

INDEPENDENT PRICING AND REGULATORY TRIBUNAL

PUBLIC HEARINGS INTO BULK WATER MEDIUM TERM PRICE REVIEW

Tribunal Members

Dr Michael Keating AC - Chairman
Mr James Cox
Ms Cristina Cifuentes

Held at Dubbo RSL
Cnr Brisbane and Wingewarra Streets
Dubbo, NSW, 2830

On Wednesday, 25 January 2006, at 9am

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1 THE CHAIRMAN: Thank you, ladies and gentlemen. I would
2 like to begin by welcoming you all to this public hearing
3 for the bulk water medium term price review. For those of
4 you who don't know me, my name is Michael Keating and I am
5 the chairman of the Independent Pricing and Regulatory
6 Tribunal of New South Wales.

7
8 I would like to begin, first of all, by introducing my
9 colleagues. My first colleague is Jim Cox on my right
10 here, who is the full-time member and chief executive of
11 the tribunal, and Cristina Cifuentes is on my left here,
12 who is the third member of the tribunal.

13
14 At the table here is Michael Seery, who is the program
15 manager for bulk water pricing, and he will be joined by
16 Colin Reid, who is the director of water at the tribunal,
17 but he is just tied up at the moment.

18
19 The tribunal is conducting this hearing under
20 section 11 of its Act. The hearing is part of a price
21 review that will ultimately result in the tribunal setting
22 a medium term price path for bulk water to be charged by
23 State Water Corporation and the Department of Natural
24 Resources from, we expect, 1 July 2006.

25
26 Before commencing hearing from the key stakeholders,
27 I would like to speak briefly about the review process.
28 The tribunal's general approach to price setting and the
29 matters its Act says it must take into account in
30 conducting an investigation were previously set out in an
31 issues paper that the tribunal released in September 2004.
32 Now, I know that is quite a long time ago, but subsequent
33 to the release of the issues paper there were quite
34 significant changes - State Water was set up as a
35 corporatised body and departmental arrangements were
36 changed, leading to the formation of what we now have, the
37 Department of Natural Resources.

38
39 Those changes meant there was some difficulty in
40 providing the necessary cost information that the tribunal
41 needed, and so the tribunal decided it would only make an
42 interim determination, and that led, in August 2005, to the
43 tribunal releasing a price determination for just one year,
44 2005/06.

45
46 In the report that accompanied that determination back
47 in August 2005, the tribunal outlined some of the matters

1 the tribunal considered important to this review. The
2 tribunal also indicated that it expected State Water and
3 the Department of Natural Resources would make submissions
4 by 30 September last. Interested parties were able to make
5 submissions up until 18 November. Indeed, State Water and
6 the department provided their submissions in the first week
7 of October last year. This was followed by a large number
8 of submissions from other interested parties which were
9 received through November 2005.

10
11 All the submissions from the various parties are
12 available for those who are interested on the tribunal's
13 web site, and the tribunal is grateful for the large number
14 of submissions that have been made to the review and,
15 indeed, for the effort that people have put into making
16 these submissions.

17
18 Some of the organisations that have made submissions
19 to the review will be presenting a case to this hearing
20 today, and I can assure you that all of the submissions
21 will be considered by the tribunal in developing its
22 findings and recommendations.

23
24 The submissions have helped the tribunal to understand
25 stakeholders' views on the key issues for the review, and
26 the tribunal is undertaking further public consultation.
27 We started with a public hearing in Sydney towards the end
28 of last year, and we are currently in the process of
29 conducting three additional hearings in regional areas, of
30 which this is one. There was a similar hearing in Griffith
31 yesterday and next week we will be holding a hearing in
32 Moree. So that covers the major irrigation areas.

33
34 A key part of the process is the review of State Water
35 and the department's operating and capital cost proposals
36 by independent consultants which the tribunal has engaged.
37 We had hoped and anticipated that the preliminary findings
38 of the consultants would be available for this hearing
39 today and that the consultants would be in fact be
40 presenting their findings at these regional hearings.
41 Unfortunately, that has not proved to be possible, and that
42 is a matter of real regret on the tribunal's part and I
43 think also on the part of you people who are also
44 participating, because getting that independent assessment
45 of the operating and capex costs is a very important stage
46 in the review process.

47

1 The tribunal does anticipate that the consultants'
2 final report will be available in mid-February, and as soon
3 as we have it we will post it on the tribunal's web site.
4 All stakeholders will be given an opportunity to formally
5 respond to that consultants' report. However, given the
6 timeframe, I anticipate stakeholders will be only given
7 two weeks to provide a formal response to the consultants'
8 report.
9
10 The tribunal does, however, anticipate providing
11 further opportunities for consultation with interested
12 parties through the course of this price review. Most
13 importantly, all parties will have the opportunity to
14 respond to the tribunal's draft determination, which is
15 anticipated to be released at the end of March 2006.
16
17 As some of you will be aware, the tribunal has been
18 involved in setting bulk water prices since 1996/97. One
19 of the tribunal's key objectives in price reform over this
20 period has been to set charges to progressively increase
21 the level of cost recovery in accordance with the agreed
22 objectives of the Council of Australian Governments back in
23 1994, but at the same time taking into account the impact
24 on customers.
25
26 The tribunal has also restructured prices to improve
27 cost reflectivity and improve conservation signals to
28 users - by "restructured" I mean changing the balance from
29 fixed to usage pricing and so on.
30
31 The tribunal last held a major review of prices for
32 bulk water services in 2001. We did have an interim review
33 last year, as I mentioned, but the last major review was
34 back in 2001. That was done with the former Department of
35 Land and Water Conservation, which was then responsible for
36 providing these services.
37
38 As I mentioned, there have been major changes in the
39 administrative arrangements since then, so that we are now
40 at the position where the task before the tribunal is to
41 actually set prices for bulk water extraction from
42 regulated rivers, unregulated rivers and groundwater,
43 starting with very different administrative arrangements.
44
45 In undertaking this task, the tribunal will need to
46 take account of a wide range of matters, as it is indeed
47 required to by its Act. These matters include but are not

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1 limited to the impact of prices on the financial viability
2 of the regulated agencies and, in particular, that is
3 important for State Water, which is set up as a
4 corporatised body, and we also need to have regard to the
5 potential impact of prices on customers, and, indeed, their
6 viability.
7
8 This hearing is an important part of the broader price
9 review process, principally because it provides an
10 opportunity for the tribunal to hear in an open, public
11 forum from the water businesses and the other key
12 stakeholders and for the key stakeholders to question the
13 propositions that are put forward by State Water and the
14 department.
15
16 Before we commence the proceedings today, I would just
17 like to say a few words about the process for this hearing
18 in particular. You have available to you an agenda which
19 indicates the order of the presenters. The proceedings
20 today are being recorded, as you can see, and a transcript
21 will be available on the IPART web site early next week.
22
23 For each organisation appearing, a presentation time
24 has been allowed, and that means we then want to allow
25 five to 10 minutes for questions. So if you have a
26 presentation time of 20 minutes, that means you can talk
27 for about 15 minutes and allow five minutes for questions.
28 I would ask presenters to stick to the allocated time.
29
30 The questions of the presenters in the first instance
31 will come from the tribunal and the tribunal's secretariat,
32 but, in addition, the tribunal has allocated a significant
33 period of time just after lunch, I think from memory, to
34 allow stakeholders to express their views on issues
35 generally so that anybody here present can express their
36 views or ask questions of State Water and the Department of
37 Natural Resources, and then we have allotted further time
38 for State Water and the department to respond to those
39 various expressions of opinion and questions.
40
41
42
43
44
45
46
47

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1 STATE WATER CORPORATION

2
3 THE CHAIRMAN: We are going to commence today with the
4 State Water Corporation, followed by the department, and I
5 therefore very much welcome Mr Abel Immaraj, the chief
6 executive of State Water, and his team to make the initial
7 presentation and his team.

8
9 MR IMMARAJ: Thank you for the opportunity to make our
10 presentation this morning. I would like to commence by
11 saying that Russell Simons and Geoff Borneman will be
12 making the presentation along with me. Russell is our
13 acting chief financial officer and Geoff Borneman is the
14 customer service manager for the central area, which covers
15 the Macquarie and the Lachlan Valleys, as well as
16 Fish River water supply. Russell is based here in Dubbo,
17 as is Geoff, and the head office of State Water is based
18 here in Dubbo.

19
20 State Water Corporation recognises it is a monopoly
21 providing bulk water services to large irrigation
22 customers, but to a whole range of customers, including
23 mines, towns, industry and, therefore, there's a lot of
24 variable requirements in the system.

25
26 By way of background and introduction, I would like to
27 cover off the process to date from State Water's
28 perspective, and also go through a brief overview of the
29 submission, rather than go through the detail. Our
30 submission itself was lodged in October last year, and
31 subsequently we put out facts sheets and frequently asked
32 questions and answers on our web site, and that has been
33 broadly disseminated to stakeholders.

34
35 At the presentation during the hearing in November we
36 provided further information and that information will also
37 be made available to our customers. We have been going
38 through an operating expenditure and capital expenditure
39 review with the IPART consultants, and we have provided
40 information in relation to the prudence of those costs, the
41 reasons for those costs, as well as the effectiveness and
42 efficiency of those costs. We eagerly await the result of
43 the review.

44
45 Going through a quick background to the submission,
46 in the submission the process we undertook was identifying,
47 first of all, what are the business drivers for State Water

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1 Corporation. There are three types of business
2 drivers - regulatory drivers coming out of the legislation
3 and the regulatory parts of legislation that drive our
4 business, and, in particular, the State Water Corporation
5 Act as well as State Owned Corporations Act as well as the
6 Water Management Act. They are the key regulatory drivers.
7 In addition, because we are large asset managers we have
8 legislation such as the Dam Safety Act, and also we do have
9 staff working on these assets, which are requirements of
10 the regulations of the occupational health and safety.

11
12 The second type of drivers is operating drivers, and
13 these relate to the operating licence that was issued to
14 State Water in July 2004. Subsequently, a revised
15 operating licence was issued - that is the issued operating
16 licence in 2005 - and State Water has recognised both the
17 drivers arising out of this operating licence as well as
18 the requirements for efficiency in the operating licences.
19 One of the key factors in this operating licence is the
20 drive for 60 per cent with revenue requirement from
21 variable charges as opposed to the current 30 per cent.

22
23 The third type of drivers are customer service and
24 levels of service required, and we have embarked on a
25 process of quantifying these not only in our customer
26 service charter, but also in our valley business plans
27 which are currently being developed.

28
29 In these business plans we are identifying the levels
30 of service that are negotiated between the customers and
31 the particular area or the valley that those customers
32 reside in, but also the type of works and investment
33 required to meet those levels of service. Having
34 identified the business drivers, we developed our program
35 structure to meet all the activities required to deliver
36 against those business drivers and the program structure
37 and costs have been identified in our submission.

38
39 The third part of our submission is the full-cost
40 recovery and the building block approach. The previous
41 determinations were based on an annuity approach, based on
42 the 30-year total asset management plan, whereas what we
43 proposed in our submission in 2005 is the building block
44 approach using the three to four-year capital expenditure
45 forecast. The building block approach requires the setting
46 of a regulatory asset base and opening of the regulatory
47 asset base for commercial business. This is consistent

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1 with all state-owned corporations in New South Wales.
2
3 The costs for which we seek recovery are three. The
4 first is the operating expenditure; secondly, a return on
5 assets with a weighted average cost capped at 7 per cent;
6 and, thirdly, a return on assets or depreciation at various
7 rates for different types of assets.
8
9 The pricing structure, which is the last part of our
10 submission, recognises the need for cost recovery based on
11 reliability of supply, so we have introduced a premium for
12 high security and general security, based on a water
13 sharing plan, as well as State Water's need to maintain
14 certain reserves in the storages for a number of years in
15 different valleys. So in each valley there's a
16 differential premium and that's been shown in our
17 submissions.
18
19 The second thing we have in the pricing proposal is to
20 move from a 70 per cent fixed, 30 per cent variable, in our
21 current regime, to a 40 fixed and 60 per cent variable in
22 the future. That was driven not only by our operating
23 licence, but we believe that submissions from customers to
24 the government in the past have asked the basic question:
25 why the water bill should be so large in a period of
26 drought for two to three years.
27
28 The third part of our pricing structure was
29 clarification and transparency of all subsidies, both
30 intervalley as well as intravalley.
31
32 The last part of our pricing structure related to
33 using one standard deviation below the long-term average
34 which has been previously used in the calculation of the
35 variable charge. That is related, as I have already said,
36 to the fact that we are moving from a 30/70 fixed/variable
37 to a 40/60 fixed/variable ratio. In a way all the pricing
38 structures proposed are interrelated.
39
40 That is a brief overview of the submission and I will
41 take you through to a brief overview today which covers the
42 Macquarie and Lachlan valleys. The Macquarie and Lachlan
43 valleys together have four major dams, two large hydro
44 storages and roughly 110 weirs and regulators.
45
46 The Macquarie consists of two dams, Windamere and
47 Burrendong, which are largely weirs flowing one above the

1 other, followed by four to five major weirs and regulators
2 and a numerous number of smaller weirs and regulators.
3
4 The Lachlan valley similarly consists of two large
5 storages, Wyangala Dam and Carcoar Dam - Carcoar on the
6 Belubula and Wyangala on the Lachlan. The two confluence
7 at Cowra. The main intention of the weirs is largely weir
8 regulation, so Lachlan, being a large system, requires a
9 large number of weirs and structures. Geoff Borneman in
10 his presentation will talk about the routine maintenance
11 program and the capital program for those services.
12
13
14 To give you an overview of the presentation, Russell
15 Simons will cover fairly quickly our regulatory asset base
16 and will also talk
17 about return on assets and about corporate costs and
18 overheads for head office. Geoff Borneman will cover
19 capital works, and then I will do a brief closure.
20
21 MR SIMONS: Thanks for that and again thank you to the
22 tribunal for the opportunity that State Water has to make
23 its presentation.
24
25 Just in talking about the regulatory asset base, which
26 is something State Water proposed in its submission, we
27 have proposed a starting asset basis of \$300m for State
28 Water. The replacement value of those assets is closer to
29 about \$2.9 billion with a replacement value of assets in
30 the Lachlan and Macquarie and Fish River in excess of
31 \$700m. This means that State Water has to have a fairly
32 rigorous and extensive program of maintenance, both routine
33 and major periodic maintenance, to keep those assets in a
34 fit-for-purpose condition.
35
36 In developing the RAB, State Water took into
37 consideration a number of issues. Ultimately what we
38 decided was that the RAB at 1 July 2004 would be equivalent
39 to the annuity that was previously being charged under the
40 old determination. That meant that there was no
41 disadvantage to customers and also, from State Water's
42 perspective, no disadvantage to them. That's beneficial to
43 State Water because any reduction in that revenue level to
44 State Water means that we then have to look at how we
45 manage our assets and the program of maintenance and other
46 activities within that reduced revenue base.
47

1 State Water considers that the RAB is a far better
2 proposal to manage revenue as it relies on
3 three- to four-year forecasts for prices rather than the
4 30-year forecasts that are built into an asset annuity. I
5 think that everybody would understand that three- to
6 four-year forecasts are significantly more accurate than 30
7 years are. Additionally, with the notion of the RAB, it
8 does allow for price adjustments to be made at the end of
9 the regulatory period or at the start of the next
10 regulatory period for any overexpenditure or
11 underexpenditure on our capital. That is significant for
12 customers and for State Water, particularly if State Water
13 overspends. If State Water overspends what was allowed in
14 their determination, then we have to ensure that we prove
15 to IPART that that expenditure was in fact prudent and
16 efficient before they will allow it to be added to the
17 pricing RAB.

