody uses water principally from rivers?

In our own river valley, I did an exercise. If you take the number of people who MidCoast Water supply and add to their costs, I calculated that the IPART cost to DPI Water for each individual at MidCoast Water is about $2 per annum. We pay just under $2,000. If all of those people who paid to MidCoast Water were to have their payment increased by another $2 per annum, you could just charge the rest of us $150 standing charge, which would get us back to where we were originally, and you would get the same amount of revenue. I would like you to consider that and look at and change the paradigm.

THE CHAIR: Thank you very much. This is primarily on DPI Water, which is not the subject of this hearing; nevertheless, it is good to hear from you. This is about the charges for WaterNSW. We try to have the charges for WaterNSW cover the full costs in the valley. We accept we are currently talking about two valleys where that is not attainable, so --

MR PATMORE: If you expand your base for charging, you might find it is different.

THE CHAIR: Thanks for that, but we have to set the prices based on the terms of reference given to us by the government and for the organisation for which we are reviewing the prices.

Fleur, you wanted to say something?

MS TONGE: No, I am okay, thanks.

THE CHAIR: Does anybody else have any questions or comments? Any general questions or comments? Now is a good time to raise them. Yes, Melissa?

MS BALAS: Just to reiterate and end on a positive note, if we possibly can, we really appreciate all the work that IPART has done. Certainly we appreciate the energy you have put in to looking at the coastal valleys and trying to come up with a way we can actually make it work. I really appreciate all the work IPART and also WaterNSW have done and, yes, greatly appreciate the time and energy involved.

THE CHAIR: Thank you very much, Melissa. I am a dairy farmer tragic, Chris.

MS MAGNER: Could I second that and thank Scott and the team that have done the footwork. We probably have seen nothing like this in the past. We most gratefully appreciate the effort that has been put in with all the other extra reviews that were done.

Whatever the outcome of this, we believe that you people have taken a very serious look at it. We are confident that you will look seriously at the submissions that we will follow up with and we would like to thank you very much now at this point on the work that you have done.

THE CHAIR: Thank you very much, Chris. We appreciate your comments and the comments from Melissa and others. Are there any other final questions or comments? No?

CLOSING REMARKS.

THE CHAIR: That just leaves me to wrap up. I would like to thank you all very much for your participation in today's proceedings. It has been a very good session and I think we have managed to ventilate a number of important issues. It has been a great benefit to us to hear your views and we really appreciate your efforts and look forward to written submissions.

A transcript of today's proceedings will be available on our website in a few days. We will consider what has been said today and what goes into the submissions. Just to remind you that submissions can be made via the website and the closing date is 17 April.

As previously mentioned, we plan to release our final report and final determination in June 2017 and the maximum prices that we set will apply from 1 July 2017.

That brings the hearing to a close. Thank you very much and have a good afternoon.

AT 2.37PM THE TRIBUNAL WAS ADJOURNED ACCORDINGLY