18
19 The opening balance of \$300m represents what we would
20 call the discounted net cash flows of the business. That
21 is in accordance with accounting standards. We see that
22 the 7 per cent WACC is a reasonable return to State Water.
23 We worked through a range of 5.9 to 7.7 per cent.

24
25 Following on from the RAB, prices are determined based
26 on return on assets of that RAB. It's important to note
27 that State Water will be levying a return on assets to both
28 customers and the government for the government's share of
29 any costs. The return on assets is designed to provide
30 State Water, as with any other corporation, the ability to
31 raise capital through either debt or equity funding, to
32 service that capital, and to be able to pay appropriate
33 taxes and dividends as required, as would any normal
34 corporation. Following on from that, in our submission our
35 operating costs do not include items such as specific
36 interest costs, dividends or income tax.

37
38 I just wanted to talk for a few minutes on overheads
39 of this business. Where possible, State Water has
40 undertaken to ensure that all costs directly associated
41 with any valley are charged directly to that valley.
42 Examples that I have on the slide there include billing,
43 engineering costs, dam safety surveillance costs - which
44 are not necessarily controlled from a valley level but
45 certainly are specific valley costs and costs that cannot be
46 directly attributed to valleys. We allocate those on the
47 basis of salary dollars in this submission.

1
2 State Water has looked at a number of different ways
3 to allocate our overhead costs and believes that this is
4 the most appropriate. In allocating our overheads we have
5 taken the view that we should not just allocate those to
6 other allocated river costs, but they should be allocated
7 to all the operating costs that State Water incurs. That
8 includes any partly-funded groundwater costs that we incur
9 on behalf of DNR, any operating costs that we incur on
10 behalf of MBDC we charge back to them, and any other work
11 that we may do.

12
13 Overall, at a regulated cost level, the level of
14 overheads at a company level is about 25 per cent of total
15 expense. This overhead comes from our central area office,
16 which is Geoff Borneman and his crew; from our operations
17 and IT, which is based in Dubbo and Parramatta; our legal
18 and risk management, which is at the Parramatta office;
19 and, of course, head office in Dubbo, of which Abel and I
20 are part. The types of costs we classify as overheads
21 include river operations support, information technology,
22 finance, payroll, and the like.

23
24 Just to show how the levels of costs are affected in each
25 valley, whilst the company overhead rate is 25 per cent, in the
26 Macquarie valley it is 23 per cent; in the Lachlan it is
27 26 per cent; and Fish River attracts 26 per cent overheads.
28 There are 64 staff in the central area. That covers the
29 systems we have mentioned, including the Barwon/Darling
30 which is an unregulated system for which we
31 undertake certain functions on behalf of DNR. The services
32 the 64 staff cover are water operations, customer service,
33 asset maintenance, and engineering and management services.

34
35 In the State Water submission we have proposed that our
36 average sales be adjusted by one standard deviation. Now
37 there are a couple of reasons for this. One is that on a
38 state-wide basis we currently recover about 30 per cent of
39 our costs through variable charges. As Abel mentioned
40 earlier, the State Water operating licence requires that by
41 1 July 2008 we have to be recovering 60 per cent of our
42 charges through variable costs. This puts a fair bit of risk
43 to State Water as our costs are largely fixed or discretionary
44 costs. We don't have what I would term variable costs
45 in this business which vary with levels of production.

46
47 This increased risk means that we have to mitigate the

1 risk to State Water in some way. We saw that the average
2 less one standard deviation was the most appropriate way to
3 reduce the risk to State Water. Because it's based on
4 averages, there will be some high years where we will have
5 higher cost recoveries. We will also have years of lower
6 cost recovery and we expect these will offset each other.
7 However, we did propose in our submission that, if we had
8 numerous years of high-cost recovery, there would also be a
9 mechanism for IPART to make any adjustments.
10
11 I would like to thank people for their time and pass
12 over to Geoff.
13
14 MR BORNEMAN: What I am hoping to do in this presentation
15 is give you some idea of how we make decisions at a valley
16 level on capital works and ongoing maintenance. I joined
17 State Water just on five years ago. When I first met the
18 customers in the customer service committee, the first
19 impression I got was the real concern about the lack of
20 work that was undertaken on the assets. I continually
21 heard concerns that money had not been spent that was
22 allocated, that the conditions of the assets were run down,
23 that some assets could fail and really affect the basic
24 level of service.
25
26 You will see the list of assets here which indicates
27 some of the works that we have undertaken. You might ask:
28 why have they undertaken work on those assets? The simple
29 answer could be that they are in the total asset management
30 plan. That would be a simple and correct answer. Yes,
31 they are in the TAMP. The reasons they are in the TAMP are
32 outlined in the State Water submission. But the TAMP is
33 really only a tool for making decisions at a valley level.
34 It's not a decision maker; it's simply a tool. But how are
35 decisions made at a valley level? How do we come up with
36 that list of projects? I might say that's only just an
37 example of projects, not all the projects that have been
38 undertaken.
39
40 Firstly and most importantly, we consult with the
41 customers and talk to them. The type of things we consider
42 in our conversations with the customers are the condition
43 of the assets. Certain assets it would not really matter
44 if they failed. How critical are they? For example, the
45 Macquarie structure at Warren, if they were to fail they
46 would cause substantial loss of service. They are the main
47 controlling structures within the Macquarie.

1
2 The next driver or the next thing we consider in our
3 discussions is statutory issues, such as OH&S. Obviously
4 if a structure is only a business that's operated
5 infrequently, then OH&S, whilst of concern - there are
6 other mechanisms that we can use. If it's something
7 operating regularly, then OH&S can be a major concern and
8 we have to look at the seriousness of that OH&S problem.
9
10 Lastly, but certainly as important as the other
11 facets, is operating efficiency. Does the structure
12 provide the control we want for operations? Does that
13 control allow us to minimise water wastage and loss? Is
14 there a way to control that structure to reduce our overall
15 operational costs? Those are the factors considered. We
16 put together a capital works program, we put it to our
17 customer service committee, and get agreement that these
18 are the things we will undertake in a period of time.
19
20 Getting on to some specific structures, Island Creek
21 Weir was an old structure, over a hundred years old. There
22 were concerns about its structural integrity, but probably
23 equally in this case as OH&S. If I jump to the next
24 picture, that gives you the best idea of the structure. It
25 was a dropboard structure, so the way flows were controlled
26 at that location was physically two men went there and
27 lowered those things down by hand. If that only happened
28 once a year, well you put in processes for a number of
29 things for those people.
30
31 This was a regularly operating structure. We had two
32 specific drivers here. Structural integrity was a major
33 concern and the other was OH&S. This slide gives you an
34 idea of what we have there. To the left of the screen is
35 the old structure that was retained due to heritage
36 considerations. This is now a modern structure that can be
37 remotely operated, can be operated at any time, does not
38 require attendance by staff, and saves a lot of our backs
39 and, more specifically, a lot of grumbling by staff. The
40 next bit of work associated with this structure which is
41 being undertaken at this time is a fishway which is being
42 constructed on the left-hand side, at the back as you look
43 at the picture. That should be constructed some time this
44 year.
45
46 With the Lake Cargelligo Weir the primary
47 consideration was structural in this particular case. We

1 found large voids under the concrete slab, cracks in the
2 concrete slab and the upstream cut-off was not covering the
3 whole weir, leading to piping failure. In a major flood
4 this structure would disappear. It was a critical
5 structure for our operations in the Lachlan, so we needed
6 to undertake some work. This slide gives you an idea of
7 what the structure looked like. Obviously now there are no
8 dropboards, so OH&D is no longer a major issue. As I said,
9 the issues mainly revolved around OH&S. That is what it
10 looks like after we finished it.

11
12 If you look at this picture of Bumbooggan Weir - and
13 obviously there are engineers in the room, I know there are
14 - obviously it's a structural issue. You just need to get
15 on with it straight away. It's a pile of rubble that will
16 wash away. But that wasn't the main driver with Bumbooggan
17 Weir. We basically had very little control over flows,
18 obviously, from the nature of the structure. We had no
19 ability to control low flows or high flows in two
20 locations. Ability to control gives us significant
21 operational efficiency, so while you would assume it was a
22 structural issue we wanted to deal with, in this particular
23 instance it wasn't. These are before and after
24 photographs. We now have a control structure. On the
25 right-hand side is the after picture, and on the left-hand
26 side is a fishway, so we addressed the environmental issues
27 associated with the structure at the same time.

28
29 Automation - again the main driver here is efficiency
30 in water delivery which will in turn result in water
31 savings and in timely delivery so that we can adjust things
32 in real time. We don't have to physically send people out.
33 In terms of doing stock and domestic replenishment in some
34 locations, it takes our staff half a day in order to adjust
35 a structure. Now in those locations that's probably a
36 reasonable sort of approach because it may have happened
37 only once a year, but with a frequently operated structure
38 that is not efficient. It results in water losses and a
39 significant amount of downtime for staff and consequently
40 costs.

41
42 Island Creek Weir we talked about before. We are in
43 the process of finalising the automation there. That will
44 be completed this year. With Bumbooggan we are in the
45 process of completing. We have installed the control
46 cabinets. The fishway gates, the regulator gates, have
47 been tested and automated. Data communication is just

1 about to be established and the radio tower contract has
2 been let.

3
4 With the automation of Jemalong Weir, similarly, the
5 bits and pieces have reached their use-by dates, so it's a
6 matter of upgrading float wells, new power and control
7 cabinets, and upgrading the PLC logic. There's an
8 operational driver there to improve control and therefore
9 improve water efficiency.

10
11 In the Macquarie there's been a lot of work.
12 Bumbooggan Weir is a two or three hours drive from Warren,
13 so again that's real time operation, so let's say a
14 six-hour round trip for our staff to make an adjustment.
15
16 Gunningbar regulator, close to the Warren, again a
17 frequently operating structure, and that's been automated
18 to undertake real time changes of Gunningbar Creek. One of
19 the things in this presentation is the major works
20 undertaken in the Warren - Gunningbar Weir, Crooked Creek
21 and Duck Creek. That's a major project. Basically, the
22 Warren Weir and the Gunningbar Weir were past use-by dates.
23 Their structural integrity was poor, so a major project was
24 undertaken. Also, Warren and Gunningbar are not controlled
25 structures - sorry, Gunningbar is, but we also automated
26 Duck Creek and Crooked Creek.

27
28 On the bottom of that photograph you can see the
29 fishway. That's an innovative design, basically a modified
30 rock drain structure - I believe the first in the world.
31 It is very effective and a cost-effective way of
32 constructing a fishway. State Water, in conjunction with
33 the Department of Commerce and Fisheries is looking at
34 innovative ways to achieve outcomes at the lowest cost. I
35 might add that fishways have been sampled in the Lachlan
36 and Macquarie and we are getting excellent results, so it
37 looks as though we have achieved what we set out to do.

38
39 I would like to quickly go through two major projects.
40 The Burrendong upgrade - why do we need to upgrade
41 Burrendong? Firstly, it's not meeting extreme flood and
42 dam safety requirements. Simply, it's not meeting the town
43 requirement for a maximum flood. There's no multilevel
44 offtake, so there are cold water pollution issues, and also
45 concern about outlet capacity in the sense that in some
46 instances demand exceeds the outlet capacity of the dam.

1 We have progressed a fair way on this project. At the
2 moment we are basically at the stage of trying to narrow
3 down the options. We are modelling the spillway, so we are
4 working out what the current capacity of the spillway is so
5 that we may be able to modify that. We are modelling the
6 intake tower - not just taking traditional engineering
7 approaches, but looking at innovative ways of doing things,
8 such as a curtain that will run around the intake tower.
9 Modelling of that is nearing completion.

10
11 Just before Christmas we took members of the customer
12 service division to the Department of Commerce lab to look
13 at both the spillway model and the intake tower so they
14 would have a better understanding of factors we were
15 considering in that project. What we're doing with this
16 project is making sure that the emphasis is on risk
17 reduction and seeing that we can actually stage the
18 project, minimise the cost and maximise our risk reduction.

19
20 The next stage is to commence our community
21 consultation, although we have been involved with the
22 customer service committee through the process.

23
24 Wyangala upgrade. It is the same basic drivers except
25 for the fact we haven't got outlet capacity problems there.
26 We are not quite as well advanced. Wyangala is probably a
27 little bit more of a challenge in the sense that the
28 solution that is presenting itself at the moment will be
29 basically not able to be staged, and we're talking about
30 \$100m-plus. So what we're looking at is to see if there
31 are other ways of risk reduction, so we'll start the
32 modelling process of the spillways and see if we can
33 minimise costs and get risk reduction in some sort of
34 staged process.

35
36 Major periodic maintenance. As Russell indicated, we
37 have a large portfolio of assets that needs ongoing
38 maintenance. Again, the process and the drivers are very
39 similar to our capital projects - what's the criticality of
40 the asset, does it need to be done.

41
42 We have TAMP for capital projects, we have FMMS, which
43 is the tool we use for making decisions on major periodic
44 maintenance and our routine maintenance. That tool, again,
45 I must repeat, is simply a tool to weigh our decision; it
46 is not the tool that gives us the decision. So if
47 something is scheduled on for basic periodic maintenance,

1 we look at it, we make some decisions, we look at the
2 drivers, we look at the issues that I talked about before
3 and decide whether they need to be done.

4
5 As an example is at Burrendong Dam on Macquarie last
6 year after an inspection - and it was only an inspection;
7 the replacement wasn't due - we found that the ropes on the
8 spillway gates were in a degrading condition and had to be
9 replaced, so that needed to be accelerated. When we
10 inspect other things, sometimes they need to be pushed
11 back. So it is an ongoing process of assessment before a
12 decision is made.

13
14 I won't go through the periodic maintenance issues
15 listed there. I will just quickly jot through them. There
16 are some at Windemere and Wyangala, Jemalong, Booberoi.

17
18 Lake Brewster. Lake Brewster, I would like to say, is
19 the most interesting project I have dealt with in my
20 30-odd years of working. It is very much a project that
21 has been driven by our customers. It is an issue with
22 respect to water quality and operational efficiency. It is
23 a project we have been doing in conjunction with the
24 Catchment Management Authority, joint funding with the
25 Catchment Management Authority and the customers within
26 Lachlan. It is a very interesting project and the current
27 proposal is very innovative. I think it exemplifies the
28 cooperative attitude that we have both in the Lachlan and
29 Macquarie between customers, State Water and other
30 stakeholders such as the Catchment Management Authority.

31
32 Future works OH&S. Again, there's the statutory
33 requirement. Gonowlia and Torrigan weirs. The reason
34 they have been low on the priority list is simply what I
35 said before. They are dropboard structures, but they are
36 operated very infrequently. So they can be operated safely
37 through process rather than modification, but their number
38 is basically coming up when efficiencies can be reached and
39 they can be undertaken. I will hand back over to Abel.

40
41 MR IMMARAJ: Just in summary, the regulatory asset base,
42 therefore, is split into two components - that's the
43 highlight from the regulatory asset base presentation. So
44 one regulatory asset base component is dedicated to the
45 government, and roughly from the opening regulatory asset
46 base \$195m of that is a government regulatory asset base
47 and \$105m is the customer regulatory asset base. As

1 Russell pointed out, the return on assets is attributed to
2 those two, if you like, customers - the government as a
3 customer and the water users as customers.

4
5 The second point is the return on assets was set at
6 7 per cent, recognising risks that at the opening
7 regulatory asset base were only seen as being the
8 equivalent of 6 per cent weighted average cost of capital.

9
10 The third point or comment that we put in our
11 submission is the overheads largely are driven by the
12 systems and processes that are being currently developed,
13 and that needs to be recognised both in terms of where do
14 we want this business to go and how efficiently we want to
15 get there.

16
17 The pricing proposals are a package. Therefore, they
18 all hang together in many ways, and as soon as you start
19 adjusting one part of the proposal, then it has impacts on
20 the others. So one standard deviation reduction in the
21 average usage is linked to the increase in the revenue from
22 the variable component.

23
24 The decision making for both the operating expenditure
25 as well as the capital expenditure: there has been
26 extensive consultation with customers and, in particular,
27 the last three to four years of drought impacts in the
28 central area, in particular the Lachlan. The customer
29 service manager and the customer service committees have
30 been working actively to make sure that the costs were
31 absolutely minimal.

32
33 The cost shares for the current upgrades - in
34 particular, the Burrendong and Wyangala upgrades that Geoff
35 mentioned. In our current submission we have foreshadowed
36 that those that are in current upgrade program will continue
37 at 100 per cent government contribution, whereas any new
38 ones that are identified subsequently will have to be cost
39 shared. Thank you, Mr Chairman.

40
41 MR SEERY: I have a couple of questions, and I will try to
42 avoid repeating questions that I may have asked yesterday.
43 Russell, you mentioned in your presentation that the
44 calculation of the RAB was an equivalent at 1 July 2004
45 between the annuity approach and a RAB approach and that
46 there is no disadvantage to customers under either
47 approach.

1
2 My understanding of the calculation suggests that this
3 is in fact true, but only for the first year; that in
4 subsequent years there is significant increases under a RAB
5 approach to customers. I just wondered if you have a
6 comment on that?

7
8 MR SIMONS: There are differences in the two approaches, I
9 agree with that. I wouldn't suggest that they are
10 absolutely significant. What the RAB approach does for
11 State Water is to provide us with a regular stream of
12 income based on the capital expenditure that we undertake
13 and build onto the RAB rather than the annuity, which is,
14 by its own term, a finite program for the 30 years. So
15 that is the benefit to all and sundry.

16
17 The other benefit, as I pointed out, in terms of the
18 difference between the two is that you're setting prices
19 based on prudent budgets for the next three to four years,
20 rather than budgets for the next 30.

21
22 MR IMMARAJ: Just an additional comment on that: in the
23 first year, as you rightly pointed out, it is equivalent to
24 the annuity. In subsequent years, as long as the capital
25 expenditure program is negotiated with the customers based
26 on levels of service, then that should pretty much be what
27 the customers actually want to pay for and the percentage
28 when an average cost of capital is set is what is going to
29 determine what the impact will be.

30
31 THE CHAIRMAN: Can I follow up on that, which is a
32 question I wanted to ask anyway. Can you or Geoff
33 elaborate on the degree of customer involvement in
34 decisions on capital expenditure?

35
36 You mentioned the customer service committees, but
37 would it be fair to say, for example, that the customer
38 service committee has actually signed off on the proposed
39 capital expenditures?

40
41 Secondly, in assessing the proposed capital
42 expenditures, how far are they able to, if you like, make a
43 choice between price and the amount of expenditure? What
44 I have in mind, for example, is that you might deem on the
45 various criteria that something needs to be done, but it is
46 a question of how much needs to be done, and that, in the
47 end, affects the price that those customers will eventually

1 have to pay. How much information do they have, how much
2 opportunity do they have to make that sort of assessment?
3 That is the second part of the question.

4
5 MR IMMARAJ: Let me just start off and then, again, give
6 it to Geoff to talk about. You raised three points: one
7 is the extent of consultation with customers on the capex
8 program; secondly, what options are there in dealing with
9 the capex projects; and the third part is whether they have
10 signed off on the capex program.

11
12 I believe that in the options development for the
13 large dam safety upgrades, where standard driven, by
14 virtue of the fact that the customers currently don't
15 contribute a share of that cost, we have included them in
16 the customer consultation process, or stakeholder
17 consultation process, but the options for meeting those
18 different standards are ultimately decided by the
19 State Water Corporation in consultation with the
20 government, as the key shareholder paying for those costs.
21 I will leave the consultation and extent of consultation to
22 Geoff.

23
24 MR BORNEMAN: I think you hit the nail on the head. It is
25 very easy to sign off on the need for something to be done
26 in terms of the drivers.

27
28 I was just smiling as Abel was speaking because
29 I signed off on my wife buying new curtains yesterday and
30 then got home and found they cost \$2,800. Now, I didn't
31 sign off on \$2,800, I signed off on the new curtains. So
32 it is a little bit the same, I think.

33
34 I'm often surprised in State Water as an engineer with
35 the cost that is associated with a particular structure.
36 To say that customers don't have access to those numbers,
37 if we have the numbers, we give our customer service
38 committee access to those numbers. I think it comes down
39 to at some time there has got to be a degree of trust
40 between the customer service committee and State Water in
41 terms of the processes we are using to establish those
42 numbers, either in terms of our estimates or how we are
43 resourcing it in terms of competitive quotes to get that
44 number.

45
46 So to say that they don't have access to the
47 information would be incorrect; they do. If we have it,

1 I give it to them. But there are limitations in terms that
2 we always are somewhat surprised at the cost.

3
4 One particular thing that I was debating with Mary
5 yesterday, or we were talking about it again, was the house
6 at Wyangala. Now, that has surprised us, that's the cost
7 of the house at Wyangala. There is no question that we
8 need that. We have gone out to competitive quotes, yet it
9 does seem a lot higher than we anticipated, so it is a bit
10 of an issue.

11
12 MR SEERY: Your proposal to use as a consumption forecast
13 based on the long run average less one standard deviation
14 appears to me to be a risk management strategy. If I
15 understand the proposal correctly, what we would do is take
16 the revenue requirement that we calculate and divide by the
17 consumption forecasts using this one standard deviation
18 approach, and this will give us an average price to apply to
19 your customers in each valley.

20
21 In the likely event that consumption is greater than
22 the long run average less one standard deviation, then my
23 understanding is that State Water would over-recover on
24 their revenue requirement, and this could occur for each
25 year of the regulatory period. How does State Water
26 propose to deal with this outcome as part of its pricing
27 package?

28
29 MR IMMARAJ: We have also proposed that there should be a
30 clawback mechanism. In our submission we recommended that
31 at the end of the price determination period IPART should
32 review what exactly was the recovered amount and claw back
33 in the subsequent determination, so at the end of the three
34 or four years of this current determination IPART would
35 look at what exactly was the recovered amount.

36
37 The only clarification I would make is we're not presuming
38 that one standard deviation should be applied to the
39 forecast consumption, but one standard deviation on the long
40 term average which has been previously used. We might
41 come up with forecasts for the next year, but really nothing
42 that would be of any use in the price calculation. So what
43 we suggest is one standard deviation for the long term
44 average and at the end of the price determination period
45 a claw back for IPART to claw back the over-recoveries.

46
47 MR SEERY: Thank you.

1
2 MR COX: Thank you. If I may, I would like to take you
3 back to the first question asked by Michael Seery, because
4 it is something that I find personally troubling, and I
5 would like to give you the chance to address it.
6
7 I think the issue raised by Michael is shifting from
8 the annuity approach to the RAB approach, particularly
9 given your large proposed capital works program, will lead
10 to a rapid increase of prices for users, whereby sticking
11 to the annuity approach would stick with a flatter period
12 of profile of recovery of costs for users. That is my
13 understanding of the factual situation.
14
15 My questions are - and you can answer these later, you
16 don't have to answer them now - is that your assessment of
17 the situation and, secondly, if it is, why is this a fair
18 thing? I would very much appreciate your comments on that.
19
20 MR IMMARAJ: We will take that on notice because the
21 second part, in particular, does require some analysis, but
22 as I mentioned, if the capex is prudent, then we do have to
23 make decisions about when do we need to invest that and
24 what sort of options we come up with, and the proposal is
25 that we do consult with the stakeholders that will be, in
26 the end, paying for it in determining what options we adopt
27 in our capex program, and that, to me, is what will
28 determine prudent and efficient capex that should
29 eventually be capitalised into the RAB. Because that goes
30 both ways - into the government RAB as well as customer
31 RAB - the question is raised at both the government as well
32 as at the customers as to what should State Water be
33 spending on its asset base to maintain services.
34
35 MR COX: I would very much appreciate your further
36 thoughts on that because I think there is a lot to be said
37 for moving from annuity to RAB. This is the most troubling
38 aspect of it, and we would appreciate your comments.
39
40 MR IMMARAJ: Thank you.
41
42 THE CHAIRMAN: I think, in terms of the interests of time,
43 we are well behind, I would like to close the session for
44 State Water now. The reason why we are behind is it is
45 really important to hear what State Water has to say, and
46 we thank you for that and particularly your response to the
47 questions from our part. So, again, I thank you for your

1 presentation.
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1 DEPARTMENT OF NATURAL RESOURCES

2
3 THE CHAIRMAN: I now call on the representatives of the
4 Department of Natural Resources to come forward.

5
6 MR O'NEILL: Good morning, everybody. I would like to
7 thank IPART for inviting DNR to present to stakeholders and
8 to themselves today. My name is Rob O'Neill from DNR. I'm
9 the acting manager of water planning policy and regulation
10 unit in the water management division in Parramatta.

11
12 I have got with me a cast of thousands here, and that is
13 partly because we have two regions here today that could be
14 potentially represented by stakeholders, so we thought it
15 was important to cover everybody. I have Paul Wettin here
16 , the manager of water management services; I have
17 Rick Rundle, the principal policy analyst; Matthew Cooper up
18 the back from Allen Consulting Group, who worked on our
19 submission; I have Richard Hicks in the back row from far
20 west, he is the manager of science and information; and I
21 have Sheridan Maher, the manager of water planning also
22 from far west. Today myself and Paul will be making formal
23 presentations, but of course the other members are here to
24 answer any specific questions that may be asked.

25
26 We will cover three parts today: I will provide a
27 very short background; also an overview from a state-wide
28 perspective of our submission; and then Paul will do quite
29 a detailed presentation on the cost drivers from a regional
30 point of view.

31
32 In terms of background, the state-wide issues were
33 covered fairly comprehensively at the November hearing, so
34 in the interests of brevity today and due to our time
35 constraints, I'm not going to go into the details and
36 reiterate everything that was said there, but I will give
37 an overview from a different angle and hopefully explain
38 some of the key issues a little better. Paul will cover in
39 detail historical activities from '01 to '05 and then also
40 talk about the forecast activities that are driving costs.

41
42 So state-wide overview. I thought it was important to
43 talk about cost recovery for the department, and I thought
44 I'd take a different angle than previously, the top-down
45 approach, and talk some numbers, which may or may not be
46 useful.

47

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1 In terms of total DNR budget, in the budget papers for
2 05/06 we are talking about \$423m. Now what we do is come
3 down to our WRM activities, and we go through a bunch of
4 exclusions. The first step of exclusion, of course, is to
5 eliminate the land use, soil and veg activities, coastal
6 and estuaries program and the DG and support staff. That
7 brings us down to what we call a rivers and groundwater
8 program, and in the current budget papers that's \$134m.

9
10 Now, we exclude again a number of items that are
11 funded specifically from grants - for example the NHT for
12 salinity management, the GAB funding for cap and pipe the
13 bores or specific government water fund for wetlands or
14 Living Murray initiative. We also exclude DBBRC and MDBC
15 costs. It is not as much of an issue in this valley as it
16 was yesterday in the Murray-Murrumbidgee. Water resource
17 management activities carried out by CMAs are also
18 excluded, and, finally, the water consent transactions are
19 excluded from our WRM activities because the costs of those
20 will be recovered separately.

21
22 Finally, that leaves us with what we're calling WRM
23 activities. There's a little bit of a cross-mixing here.
24 I have actually incorporated the forecast figure there, but
25 I guess by way of demonstration it is still reasonable to
26 show that.

27
28 So \$53m is the average of the forecast figure for the
29 post 06/07 period. If we go down into some detail into
30 that figure, then we have got another level of exclusions
31 that we go through. Now, that is the decision framework
32 outlined in our submission. There are a few levels of
33 exclusions there. First of all, we eliminate the
34 ministerial and parliamentary services. The activities are
35 analysed for whether they are past legacy impact or past
36 activities or future ones. We eliminate the legacy
37 component. We then look at what we define as a minimum
38 environmental standard and any activities required to
39 exceed that are also excluded. In our submission we
40 identify that the standard we are calling minimum is our
41 water sharing plans.

42
43 Now, after that is done, that comes up with user
44 shares for each of the activities. This share could be
45 anything between zero and 100 per cent, and the details of
46 those shares are outlined in appendix 3 of the submission.

47

.25/1/06 26 DNR

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1 That brings us down to what we're calling costs
2 attributable to water users, so about \$45m. Again, these
3 are indicative figures, so they are by way of example.
4
5 Now, we call that full cost recovery amount if we get
6 that amount, which represents about 85 per cent of all WRM
7 activities or, conversely, you could say 15 per cent of the
8 WRM activities after all those other exclusions are made,
9 we're saying, are not attributable to water users.
10
11 Now, effectively, between that attributable cost, full
12 cost recovery, and the actual costs that are recovered is
13 what we're calling a subsidy. This subsidy is, of course,
14 a function of the determination made by IPART on
15 appropriate user percentages and, of course, the price path
16 to achieve that ultimate target recovery.
17
18 Just to give you some more example numbers in terms of
19 historical figures, WRM activities for the period 01/02 to
20 04/05 are approximately \$43m for the actual costs.
21 Attributable costs. Using the previous IPART determination
22 of a weighted average of about 65 per cent gets us to about
23 \$28m.
24
25 The notional revenue for that period - now, we're
26 calling it notional because it is based on average use and
27 the price is set by IPART for that period - comes in at
28 about \$17m, which represents about 39 per cent of the
29 historical WRM costs. Now, that, again, using the word
30 "subsidy" equates to approximately an \$11m subsidy.
31
32 In terms of the key proposals in the submission, there are
33 just three that I want to quickly go through before I hand
34 over to Paul. First of all, there's a simplified tariff
35 structure that we are proposing. The second one is the
36 removal of discounts for irrigation corporations, which
37 , again, is a much more significant issue in
38 Murray-Murrumbidgee, but of course we have Jemalong in
39 this region, and finally the removal of security premiums on
40 licences.
41
42 So the simplified tariff structure, first of all,
43 recognises, of course, that State Water and the Department
44 of Natural Resources are now separated, which means WRM
45 activities are now DNR's responsibility.
46
47 WRM has two major functions: it protects the

1 entitlements, of course, and the second one is it protects
2 the environmental standards - as I said, the minimum
3 standards, as we're calling it. Now, we're proposing that
4 WRM charges are based on entitlement. We do recognise that
5 there are variations between water sources and valleys.
6
7 In the submission we allude to possible
8 groupings - north/south in reg systems, possible groupings
9 of east/west in unreg systems and also possible groupings
10 on groundwater in terms of highly managed or other, as we
11 call it. Now, we're only making proposals there, and I
12 guess ultimately it is IPART's determination of which way
13 to go.
14
15 We also recognise that from year to year WRM
16 activities will vary, and Paul will give a lot more detail
17 on that and you will get a much stronger picture of the
18 variations over time. There are two causative factors
19 there, the first one being the stage of the planning cycle
20 we are at and also there is a climatic cause there.
21
22 Water resource management we are asserting is not a
23 function of water delivered. We are also asserting that it
24 is not a function of licence class or security. It has
25 been mentioned that if that is the case, then there is no
26 incentive for users to be efficient, but it is our position
27 that the tradability of savings encourages efficiency,
28 effectively.
29
30 The second major issue is the removal of security
31 premiums. Again, WRM is separated from water delivery so
32 we assert that WRM is not a function of the security on the
33 licence. The costs of WRM. Effectively, if you go through
34 all the activities and break it down one by one, the
35 monitoring and management of WRM, there is no direct effect
36 of security on licence in those. Cost delivery, as we have
37 said, is effectively a responsibility of the State Water.
38
39 Removal of discounts. DNR is proposing to remove
40 those discounts. As I said, it is not such as significant
41 an issue in this valley as it was in the
42 Murray-Murrumbidgee, but the background to those is we
43 recognise that they were originally granted mainly for
44 metering services undertaken by ICs. Separation of DNR and
45 State Water means that effectively that service is more
46 relevant to State Water, and they covered that in their
47 submission. DNR is no longer responsible for those

1 services.
2
3 Removal of the discounts. It is our position that,
4 effectively, the increased charges for ICs will result in
5 reduced charges for other users in the valley, but no net
6 difference in our revenue.
7
8 Now, what we are saying is we are still open to negotiation
9 on the WRM component of those activities. It was
10 mentioned yesterday that there is a study being commissioned
11 to look at the WRM services provided. We want
12 to look at that and the quality of the data that is output
13 from those services, and we want to agree on a level of
14 benefit that they provide to DNR and then ultimately come
15 up with some sort of agreed figure to cover that.
16
17 That is a really quick overview. I will hand over to
18 Paul to go through some detail on regional specific cost
19 drivers.
20
21 MR WETTIN: Thank you, Rob, and thank you to the tribunal.
22 Firstly, I would like to offer an apology from the regional
23 director for his absence today.
24
25 I'm going to talk basically about the regional
26 operations component of the IPART submission and try to
27 provide some detail as to the nature of how the business
28 has changed. The tribunal asked for a review of how things
29 have changed in the last five years, so I will run over
30 that fairly quickly in terms of program activities - those
31 that have continued, those that have been deleted, or
32 efficiencies that we have undertaken. I will then provide
33 a bit of a resources overview, and then I will go into
34 '06/'07 and give some detail in terms of the proposed
35 activities.
36
37 To start with '01/'02, most of us in the room would
38 realise the major change in the nature of water resource
39 management during that period. We were removed from the
40 old Water Management Act, which was long past its use-by
41 date, into the new era of water resource management under
42 the Water Resources Management Act. The '01/'02 period
43 was also the commencement of the water sharing plan period,
44 so there was a major period of extra preparing of plans. In
45 the central west we have six plans which cover about 80
46 per cent of the extracted water use. There are two
47 regulated plans, two unregulated plans, and two groundwater

1 plans.
2
3 That period was also drought-dominated. The last
4 flood period we had in both valleys - and it was a fairly
5 wet year in '01/'02 in the Macquarie, not so wet in the
6 Lachlan - the last flood in the Lachlan was back in 1998.
7 So we have been very much in a drought-dominated system
8 which creates a number of pressures, particularly in terms
9 of demand for groundwater. There has been a very strong
10 demand on groundwater during that period because of the
11 shortage of surface water resources.
12
13 For the '01/'02 period and '04/'05, I will cover the
14 three areas of water administration, strategic support and
15 technical support. Over that period the water
16 administration area continued to provide assessments of
17 water licence applications under the Water Act, but also
18 progressively into the Water Management Act for both
19 surface water, groundwater, controlled works on flood
20 plains, and controlled activities on rivers and foreshores
21 - the 3A permits. It dealt with renewals of consents, so
22 it was a renewal period that had to be dealt with; the
23 transfers of water consents, largely with the permanent
24 water transfers; the usual thing with complaint resolution
25 which, once again, during a drought period tends to be at a
26 higher level than if you have lots of water around; and
27 special projects dealing with amnesty registrations, the
28 volumetric conversion process where the unregulated
29 licences went from an area base to a volumetric base, which
30 is a major change; and the development of water sharing
31 policies as well.
32
33 In terms of resourcing of water administration, the
34 staff in large remained fairly static in terms of numbers
35 of staff, but there was an actual workload increase, so, if
36 you like, a backlog, particularly in terms of consents
37 built up over that period because of the changeover in
38 terms of the consents required by the different Acts.
39
40 Strategic support: what I am talking about here is
41 the support provided to the water sharing plan process and
42 particularly the water management committees. Strategic
43 support dealt with at the consultation - supports for these
44 were the officers that were involved in providing direct
45 support to the water management committees. It also dealt
46 with the operational costs. The committees were all
47 ministerially appointed, so they were entitled to sitting

1 fees, and they were quite substantial costs, both in terms
2 of accommodation and food and sitting fees.
3
4 There was the ongoing macro plan process that's still
5 going on, so that strategic support is still being provided
6 but in a different way. The changes in efficiencies that
7 have occurred during that period is that four water sharing
8 plans commenced in July 2004. The two groundwater plans
9 are operating on an interim basis, but are proposed to
10 commence in '06. Some of those facilitation staff have
11 been re-employed, either into the macro plan process or
12 into other water resource management related activities,
13 but also some of the staff departed during the department's
14 recent process of reducing numbers when voluntary
15 redundancies et cetera which were made available.
16
17 One of the major changes in terms of operating
18 efficiencies is the reduced operational costs that were
19 going to those water committees.
20
21 Technical support is the third area. That covers
22 three main areas: river and wetland ecology and water
23 quality area, the hydrogeology, and hydrometrics. The main
24 activities undertaken in these areas are the monitoring and
25 reporting on resource condition, and response to water
26 management actions. They include things such as the real
27 time measurement of river flows, largely for the operations
28 of State Water; groundwater monitoring, and ecological
29 responses to environmental water delivery. This group
30 continues to provide technical support to water committees
31 and water sharing plans and it also provides technical
32 support to water administration in terms of licensing
33 consents and also development consents, so that's
34 environmental impact statements and the rest.
35
36 A major change in that period was a shift from support
37 and development of water sharing plans and implementation
38 activities. Early in the period it was about providing
39 support to the committees, whereas now most of the effort
40 goes into implementation of the water sharing plans, but
41 there is still support provided into the macro planning
42 process. There was a need to reduce and eliminate programs
43 and activities due to, one, the need for greater
44 efficiency, and that was recognised, but also loss of staff
45 or access to funding sources. Major examples of that are
46 that we rationalised the groundwater monitoring network,
47 and that was something that was needed. There was, if you

1 like, redundancy in the network in terms of numbers of
2 sites, but also site visitation, so we had a major review
3 in that area to make the groundwater networks more
4 meaningful in terms of what was required by site visitation
5 and the overall running costs of that.
6
7 Because of the loss of staff, we were forced to mothball
8 basically the entire hydrometric network in the unregulated
9 streams. We have brought that back on line in this financial
10 year, which I will talk about later. We ceased undertaking
11 the key sites water quality program. We ceased
12 undertaking a number of studies on water management
13 that were undertaken under NHT1. Geoff Borneman may
14 mention the Lake Brewster work that is being undertaken at
15 the moment. That work actually arose out of an NHT funded
16 study that was undertaken jointly by the department and the
17 river management committee, and that's the lower lakes
18 water quality study. With Lake Brewster there were
19 problems with water quality and pollution of the lower river
20 from releases thereof. Another example is a range of
21 studies in the Macquarie Marshes, including groundwater and
22 river red gum monitoring.
23
24 The overall summation of what happened in this period
25 is that we had 43 positions in '01/'02 and as of '04/'05
26 there are 23 positions remaining.
27
28 Moving into the forecasts for '06/'07 and beyond, the
29 main drivers are, once again, implementation of the water
30 sharing plans including the current macro plans when they
31 are implemented; the ongoing changeover from the Water Act
32 to the Water Management Act; and the meeting of the
33 national water initiative's obligations. There is also a
34 need to undertake resource condition monitoring and
35 reporting through the catchment action plans and Natural
36 Resources Commission, but as Rob stated in his
37 presentation, there is insufficient information available
38 at the moment as to the actual requirements for resource
39 condition monitoring under the catchment management plans
40 and the Natural Resources Commission will compile a
41 requirement from that. That has been excluded from the
42 total water resources management costs at this stage.
43
44 I will give a general summary now on an activity basis
45 according to the new activity schedule that was in the
46 department's submission.
47

1 The first activity is the surface water information
2 activity area which is forecast to decrease expenditure
3 versus that for '04/'05. This is to meet State Water's
4 operational needs, but also water sharing plan needs,
5 particularly on unregulated streams. What we are
6 forecasting is that there will be a need for an additional
7 four hydrometrics staff. We have appointed an additional
8 four hydrometrics staff this financial year. As a
9 consequence of that, we'll be able to re-open those
10 hydrometric sites we mothballed over the last couple of
11 years, but we will also require four additional hydrometric
12 staff for '07/'08 for additional flow monitoring and
13 reporting, including assistance for ecological reporting
14 requirements.
15
16 Groundwater information: there is increased
17 expenditure versus '05, once again to meet water sharing
18 plan needs. Partly this is related to the increasing
19 reliance on real time data collection and data loggers and
20 telemetry, particularly in the highly managed groundwater
21 areas. Eventually this will lead to efficiencies down the
22 track once telemetry and the rest is established, but you
23 actually need additional staff to install those because
24 they are highly specialised staff who look after the
25 telemetry and data logging systems. These resources are
26 included in those four additional hydrometric staff that I
27 identified above. I should also point out that the New
28 South Wales Government has provided the capital funding to
29 do the installation of the upgrades in the first place, so
30 the monitoring network, the new laws, and the use of data
31 systems are actually being provided by the New South Wales
32 Government.
33
34 Surface water and groundwater analysis is the next
35 program. This is the analytical services provided by our
36 water analytical laboratory, things like what's the quality
37 of water, whether it be groundwater, blue-green algae
38 analysis, and the rest. It's fairly minor, but it's an
39 essential service that has to be provided in some fashion.
40
41 The next major area is water modelling and impact
42 assessments. Once again, this is not something that's done
43 in the region but it's done by our central office, by our
44 hydrologist. We are solely reliant on that service. It is
45 run from central office and it is absolutely fundamental to
46 the water sharing plan implementation, particularly in
47 terms of assessing plan limit compliance, and I'll talk a

1 little bit about that further on.
2
3 The other component of this is that we are moving the
4 water modelling into linking the hydrology models with our
5 ecological information that we obtain from programs such as
6 integrated monitoring of the normal flows, and it's also a
7 major partnership area with the new water CRC, so it's a
8 major program in terms of linking hydrology with the
9 ecological models. We have a high degree of predictive
10 capacity or water scenario capacity in hydrology, and most
11 of the stakeholders in the room would be aware of that.
12 What we don't have is that similar predictive or what-if
13 scenario capacity for ecological outcomes, so this is a
14 major investment area that we believe is critical to
15 follow.
16
17 The major area I want to talk about now is water
18 sharing plan implementation. It's the largest area for
19 increased activities. Some of it relies on the activities
20 I spoke about. It covers the four current water sharing
21 plans, the interim groundwater plans and the two macro plan
22 areas. Some of the macro plan areas we anticipate will
23 require some additional effort. For example, the upper
24 Lachlan groundwater will end up being a highly-managed
25 area, so there will be some decisional activities perhaps
26 to parallel the lower Lachlan groundwater area as well.
27
28 Each plan has specific commitments and I am going to
29 run through some brief things about additional activities
30 required for each of those plans so that you will get a
31 feel for it. This is not a complete list; this is just a
32 run through some of the additional activities that are
33 required.
34
35 The Lachlan regulated plan, one of the major things
36 about the hub of the plan is the plan limit assessment and
37 this is undertaken by a compliance and assessment advisory
38 process. This is an industry-appointed advisory committee
39 under the water sharing plan. It will require operating
40 costs and it will require technical support, such as the
41 hydrological modelling I spoke of. The plan requires a
42 review of what's called the 250GL inflow trigger into
43 Wyangala Dam, which is a trigger for the translucent
44 environmental flows being available. That review is
45 required in year five of the plan.
46
47 Currently there is a trading barrier at Lake

1 Cargelligo that restricts permanent water trades across
2 that barrier. Temporary trades are still allowed, but
3 there's a commitment in the plan to undertaking a
4 socioeconomic and environmental review of that area. There
5 is also an annual reporting requirement to the catchment
6 management authority and subsequently interim five-year
7 review by the Natural Resources Commission.

8
9 Going back to my slides now, with the Macquarie
10 regulated plan one of the major things is support for the
11 environmental flow reference group, which is again an
12 administratively-appointed group with operating costs.
13 Once again you have the compliance assessment advisory
14 committee and there were some specific requirements in
15 terms of review of the plan.

16
17 The lower Lachlan groundwater plan has once again some
18 specific requirements. We are currently finalising the
19 sustainable groundwater tolerance program. There is an
20 ongoing process of review of recharged environment and
21 extraction provisions, and there is a reporting
22 requirement. The lower Macquarie groundwater plan has,
23 once again, similar requirements, particularly in terms of
24 the recharge of environmental review extraction limit
25 provisions.

26
27 Water resource management planning covers a wide range
28 of planning activities. A large element of these Rob
29 covered in his submission. It also covers, as I already
30 mentioned here, that there will probably be some residual
31 work in terms of planning for a couple of areas: in the
32 central west in terms of the upper Lachlan, the life of the
33 river and some of the flood plains. It also includes major
34 activity such as wetland recovery plans, CMA support, dam
35 impacts on water quality.

36
37 The water consensus administration program, the future
38 forecast is not dissimilar to what we have been through so
39 far. I will not go through that in detail; it's on the
40 slide. As I mentioned, resourcing levels are similar to
41 what they were in '01/'02, and the same with the water
42 consensus transactions.

43
44 I would just like to talk about additional water
45 management activities in the central west to follow on from
46 Rob's general presentation. There are a range of
47 activities that are being undertaken that are being funded

1 by New South Wales Treasury in terms of enhancements in the
2 central west. To run through what they are, there's \$10.6m
3 for the wetland recovery projects in the Macquarie, and we
4 are hopeful that the National Audit Commission will provide
5 matching dollars for that; \$1.3m, which I made reference to
6 in terms of installation of groundwater monitoring bores;
7 about \$400,000 is being spent on enhancement of the
8 integrated monitoring event flows program; and additional
9 dollars are being sought for expansion of the water
10 extraction monitoring network in the groundwater areas; and
11 also additional money to enhance the hydrometric network,
12 particularly on unregulated schemes, and that's within the
13 DNR submission. There is also additional funding being
14 provided from catchment action plans and also a recently
15 announced allocation of \$105m under the riverbank fund.

16
17 To summarise, the central west forecast is driven primarily
18 by implementation of the Water Management Act and
19 the water sharing plans. The water sharing plans require
20 significant support and contain many studies, particularly
21 within the first five years. River environments in the
22 central west have been and will remain areas of public
23 focus. For those of us involved with the Macquarie
24 Marshes, the National Parks Association has just announced
25 a major program in terms of restoring the Macquarie
26 Marshes. They are an international icon and that issue
27 won't go away. It actually requires large public
28 investment to manage that issue. There is a significant
29 level of increased government investment in improving river
30 and wetland health, and the issues of the CMA and NRC
31 requirements are still evolving but will require additional
32 resources. Thank you.

33
34 THE CHAIRMAN: I thank the department for its
35 presentation. There is limited time for questions.

36
37 MR REID: Thanks very much. I would like to ask three
38 questions. One relates to this top-down approach to
39 assessing what the attributable cost is. The second
40 question relates to the user, the government share, and the
41 changes in that. The third question is a repeat of one
42 that was asked yesterday and that relates to metering
43 unregulated rivers.

44
45 The top-down approach you showed, Rob, is very useful
46 in demonstrating the total cost, obviously, for the
47 department, and the extent that that total cost is covered

1 by moneys from other sources and attributable to
2 other activities. Paul has outlined the
3 bottom-up approach as to the actual
4 activities that are being undertaken. But unlike State
5 Water, which has an operating licence and there is a public
6 reporting mechanism that they actually achieve and maintain
7 customer service levels and performance standards relating
8 to their budgets, I am just wondering what's in place so
9 far as DNR is concerned as far as a comprehensive public
10 reporting mechanism is concerned to demonstrate to
11 customers that they are actually achieving what is
12 associated with the costs that are being incurred?

13
14 MR RUNDLE: DNR does participate in the customer service
15 committees, as required, and we do have representatives who
16 attend customer service committees, providing information
17 through that venue. We don't actually at this stage have a
18 formal process of consultation, as does State Water.
19 Because of the nature of WRM, I guess we have a far wider
20 range of stakeholders in terms of what's attributable in
21 terms of WRM costs. Primarily we deal with the
22 environmental groups, government, and water users. At this
23 stage in the development of WRM as a business function,
24 that process hasn't been taken any further, but certainly
25 we will be looking at that in future in terms of developing
26 a forum for providing information to customers.

27
28 I suppose there's the other general sorts of
29 information provision which we provide through publications
30 and information on our web site, and information through
31 regional offices. Certainly there is a lot of liaison
32 through staff in regional offices. That's the sort of
33 general response I can give at this stage.

34
35 MR WETTIN: Can I add to that? Certainly with the
36 hydrometric business that we provide to State Water, that's
37 according to a local service agreement, so at least that part
38 of the business is according to the requirements that State
39 Water wants to be met for their river operational purposes.
40 For other parts of the business, Rick is right to some extent.
41 We are at the behest of other stakeholder groups in
42 providing information. I would point to advisory committees
43 on the water sharing plans where they can request any
44 number of things from the department to service that, so we
45 are not really in control of those sorts of requests. Nevertheless,
46 we are accountable to catchment management
47 authorities and the Natural Resources Commission

1 in terms of the deliver of those services and they will be
2 undertaking reviews of how we provide those services,
3 particularly how our water sharing plans are implemented.

4
5 MR REID: You are proposing some significant changes in the
6 government user share of costs. Obviously in total there's
7 a significant increase in the costs it is proposed that
8 users pay. I am wondering if you can give us an indication
9 of that increase in costs proposed to be paid by users, how
10 much is attributable to new or additional activities and
11 how much is attributable to the change in the government
12 user share?

13
14 MR O'NEILL: I can give a brief answer on that; Paul might
15 want to add something to what I say. I guess the first
16 part of it is to recognise that State Water and DNR are
17 separated, so we are talking about water resources
18 management activities now. I guess by way of some detail
19 you can look at the 12 activity groups in our submission
20 and one by one you could go through them, which is
21 effectively what we did. Each one goes through the
22 process, as we said, that there is a framework of
23 decisions, the first step being the legacy part, the second
24 step being is it directly attributable to users, and then
25 finally, if it's not directly attributable, how much of it
26 is? We decide what's attributable to the minimum standard.
27 If it's to the minimum standard, then we are still saying
28 it's attributable to users. We call that minimum standard
29 the water sharing plans. Anything in excess of that will
30 be funded by government.

31
32 I thought also, to give you a couple of examples,
33 specifically we could look at some of those activity
34 groups, and Paul certainly gave a lot of detail in his
35 presentation, but from a simple point of view, for example,
36 our surface water information and groundwater information
37 groups are both required, irrespective of any other
38 factors, so we need to have some knowledge of what's there
39 and we need to understand what's going on. We have
40 operation and compliance issues with our water sharing
41 plans. We feel all of that should be passed on to users.

42
43 I could go through each one in detail, but I won't.
44 Basically the end result of that decision framework comes
45 up effectively with our 85 per cent recovery.

46
47 MR RUNDLE: I think, to make a comment, one of the primary

1 drivers of the increase in the cost share that we are
2 proposing is because the benefits under the water sharing
3 plans and the new water access framework, which primarily
4 is a benefit to the water users, the licence holders, and
5 we have seen a decision framework that actually does
6 allocate costs accordingly 100 per cent to users where that
7 is the case. That's been a shift in the WRM activities
8 over the years to more of a, if you like - we are not using
9 the word "beneficiary" so much in the submission, but in
10 fact that's the case. We see therefore that's the primary
11 reason for a larger share of recovery. There are other
12 activities that we consider, but the previous cost shares,
13 based on the same product basis, were too low.
14
15 MR REID: One of the questions raised yesterday was the
16 question of metering on unregulated rivers, but it may be
17 more applicable to today's hearing. A number of users have
18 obviously over time installed meters based on the
19 department's intention to charge on a usage basis for
20 unregulated rivers. What is the current status of the
21 department's position on that, because obviously for some
22 of these users who have gone to the cost of installing
23 meters where there has been no move to date to usage
24 charging, it has created a cost for them for no obvious
25 benefit to them.
26
27 MR RUNDLE: If I could just make a comment, the primary
28 reason the metering is not really for the purpose of
29 billing, for water charging; it is really for operational
30 purposes coming under the water sharing plan process.
31 So the metering program will continue to cover unregulated
32 rivers and groundwater for that purpose.
33
34 The metering for billing purposes is secondary and we
35 are certainly not advocating that we actually bill for
36 that on a two-part tariff basis. In any event, we're
37 advocating a single access charge.
38
39 We have got a prerogative to implement the metering
40 program through the national water initiative, and that is
41 primarily for operational requirements, and that would
42 satisfy the NWI requirements. The tariff issue is
43 effectively separate from that.
44
45 THE CHAIRMAN: We are now half an hour behind schedule,
46 so I would like to wind this session up. I would like to
47 again thank the Department of Natural Resources for their

1 contribution. We will have a tea and coffee break, and
2 I would like to try to resume in about quarter of an hour.
3

4 SHORT ADJOURNMENT
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2
3 THE CHAIRMAN: I would like to now call on a
4 representative of the Lachlan Valley Water to come forward
5 and present.
6
7 MS EWING: Thank you. Mary Ewing, the executive officer
8 for Lachlan Valley Water. I will be doing all of our
9 presentation on this. Thanks for the opportunity to speak
10 at this hearing. We will address the issues that you have
11 flagged as key ones, and on opex we would like to confine
12 ourselves to the principles and speak about detail when the
13 PB Associates report is available.
14
15 In terms of the principles, IPART's 2005 determination
16 found that the Lachlan was already at full cost recovery.
17 We are, therefore, surprised that State Water is projecting
18 a 50 per cent increase from round about \$3.1m to \$4.5m now
19 and are still claiming that that is full efficient costs.
20 We don't believe it is an efficient level of costs and the
21 MJA Cardno report last year supported that feeling.
22
23 With the inefficient level of costs we are concerned
24 that the business practice that State Water have used, the
25 zero budgeting method, is not actually producing efficient
26 cost levels. It is not an appropriate method of operating
27 a business that is in a monopoly position. We believe the
28 \$4.5m that State Water is now saying it is going to cost to
29 operate the Lachlan is a reflection of their monopoly
30 position, rather than a reflection of fully efficient
31 costs.
32
33 We are concerned particularly at the apparent increase
34 in the costs of corporatisation of State Water - \$2.7m was
35 what it was quoted in the 2004 State Water submission, it
36 is now up to \$8m, and from our point of view there's a lack
37 of justification for that increase.
38
39 We had some discussion earlier this morning about the
40 input that customers have to costs for level of service and
41 the input that the customer service committee has. As we
42 noted in our submission, the customer service committee
43 actually is not having informed input into that.
44 State Water's 2005 submission was prepared without input
45 from the Lachlan customer service committee. It was after
46 the event that the customer service committee was able to
47 see some of those costs, and our concern is that there is

1 not the opportunity for customers to have input into the
2 trade-offs between the cost of service and the level of
3 service to be provided, and I think that is one thing that
4 certainly in the Lachlan we are very keen to be involved
5 in.
6
7 Some of State Water's justifications for their costs
8 to us just don't stack up, and we will deal with this a
9 little bit more detail when we talk about consumption
10 estimates, but certainly in some of their risk management
11 proposals we find it hard to see where State Water has
12 justified the level of premium that they want to charge for
13 costs.
14
15 One of our difficulties with this has been some of the
16 lack of information that is available, particularly with
17 publicly available information. State Water's annual
18 report is available now, I understand, but the accounts are
19 still not available, so maybe someone from State Water can
20 comment on that.
21
22 Turning to the consumption estimates and picking up on
23 the comments that you made, Michael, when questioning
24 State Water, we are strongly opposed to the proposal that
25 State Water has put forward. We think it is totally
26 unrealistic to use consumption of one standard deviation
27 below the average, bearing in mind that the long-term
28 average plan limit takes into account climatic fluctuation
29 over 100 years and, in the Lachlan's case, the use limit
30 that is required to keep the Lachlan at and under the plan
31 limit. We think to go down to one standard deviation below
32 that is an extreme over-reaction to the risk management.
33 I think it is a clear example of the lack of rigour in
34 State Water's justification of some of its costs.
35
36 In the Lachlan's particular case, one standard
37 deviation below is 200,000 megalitres delivered. Only
38 17 per cent of the years out of 100 are actually going to
39 be at 200,000 megalitres or less. We have had two in the
40 last 80 years, but we are currently in a record drought.
41
42 For the last eight years - in other words, since the
43 Murray darling basin CAP was implemented - the Lachlan's
44 average delivery has been 260,000 megalitres, including
45 two years where there has been zero general security
46 allocation where there has only been 18,000 megalitres
47 delivered in total for consumption one year and 39,000 the

1 year before. So even given that period, we are still
2 averaging 260,000 megalitres delivery, so I simply think
3 that to base it on 200,000 is a vast over-reaction to the
4 risk management.

5
6 The impact of that for customers, for example at the
7 usage rate of \$14.40 per meg, which would be the
8 unconstrained price, the difference between 200,000 and
9 300,000 megalitres is \$1.5m. So three years at \$1.5m,
10 that's \$4.5m, so State Water have already recovered a full
11 year's operating costs. It is just unmanageable. It is \$5
12 per megalitre cost to the irrigator. One of the most
13 important things in this determination for us is to have
14 realistic consumption estimates, and realistic risk
15 management in this issue. We do accept that extreme
16 drought is another situation and we have actually got a
17 comment on that later on in terms of cost shares. I don't
18 think that a situation such as the Lachlan has had over the
19 last two years where there has been absolutely no general
20 security water is something that can be managed by normal
21 risk management.

22
23 Within cost sharing, State Water acknowledged that
24 they have got a range of users. They have both paying and
25 non-paying customers and they acknowledge that those
26 non-paying customers, in other words, be required to
27 provide environmental flows, riparian users require
28 year-round operation. We are disappointed that, while
29 flagging that on one hand, State Water have made no effort
30 to actually allocate their costs to non-paying customers
31 and we question how State Water can possibly operate
32 efficiently when they are not recovering their costs from
33 the full range of those who actually drive the requirement
34 for service.

35
36 In the cost sharing, one of the issues that has become
37 particularly obvious in the Lachlan over the last two years
38 is the delivery of basic rights water; in other words,
39 stock and domestic people who don't have a licence. We are
40 actually suggesting there should be a new cost-sharing
41 principle applied to this. The vast majority of the water
42 that has flowed down the Lachlan in the last two years,
43 approximately 80 per cent of it, has actually been base
44 running of the river and for delivery of basic rights; it
45 has not been extracted water.

46
47 When there is a lot of water in the system, that is a

1 much lower proportion of overall costs and overall effort
2 for State Water. However, once you get into the situation
3 we are in now, in fact the vast majority of State Water's
4 efforts in delivery in the Lachlan have been to simply
5 provide for these requirements for people that - you know,
6 basic rights, don't pay anything for the water. It is a
7 right that they have by virtue of being riparian
8 landholders.

9
10 We suggest that a community service obligation should
11 be applied to the delivery of basic rights. This would
12 also address one of the risk management issues where in
13 extreme drought where the river is still operating but it
14 is delivering virtually no extractable water.

15
16 Turning to capex, again, we would like to defer our
17 comments on the actual level of capex until the
18 PB Associates report is available. We would like to talk
19 about the RAB versus the annuity, and we accept that it is
20 in everyone's interests that State Water are actually able
21 to fund reasonable capex and be viable. Our concern is
22 with the method of funding.

23
24 RAB may well be a good method of doing it. We don't
25 have enough information at this stage, but we certainly
26 don't think that the construction of RAB that State Water
27 has used is an appropriate one, particularly the starting
28 value and the rate of return that they are quoting.

29
30 Starting value. It has been a well-established
31 principle by IPART that pre-1997 assets are not included
32 for pricing purposes because they were constructed for
33 other purposes. The only way that State Water can generate
34 a desired income is by overturning those pricing principles
35 and by establishing the RAB at \$300m, rather than at \$75m,
36 which is the post-1997 asset investment.

37
38 Now, that penalises current customers for changes in
39 government policy. Corporatisation hasn't changed the
40 reason that investment was made in those assets.
41 Therefore, why should it change the pricing treatment of
42 those assets? This was well known at the time that
43 State Water was corporatised. We think that State Water
44 has been fairly cavalier in its willingness to simply drop
45 those pricing principles and move to their current proposal
46 for RAB.

1 The other issue, of course, is the rate of return and
2 the 7 per cent proposed. In other words, this is simply
3 moving to generating profit. It is exploiting the monopoly
4 position again, generating excess profit.
5
6 I think you asked a question earlier on, Michael, of
7 State Water in terms of the escalating level of income that
8 the RAB would bring to State Water, and certainly we have
9 recognised that. But it is not only funding capex that is
10 the issue, it is the providing of profit to the shareholder
11 ministers. RAB performs that function and we are concerned
12 that profit be taken out of the regional economy and the
13 justification for that profit.
14
15 Moving on to briefly comment on the high security
16 versus general security ratios, there is obviously a
17 differential there. We are not sure that the ratio
18 actually proposed by State Water is appropriate and
19 recommend it should be based on the share of extraction
20 which incorporates a share of the dam. We have included
21 that formula in our submission, but, basically, it would be
22 a ratio of about 2.4, rather than the 3.8 proposed by
23 State Water.
24
25 Turning to the DNR costs, we are extremely concerned
26 about the redefinition of water resource management costs
27 that DNR has proposed which results in this wholesale cost
28 shifting from about 65 per cent, which it was previously,
29 to something like 85 per cent now. IPART has spent a fair
30 bit of time in previous determinations assessing water
31 resource management inputs and determining what
32 proportion of activities that DNR undertakes are water
33 resource management related.
34
35 The information that DNR has provided, both in their
36 submission and today, really gives us no confidence that
37 there is a sound basis for this redefinition. To us, it is
38 cost shifting, moving DNR's core business to water users,
39 rather than apportioning the costs which should be borne by
40 the community as a whole.
41
42 Again, IPART's 2005 determination found that the
43 Lachlan was already at full cost recovery for DNR costs.
44 In their submission, they are proposing that the Lachlan
45 overall - regulated, unreg and groundwater - should pay
46 another \$1.4m to be full cost recovery now. There is no
47 justification for those costs and no justification for

1 that move.
2
3 DNR staff quoted several times the minimum standard in
4 terms of where they think that should underpin water
5 resource management costs and user shares, and in their
6 submission they made a statement about water users having a
7 primary duty of care to achieve environmental objectives of
8 the water sharing plan.
9
10 To us, that statement is simply nonsensical. The
11 environmental objectives in the Lachlan plan at least are
12 poorly defined, they are not time bound, they are not
13 quantified. Some of the environmental outcomes are related
14 to land management in the wider catchment, to riparian
15 management. Clearly it is unreasonable to expect that
16 water users can be held accountable for all those outcomes,
17 and it is symptomatic of DNR's approach towards a simply
18 wholesale shifting of costs to users. There is a lack of
19 substantiation for their claims, and we do not support any
20 move away from the previous definition of water resource
21 management costs.
22
23 Also with DNR, a number of the costs they are talking
24 about are related to remedying previous management
25 decisions, previous government policy. For example,
26 over-allocation in groundwater. Again, it is not
27 reasonable that water users should be required to manage
28 that cost.
29
30 One more thing on water resource management costs, and
31 I think Rick Rundle mentioned it: DNR have a wide range of
32 stakeholders, a wide range of users of their services, but
33 one user is bearing 85 per cent of the costs. A number of
34 the functions that they talked about - information
35 provision, resource management generally - are part of
36 government core business and not costs that are incidental
37 based on water use alone.
38
39 In closing, we would like to ask for a longer-term
40 price path than three years. Over the last two years,
41 organisations such as ours have had high costs and been
42 responding to two sets of submissions, one of which was
43 very poorly substantiated, very poor standard of
44 information. This is a high demand on our organisation.
45 We would be in favour of a longer term price path.
46
47 THE CHAIRMAN: Thanks very much. I will just let you know

1 that we are envisaging a four-year price path. Are there
2 any quick questions?

3
4 MR SEERY: I have a couple of quick questions; hopefully
5 you will have quick answers. The first relates to the high
6 security premium. You are suggesting a ratio of
7 approximately 2.4 in your submission and that you have
8 based that on the calculation of entitlements and average
9 availabilities, which seems to suggest to me that the
10 premium for Lachlan may be different to that in other
11 valleys. Is that what you propose?

12
13 MS EWING: Yes.

14
15 MR SEERY: Do you think that's the appropriate way to go,
16 that across New South Wales there is a different high to
17 general security premium that differs across valleys?

18
19 MS EWING: I imagine it's related to the circumstances of
20 the individual valley, what is the relative availability of
21 high security versus general security water in each valley,
22 but that in turn reflects the percentage of the dam that is
23 available. Personally I wouldn't see a problem with having
24 a different ratio in different valleys.

25
26 MR SEERY: I think we would be interested in hearing the
27 view of State Water on that later this afternoon.
28 Following on from that, the Department of Natural Resources
29 is proposing to remove the high security premium for water
30 resource management costs. I don't recall seeing your view
31 on that. Do you have a particular view on that issue?

32
33 MS EWING: No. We actually concur, that we don't see that
34 there is a large difference in management input to high
35 security water versus general security water from the point
36 of view of water resource management.

37
38 MR SEERY: The final question: I understand that there's
39 been no allocations in the Lachlan valley in the last two
40 years and that the government waived the fixed charge. I'm
41 not sure what the situation is with allocations for the
42 current year, but do you know whether the government is
43 proposing to continue to waive the fixed charge?

44
45 MS EWING: No, I don't. It's a very interesting question.
46 We would obviously like the support of IPART on that. Both
47 the 2003 and 2004 charges, we have put a proposal to them

1 for 2004-2005 which they are considering, and that's as
2 much as we know.

3
4 MR REID: Can I ask two very quick questions? The first
5 is to ask you to expand on your position so far as State
6 Water is concerned about the usage charge as opposed to the
7 fixed charge, and on the proposal by the Department of
8 Natural Resources to move solely to a fixed charge. My
9 second question is; what proportion of on-farm costs would
10 relate to water charges?

11
12 MS EWING: Dealing with the first question, we have a
13 range of views within the valley on the fixed versus
14 variable split. We didn't put a position in our submission
15 simply because we don't have a strong view one way or the
16 other on that. To us that's not the critical issue. The
17 critical issue is: what are the efficient levels of costs?
18 That's the same with the position with water resource
19 services costs. In terms of on-farm costs, water costs -
20 it's difficult because costs of different inputs vary from
21 year to year, but we might be talking about 3 to 7
22 per cent, something like that. The concern for us is that
23 any increase in water costs doesn't provide any additional
24 services, any ability for the operator to earn more from
25 that water, so an increase in water charges comes directly
26 off profit.

27
28 MR REID: Thanks very much.

29
30 THE CHAIRMAN: Thank you very much, Mary.

1 MACQUARIE RIVER FOOD AND FIBRE

2
3 THE CHAIRMAN: I would now like to ask the representatives
4 of Macquarie River Food and Fibre to come forward. As
5 there a few of you, it would help if you could introduce
6 who is presenting to the others. To help you stay within
7 the 15 minutes allotted time, I'll give a warning when you
8 have three minutes to go.

9
10 MS WARD: Thanks, Michael. What I do propose to do is
11 that we will actually make up time for you, but we'd like
12 to spread across the hour. We have our three different
13 groups presenting, but we actually have all our issues in
14 common. We have tried to make it that way so it's
15 interesting for IPART.

16
17 THE CHAIRMAN: So the three groups here until lunchtime
18 will cover that?

19
20 MS WARD: Yes, including Lower Macquarie groundwater and
21 Tenandra. I'm Michelle Ward and I have a team of not
22 technical experts perhaps, but volunteers and people who
23 know a lot about irrigation at least.

24
25 I'd like to dwell on that point for a second because
26 the IPART process is quite laborious and resource-hungry
27 from the point of view of customers as well as government,
28 because we are not forking out large amounts for
29 consultancies, even though I am a paid consultant on this
30 process. I also wanted to make the comment that I can
31 remember thinking that it would be an ideal world if we had
32 separate submissions from DNR and State Water, but that
33 world has not got any easier with separation because now we
34 have a new set of issues, double the work, and actually no
35 increased clarity from the DNR on costing. Consequently we
36 focus on State Water's submission because there's more to
37 argue about, but it doesn't sidetrack us from the
38 frustrations we still have from the water resource
39 management side of things.

40
41 In the preparation of our submission I would like to
42 acknowledge that we appreciated the open-door policy that
43 State Water offered. We had to and fro and had questions
44 responded to while we were writing our submission.

45
46 Unfortunately, the DNR approach was a bit more
47 removed. We got a head office formal response after our

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1 submission was completed, so that's always something that
2 could be improved upon.

3
4 Also, the value that we see from today is actual
5 discussion in hearing IPART's current thinking on some of
6 our key issues which are cost sharing, less than average
7 use, and rate of returns. So we would appreciate getting
8 into some discussions about that, so that's why we'll keep
9 things brief.

10
11 We will hear from Michael Egan and Glen Whittaker on
12 some of the issues. Obviously we have 10 minutes versus
13 the two hours of the two earlier presentations. Our key
14 messages are that prices would be reasonable if
15 cost-sharing ratios reflected the other beneficiaries and
16 the CSOs. Somewhere along the line we have got way out of
17 kilter with the impactor pays principle, in our view. We
18 think it needs an update so that it is more sustainable and
19 appropriate in terms of State Water identifying a wider
20 customer base.

21
22 Secondly, sorry State Water, but you really need to
23 scrap this less than average use. It has a big impact in
24 the Macquarie and there are far more cost efficient ways of
25 managing risk. Also, irrigators bear their own risk. We
26 have the same variability of access to this water supply
27 which drives businesses.

28
29 Thirdly, scrapping the rate of return, and we have
30 speakers who will get into that. What's not on the
31 overhead is to do with Department of Natural Resources
32 thinking and also IPART's previous rulings. We are looking
33 for a shift in the paradigm in thinking that water resource
34 management is actually attributable to water users at all.
35 Sure there are some elements, but we would actually
36 completely reverse the 85/15. I support Mary Ewing's
37 comments earlier, so we'll get more into that.

38
39 Talking about the principles, we have always talked
40 about users or beneficiaries of State Water. As Mary said,
41 it has acknowledged its non-paying customers. There's a
42 new playing field. With the national water initiative the
43 environment now has rights, and basic rights are a
44 community expectation, so there are customers and costs
45 need to be recovered. Given the impact of case theory, I
46 don't think we ever looked completely into - and IPART
47 didn't either - the assumption that irrigation is a net

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1 impactor, that all of these costs, water resource
2 management, et cetera, are being attributed to extractive
3 users.
4
5 Irrigation is a positive net impactor on the
6 community. Some of these communities would not be here
7 without irrigation. Grasping the full social consequences
8 of impactor pays has never been done. I made the point
9 about community expectations.
10
11 Water sharing plans - on the one hand they were
12 required for reviewing environmental needs, actually
13 providing the environment with rights, and on the other
14 hand we're being told that they are for our benefit and
15 improving our security, so I didn't think those two things
16 run together.
17
18 Basically we think all users should pay their share,
19 either direct or via a CSO. Stock and domestic and town
20 water supply as users - Mary touched on the issues and they
21 are pertinent with the Lachlan. There are massive
22 operating costs in both our valleys to deliver the
23 replenishment of stock and domestic flows in low flow
24 periods. There is no benefit to irrigation from these
25 deliveries. Actually, if you want to talk about irrigation
26 as an impactor, these flows and basic rights were not able
27 to be delivered to stock or domestic or riparians without
28 the infrastructure and the regulation of the rivers.
29
30 I mentioned in our submission the operating licence
31 requirements. Again the point is made that onerous costs
32 are put on State Water by government in terms of membership
33 and what drives State Water's delivery. I just don't think
34 there's justification that all of these are borne by
35 irrigators.
36
37 On the subject of community service obligations, I have
38 a quote a bit further on where the former IPART report refers
39 to the government identifying community service
40 obligations. Why aren't there any identified? It's a
41 conflict in the process. I suppose we are putting it to
42 IPART because we do think it's part of IPART's role.
43
44 That bottom dot point is that we've been writing the
45 same thing about cost sharing principles for several
46 submissions. I was thinking: what can we possibly say to
47 open IPART to shifting a paradigm, but there are many

1 different ways of calculating what the extractive user
2 share should be in the Macquarie.
3
4 I am just going to ask Glen Whittaker to come up and
5 talk briefly about environmental water as a customer in the
6 Macquarie.
7
8 MR WHITTAKER: My name is Glen Whittaker. I'm a pretty
9 simple irrigation farmer on the Macquarie. I guess my view
10 is that I accept full cost recovery and I accept paying for
11 my share of the resource. Obviously my key concern is the
12 costs being incurred by me compared to my access to the
13 resource.
14
15 Just to give you some examples, I guess the Macquarie
16 system is a complex system when you get down to the bottom
17 end near the Macquarie Marshes, but to give you some
18 numbers, the regulated section of the river and creek cover
19 some 400 kilometres. The section of creek and rivers that
20 stock and domestic and environmental water has to be
21 delivered to covers some 1,000 kilometres, so the ratio is
22 amazing. For these creeks and lower sections of the rivers
23 that replenishment flows and stock and domestic flows have
24 to be distributed to, it's low flows that have to be
25 monitored exactly. They have structures and there's quite
26 a big cost in managing those.
27
28 I see it as a huge burden to place all that cost on
29 the irrigation industry when a huge expanse of the river
30 system from the point of view of delivering stock and
31 domestic and environmental water is placed on the
32 irrigators.
33
34 Just to give you an idea, the environmental water
35 under the water sharing plan is that the marshes get some
36 390,000 megalitres a year, of which 160,000 megalitres is
37 general security water equivalent to a general security
38 irrigation licence, so that's managed in the dam and
39 delivered from the dam as required by the environmental
40 flows reference group. So that 160,000 megalitres is
41 exactly equivalent to a general security irrigation
42 licence, but also the rest of the environmental water is
43 managed as such. It's not tributary flows or surplus flows
44 or irrigation cancellations that are just let flow down the
45 river. That water is targeted to specific areas. It's
46 managed to go down a different river or creek to an
47 environmental area in the marshes. So whether it's a small

1 flow of a cancellation or a tributary flow, there's still a
2 cost of managing that water to get it to the environmental
3 area that has been targeted by the environmental flows
4 reference group.

5
6 A final point on that environmental water, you also
7 have that 390,000 megalitres and 160,000 of general
8 security, but the environmental movement and government
9 agencies are in the process of purchasing more water from
10 general security irrigation licence holders to move to the
11 environment. It will be a move that will be interesting to
12 watch as to how State Water recovers the cost of that
13 general security water when it gets transferred to
14 environmental water.

15
16 The last point I'd like to make is that in general
17 terms - I will not give you exact figures - the
18 environment, being mainly the marshes, gets some 390,000
19 megalitres a year. The essential requirements for the
20 river system as a whole need to have some 340,000
21 megalitres stored in the dam, and the flood mitigation
22 protects some 400,000 megalitres, so there's air space in
23 the dam that's protected for flood mitigation, which is one
24 of the key components of why the dam was built. It was for
25 flood mitigation for Wellington and Dubbo. So it is a key
26 component that is obviously a difficult one to account for,
27 but there's some 400,000 megalitres of flood mitigation in
28 the dam.

29
30 Of the total system, irrigation is some 25, 26
31 per cent of the water. Just a couple of other quick
32 things: in the development of the water sharing plan, which
33 is what we are under now, the irrigation industry had two
34 representatives developing that plan in a committee of 16.
35 Obviously we are a part of the management of the river, but
36 we're not the key player by any means when it comes to
37 writing the rules or regulation. Also, the State Water
38 customer service committee, there's environmental people on
39 that, there are representatives from effluent creeks, and
40 stock and domestic users, so they have a big say in how
41 State Water operates in that part of it, so it's a burden
42 for the irrigators with all the costs.

43
44 I just get confused with some of the wording with how
45 we are treated, whether we're a user, a stakeholder, a
46 customer, or a beneficiary, because it seems to be a fairly
47 grey area, who receives and who pays. Thank you.

1
2 MS WARD: Thanks Glen. Just touching again on that flood
3 mitigation role and the stock and domestic role, we were
4 talking earlier about impactor pays and I don't know if I'm
5 right in assuming that some of that comes from assuming
6 that river regulation happened for the purpose of
7 irrigation.

8
9 This is the plaque at Burrendong which actually
10 specifies irrigation, stock and domestic, and flood
11 mitigation. I don't know how much more simple we can get
12 in trying to prove to you that all of the costs associated
13 with running these structures and the consequent regulation
14 impacts cannot be attributed to irrigation as an impactor.
15 One third of Burrendong is for flood mitigation. If
16 Burrendong fails, a DLWC 2001 study estimated that the
17 agricultural component of the total cost is 3 per cent.
18 Now I know that there's a significant government share in
19 funding the capital cost of flood mitigation, but what
20 about the opex? Also, whenever there's a user share, it's
21 a hundred per cent extractive users at the moment. We'd
22 like that divided across the other beneficiaries or users.

23
24 The spillways gates and associated mitigation projects
25 are massive expenses and also, from a flood mitigation
26 point of view, water users actually don't gain benefit from
27 the dam in terms of flood mitigation. They've all built
28 their own structures.

29
30 Opex and capex: as you can see, it's difficult to
31 comment and again we haven't employed consultants to
32 analyse anything for us, so it's this issue of a level
33 playing field in terms of being able to engage meaningfully
34 in the IPART process. But, as Mary said, for the Lachlan
35 we had already reached full cost recovery, and we
36 understand State Water's logic that there are new costs
37 with corporatising, but when you're looking at a monopoly
38 pricer, where is the increased service? Basically our key
39 message is: water prices in the Macquarie would be okay if
40 the cost share reflected all the users.

41
42 Timing of pricing path: Mary also touched on this.
43 They should be longer for a number of reasons. DNR and
44 State Water requirements to meet reporting standards - both
45 to us and to IPART in this submission process, I've talked
46 about our frustration in being able to really interrogate
47 the DNR reports. We're still no better off in knowing what

1 our valley prices are for the next determination being
2 proposed because there's no simple table that you go to
3 where you add State Water and DNR for your valley. That
4 information is still not forthcoming. Also, there's going
5 to be more stability for all parties. We acknowledge that
6 the agencies have massive expenses in trying to meet these
7 submission deadlines as well.
8
9 I touched before on the cost to customers of the
10 process, the technical and specialisation required and the
11 cumulative financial and social impacts of constantly
12 fighting against the avalanche. I think somewhere a few
13 years ago we got off the boat, and now we're fighting
14 against things. The impactor pays is getting way out of
15 kilter, rather than having all users acknowledged.
16
17 Affordability and the impacts of price increases: we
18 would far prefer to focus on getting fair prices and
19 knowing actually what information we are looking at and
20 understanding whether it is efficient, rather than
21 affordability. Let us, as the irrigators, work out how to
22 afford the cost. We accept full cost recovery. We do
23 note, however, that there are significant regional economy
24 flow-ons when you add something like a rate of return on
25 investment or a risk premium. That money going out of
26 small towns never comes back. Just even a tiny increase in
27 allocation recently has seen small local towns in the
28 Macquarie really starting to tick again.
29
30 Also, in terms of affordability, there's a linkage to
31 our argument for a longer pricing period with a more gentle
32 glide path, especially with these massive increases being
33 talked about, and there's that issue of costs and skills
34 associated with meeting the submission process.
35
36 On to DNR issues: again I have talked about our
37 frustrations with the detail of the submission and us not
38 being able to see where it puts us as a valley with prices.
39 We are not really sure about the service agreements. I
40 understand that they are not in place. That makes me
41 nervous representing customers and talking about service
42 delivery from DNR, when there's no accountability and the
43 agreements aren't yet in place.
44
45 With respect to DNR's proposed change to the water
46 resource management definition, okay, I understand that the
47 issue is that Treasury hasn't provided an adequate budget

1 to DNR, but that does not give a legitimate reason for
2 twisting cost sharing principles and redefining what your
3 products are to try to put a spin on them that they are
4 providing benefit to irrigators. I would actually
5 challenge that water resource management is of benefit to
6 irrigators. Sure, there are some benefits, but to
7 attribute all the minimum standards, as Mary said, and the
8 water sharing plans to irrigators being a large
9 beneficiary, I don't think it stacks up. Also, there was
10 no cost/benefit analysis done on the water sharing plans.
11 They're based on community expectations which led to
12 government legislation and policy, and to try and tie that
13 in with some kind of fee for service that has any
14 accountability around it is pretty difficult.
15
16 Another concern we have raised is with regard to
17 minimum standards of reporting. I understand State Water
18 is still reliant on DNR's financial reporting system. We
19 really need valley-based pricing. I notice in DNR's
20 submission they're trying to have a shift away from their
21 product coding, away from outputs. To me, from a business
22 point of view it's very concerning if you are shifting away
23 from an output-based pricing. It takes the rigour out of
24 the service delivery for a fee. I have already talked
25 about this shift. IPART has already previously determined
26 that 65 per cent of WMR costs be recovered from users. We
27 strongly oppose that. Obviously the 85 per cent is getting
28 way out of kilter.
29
30 In terms of us receiving benefit or service or
31 increased security from DNR, we just make the comment that
32 the only outcome we seem to receive is a decrease in our
33 reliability and an erosion of rights. Fair enough, the
34 water sharing plans are in place, but there are enough
35 loopholes to remove entitlement every 10 years.
36 Unconstrained pricing: we really can't see how this can be
37 an efficient approach because it demonstrates the lack of
38 accuracy with costing of data at the moment.
39
40 Externalities and demand management: I want to really
41 emphasise for IPART that there's no place for this in bulk
42 water pricing. It's the permanent price, not the annual
43 usage and entitlement fee that will really drive
44 efficiencies. The more valuable water gets, this does
45 increase efficiency, but you're not to decrease your use of
46 something that you have paid thousand of dollars a
47 megalitre for the entitlement for. Also remember the

1 variability of annual supply with bulk water. There's a
2 conflict of demand management with the way State Water is
3 set up in terms of its business drivers.

4
5 This comment about future water for the environment,
6 State Water touched on it in its submission. What if more
7 water goes to the environment? It's very likely to happen,
8 given the \$100m government funding announcement for
9 environmental water. I really think that there needs to be
10 some forethought about this. You can't seek to continue
11 recovering costs from a shrinking customer base. That's
12 another reason why the cost sharing principles need to be
13 reviewed to include some extractive customers.

14
15 I will hand over now to Michael Egan who will talk
16 about less than average use, then we might have a short
17 break for questions because this is the end of this section
18 before we go on to other groups.

19
20 MR EGAN: My name is Michael Egan and I am on the
21 customer service committee that represents irrigators on the
22 Lower Macquarie below Warren. I am going to talk to you
23 about risk premiums.

24
25 The State Water proposal is one standard deviation
26 below average use, and the implications for the Macquarie
27 are particularly severe as it is really asking a
28 53 per cent risk premium, as the table on 10.4 on
29 State Water's submission demonstrates. Basically, our
30 average use is 386,000 megs a year and they have reduced
31 that to 208,000 megs, giving us a 53 per cent premium,
32 which actually relates to an average of a 33 per cent
33 allocation, and if you look back on what we have extracted
34 our average allocation is around 61 per cent, so it is just
35 about half.

36
37 It is not really a cost-effective means of managing
38 risk. As we see it, it is just far too conservative. It
39 is a bit like fudging marbles in the school yard. The
40 reliability in each valley hasn't been factored in, and I
41 think that is why it has made it particularly difficult for
42 the Macquarie. When you compare it to some of the other
43 valleys in that table you see that the Murray and the
44 Murrumbidgee hardly get affected at all, yet they are
45 67 per cent of State Water's market.

46
47 Customers have an identical risk in terms of

1 variability of water supply, so we are suggesting that
2 State Water should manage their own risk in a legitimate
3 way because they have got a large geographical spread
4 across the state, so it is a natural insurance policy on
5 its own. It is not every valley will be in drought at a
6 similar time. At the moment we are probably in one of the
7 100-year positions where we are mostly in drought, or just
8 coming out of drought, but it is a national insurance
9 policy just having that geographical spread, and that is
10 part of being in the real world of business.

11
12 This proposal put forward really distorts prices.
13 From valley to valley it is showing how some of the
14 increases are just way out of kilter, and the Macquarie is
15 one. As I say, it has been hit particularly hard.

16
17 So we are proposing that the potential for a
18 cost-efficient risk management option is basically, one,
19 its commercial insurance, and that is probably only
20 5 per cent of the years or even less. If they were really
21 serious or worried about their risk factor, there are
22 plenty of things on the market. I know that the
23 electricity industry has some quite creative policies as
24 far as insurance against weather and pricing structures
25 with caps and collars, et cetera, et cetera, so there is a
26 potential out there for them to reduce their risks in the
27 commercial area.

28
29 I think the main way that they should be considering
30 is debt funding any shortfalls and in years where they have
31 a reduced water year and they are not covering their costs,
32 full cost recovery, they borrow the money at, say,
33 6 per cent and then when they get higher years where they
34 have got surplus funds, they can deposit that money back on
35 deposit for 4 per cent, so it actually ends up only being,
36 say, 1 or 2 per cent as a risk premium. So from our point
37 of view, we can see that as a far more cost-effective way
38 of managing risk than a 53 per cent risk on water.

39
40 The last thing that we, as irrigators, would like is
41 being hit with large water bills in low water years. We
42 manage that risk as best as we can through other means, and
43 I consider that State Water should do the same.

44
45 We also have a concern that a state-wide application
46 of less than average use may lead to cross-subsidisation
47 and move away from cost reflectivity. It is something that

1 could happen. It is a little bit vague in that respect,
2 but it is something that is of a concern to us.
3
4 In State Water's operating licence they have got a
5 40 per cent/60 per cent fixed to variable price structure,
6 which we totally agree with. The less than average use
7 approach seeks to meet the ratio by inflating variable
8 prices, trying to squeeze as much out of the premium from
9 the variable portions.
10
11 Yesterday we made up a little table to see what effect
12 it has on our pricing structure on three different
13 scenarios. The first three lines is basically 30, 60 and
14 100 per cent allocations as they are at the moment on 04/05
15 pricing structures, and we have the fixed costs - this is
16 all pricing on a 100 megalitre allocation.
17
18 So the first three years is our pricing structure as
19 it is at the moment. Then the bottom half of the graph
20 there is the 30, 60 and 100 per cent allocation as it would
21 be in 08/09. As you can see from the graph there, the
22 ratios that are being asked to be achieved from the
23 operating licence have been pushed beyond what they are
24 supposed to be basically to retrieve more income in those
25 higher and lower water years. They are basically saying
26 that 30 per cent allocation is about average - that's 37 to
27 63. So that's somewhere around the 60/40 requirement.
28
29 It is interesting to note that there is a 54 per cent
30 increase in the cost from '04 on a 30 per cent allocation,
31 which reconciles with our risk premium that they are asking
32 for us to take on board. So what we are really asking is
33 that State Water should be managing their own risk through
34 debt funding.
35
36 The normal business notion of increased price is based
37 on increased customer service, so I ask the question, well,
38 what do we get for our 53 per cent premium? Do we get
39 extra security? No, we don't. Do we get more service?
40 No, we don't. So where is the benefit and where is the
41 consultation to get any benefit or any better service,
42 et cetera.
43
44 From what I can see, there is no evidence of
45 State Water having any understanding of its market.
46 In other words, have they been doing any sensitivity
47 analysis in pricing? In any business, we really need to

1 find out what our market is, what depth it has, et cetera,
2 et cetera. State Water's market is a mature market. There
3 is no growth so they have to make their money out of what
4 they have got. So there is no more increasing allocations,
5 no more dams to build, et cetera, et cetera.
6
7 I think it is very important that State Water
8 understands under what circumstances do we as irrigators
9 use all our water, use no water, and under what
10 circumstances will we sell our water and when would we stop
11 irrigating. In reality, the price of water has a major
12 effect on irrigator usage patterns.
13
14 Government and IPART have set a lot of parameters,
15 like cost recovery, percentage, return on assets, return on
16 investment and they have the operating licence conditions
17 to deal with, but my question is is it really achievable in
18 a market economy today?
19
20 To lead on from there, I checked with a Boyce comparative
21 analysis - the last one out is 2004. They do a lot of
22 cotton industry work and they have a web site of their
23 own as well as the CRDC - Cotton Research Development
24 Corporation - who have their site. Basically, they have a
25 benchmarking of all the cotton growers in the state, and
26 I ask where is the break-even point for customers?
27
28 Basically, for the last three years cotton growers
29 have been making money, and that is where most of the water
30 has been used in recent years because it is the most
31 effective way of making money, basically. For the average
32 grower of 500 hectares he has made a loss in the 2004
33 season of \$263 a hectare and a break-even point of 9.11
34 bales a hectare. Seventy-five per cent of the country they
35 put in was grown on fallow and new country, so they have
36 used as much of the moisture from rain in the preceding
37 10 to 12 months as they could in trying to get their water
38 use efficiencies up as well as they can.
39
40 I just wanted to put those numbers past you to make
41 State Water think, righto, where is the market, how far can
42 we go with prices and develop their cost structure
43 accordingly. So my take-home message, basically, as far as
44 risk premium is concerned, is State Water should manage
45 their own risk. Thank you.
46
47 MS WARD: Thanks, Michael. We will just see if you have

1 any questions at this point before we go on to the Lower
2 Macquarie groundwater irrigators.
3
4 THE CHAIRMAN: Thank you for that. I perhaps should let
5 you know that, on my reckoning, you have used 40 minutes of
6 your hour. That is my reckoning.
7

8 Also, in your opening remarks you indicated you would
9 like the tribunal to answer a number of questions. An
10 essential part of our process is to collect information
11 before we come to work out the answers, and so the
12 opportunity to find out the tribunal's views really comes
13 through its draft report. That is why we have a draft
14 report, so that people can have a chance to respond to that
15 and if they disagree, they can argue the point on the draft
16 report.
17

18 Nevertheless, I will make a comment in terms of what
19 guides our thinking on a couple of points that you have
20 raised. One was this general issue of impactor pays.
21 There can be debate about how it is applied, but the
22 principle, as I understand it, is that where the irrigator
23 is seen to cause the damage by virtue of irrigating it,
24 then the irrigator, if you like, pays to fix the damage.
25 I think you made your point very well with flood
26 mitigation, which is not caused by irrigation. So I think
27 that point was extremely well made.
28

29 The other issue I just wanted to touch on was
30 the length of the price path. In judging the length of the
31 price path, it really comes down to the amount of certainty
32 that we can have that we have got it broadly right. The
33 further out you go, the less certainty there is, as with
34 any forecast.
35

36 The reason, for example, why we made a one-year
37 determination for the current financial year, which was
38 never our first preference, was because of our lack of
39 confidence in the body of information that we had at that
40 time. That is the background, if you like, to how the
41 length of the price path is determined.
42

43 The longer the path, the longer the glide path, and
44 the longer the glide path, the longer time you take to
45 phase in any change, and that can be an advantage. Against
46 that is, if you like, the increased uncertainty as you go
47 further out in terms of costs, et cetera.

1
2 MR SEERY: My question is a fairly simple one, and it is
3 similar to the question I asked Mary earlier: what is your
4 view on DNR's proposal to remove the high security premium
5 for water resource management costs?
6

7 MS WARD: I think MRFF didn't make substantial comment in
8 our submission on that issue and, if you like, I will take
9 it on notice. As far as I'm aware, we didn't have a strong
10 position. The same as the Lachlan, our focus is on getting
11 costs to be reflective and fair, rather than the
12 difference.
13

14 MR REID: Michelle, in your submission you hinted, if that
15 is the right word, at possible double dipping between
16 State Water and DNR. I refer here to the groundwater
17 monitoring network. Would you like to expand on that a
18 little bit?
19

20 MS WARD: Yes, Colin, the concern was with DNR presumably
21 providing a service which was information which customers
22 were going to be directly charged for, and then there was a
23 question about the responsibility for actually making the
24 initial investment in the capital that's required to
25 collect that information, and I understand that that's been
26 clarified from DNR that that is a government
27 responsibility, but then all of the operating and
28 maintenance of that equipment is to be passed on to
29 customers. So if you are a normal consultant and you are
30 charging for some information that you are providing, to
31 also recoup capital costs for operating and maintenance I
32 wouldn't have thought it was appropriate, but, again, it is
33 just so hazy for us to be able to delve into in terms of
34 the detail.
35

36 So it was a question we were hoping to clarify, and
37 I understand that the capital is being covered by
38 government, which is one plus for customers, if that's the
39 case, but there's also the ongoing operating and
40 maintenance.
41

42 MR REID: While we are still to deliver to you, obviously, our
43 consultant's report on operating capital expenditure, I'm just
44 wondering whether you have any examples, yourself, of where
45 you believe State Water and DNR could provide their services
46 more efficiently? I know in your submission you mentioned
47 the implementation of monitoring requirements

1 and the imposition that is imposing upon irrigators.
2
3 MS WARD: Well, there is a great example coming up in the
4 Lower Macquarie groundwater irrigators' presentation in
5 terms of perhaps more efficient ways of providing services,
6 and with respect to the river I will take that on notice
7 and see if one of the customer service committee
8 representatives wants to comment. Does anyone want to
9 comment at the moment?
10
11 MR WHITTAKER: We are involved with the customer service
12 committee and have been working on improving efficiency.
13 There is twice annual stock and domestic replenishment
14 flows, and one of the things we have been pursuing is
15 rather than just delivering them, and the difficulty of
16 managing them or monitoring how they get to the end of a
17 system, how we can deliver that water a lot better with
18 less water and still achieve our end goal. So we are
19 working with them to try and achieve those things, but
20 there is a lot of opportunity to improve those systems in
21 particular.
22
23 MR REID: Thanks very much.
24
25 THE CHAIRMAN: I would ask you to continue, then,
26 Michelle.
27
28 MS WARD: I will call on Peter Gainsford now from the
29 Lower Macquarie Groundwater Irrigators Association.
30
31 MR GAINSFORD: I'm an irrigator west of Narromine.
32 Development of groundwater irrigation took off in mid-1995.
33
34 Basically, a bit of history to start off with. In
35 September 1995 when groundwater was just starting off, as
36 there was a lack of water in Burrendong, the proposed
37 irrigators were just developing their boards. We had a
38 meeting with DNR in Narromine where we had a hydrologist
39 Gabriel Salas explain sustainable yield and how it was
40 calculated. At that stage it was 80,000 megalitres.
41
42 He showed us the methodology and how he obtained these
43 figures of this 80,000. He was actually picked up by one
44 of our own irrigators on this, and he actually there and
45 then revised his figures back to 65,000 megalitres.
46
47 Going around the table after this meeting the

1 consensus was that everyone sets sustainable management, no
2 over-extraction, don't want a repeat of the Namoi Valley.
3 DNR said, "Trust us. We won't allow that to happen."
4
5 Within 12 months, August '96, irrigators were
6 concerned about the allocations that were being handed out.
7 We rang DNR. No response from them. But one week later
8 they announced a moratorium. They had reached an
9 allocation of a 120,000 megalitre base allocation plus
10 30,000 in conjunctive. Whether it is 65,000 megalitres
11 sustainable yield or 80,000, it is still way above that.
12
13 DNR's policy of February '98 was still talking about
14 sustainable yield of 80,000 when in September '95 Salas,
15 the hydrologist for DNR, told irrigators it was 65,000, and
16 10 years on this is still the sustainable yield figure
17 being shown today.
18
19 Licence cuts. Today they are looking at licences out
20 there of 137,000. Now, this has been cut from 150,000
21 because conjunctive licences have been cut back, have been
22 cut out to base, so there's 137,000. This has to be cut
23 back to 65,000, according to the water sharing plan, by
24 2009/10. This, in itself, is causing a lot of frustration
25 and problems for irrigators as we have to still go on with
26 meetings and things like that, consultations, and then we
27 have the retractions of promises of governments in
28 compensation, how they are going to go about doing things.
29
30 With the costings in 2006/07, DNR are wanting \$1.37m
31 from the Lower Macquarie groundwater irrigators. That
32 quickly works out at \$10 a megalitre. You don't have to be
33 Einstein to work that one out. Then in 2009/10, when it's
34 reduced to 65,000, they want \$1.45m from groundwater
35 irrigators - that's \$22 a megalitre. This means a
36 megalitre of water onto a crop on an irrigation farm is
37 going to cost well in excess of \$100 a megalitre. By the
38 time you take in the pumping costs, like diesel pumped and
39 things like that - even if we converted to electricity -
40 there is no savings. It has been mentioned earlier that
41 the price of commodities is making it very hard as it is to
42 substantiate these costs.
43
44 DNR didn't even follow their own policy at the time
45 when issuing these allocations. They issued irrigation
46 allocations out in sandstone aquifers, which is against
47 their own policy. Now, this actually impacted on stock and

1 domestic water users in these areas. DNR's answer to that
2 was to cut back all allocations. That doesn't stop
3 extraction rates or wasn't going to help the problem
4 whatsoever.
5
6 The irrigators and the stock and domestic users got
7 together and worked out an interference program where it
8 was kept to a minimum. So if it was drawn down and stock
9 and domestic users were being harmed, then irrigators
10 stopped pumping until the water levels were replenished.
11 So that was just showing that the irrigators themselves and
12 the people in the community were able to manage a problem a
13 lot better than what DNR was able to do.
14
15 Sustainable use. Under the water sharing plan, like
16 they said, there was water loggers and probes and things
17 like this. DNR already has automatic loggers and
18 observation bores out there. Irrigators have records of
19 water levels from their own bores, and also what drawdown
20 levels are occurring and when.
21
22 Salinity probes would be for the benefit of the whole
23 community, not just the irrigators. When we first started
24 putting bores in this area out there the big push was from
25 DNR to put bores in because of the rising watertable out
26 there, so that irrigators would help pump that and relieve
27 the rising watertable problem. This then turned out to be
28 completely wrong as pumping from where irrigation water is
29 pumped has nothing to do with the rising watertable.
30
31 Monitoring costs. In my situation the costs are going
32 to go up to 3,000 megalitres, so it is going to cost me
33 \$30,000 a year in fees. For \$3,000, irrigators could put
34 meters on bores to measure how much is being pumped and
35 when, and this could be downloaded to computers by
36 telemetry technology. The drawdown levels could also be
37 measured from irrigators' bores. Also, they could be
38 measured from their own observation bores. They still have
39 people, drivers, driving out there and measuring. To me,
40 DNR's technology is that inefficient and way out of date
41 that they are not helping their own situation and they
42 don't show us the competence that they are going to be able
43 to do this, or manage the whole problem properly anyhow.
44
45 So why are they asking us to give them more money for
46 loggers, probes and staff and vehicles. They haven't told
47 us how many loggers or staff or what vehicles or anything.

1 They have just plucked a figure out. Their costs at the
2 moment don't show us what they represent. We don't know
3 what they are actually spending their money on at the
4 moment.
5
6 As the late Kerry Packer has said, "You're not doing
7 such a good job of spending it, so why should we give you
8 any more!"
9
10 The cost sharing principles mean irrigators should not
11 pay for expenses that are not of benefit to the
12 environment/community. Shallow aquifer monitoring/stock
13 and domestic, etc, are not water user's responsibility.
14 Michelle will touch on that more.
15
16 It has been hard for us to comment on the costs that
17 they are installing on us because there has been no
18 breakdown of what they are going to do and where they are
19 going. I have found, talking to ex-staff of State Water
20 and DNR, that they leave the departments and go out and set
21 up businesses that provide irrigators with a lot better
22 service. So some of their staff are up to date once they
23 have left the department with the knowledge of knowing
24 what irrigators want.
25
26 As the chairman stated earlier, if you cause the
27 problem, then you pay. To my way of thinking, DNR caused
28 the problem with the lower Macquarie irrigators by
29 overallocating. They had the figures of sustainable yield.
30 Basically they just didn't have the competence in office
31 management of calculating how much had been allocated out.
32
33 The water sharing plan is not an irrigators' push.
34 We're not getting any benefit out of that. All we're
35 getting is pain of restructuring of the licences and
36 cutbacks, and increases in costs. The current cost is
37 roughly \$2 a megalitre. To me, this is the appropriate
38 cost for what they have done and what they do. I can't see
39 how they can justify any increase. For the \$22 a megalitre
40 in 2009/2010, in my situation that will amount to a bill of
41 around \$60,000 a year. That's more than I have out at the
42 moment on lease payments on machinery. It's also greater
43 than my interest bill on loans. That will be an inhibiting
44 factor in how I run my operation.
45
46 With the increased costs per megalitre, irrigators are
47 going to use every megalitre of water to generate income

1 because they have to in order to meet these costs; whereas
2 at the moment you can be more sustainable. If you think
3 it's dry, water levels are starting to draw down, you don't
4 push the system as hard, so you're conservative in trying
5 to look after your resource. But if the costs increase
6 that much, then irrigators will be forced to generate as
7 much income as they can to pay for these excessive charges.

8
9 MS WARD: Thanks, Peter. We'd like to take some questions
10 now from the panel.

11
12 THE CHAIRMAN: You have only 10 minutes left all
13 together. Do you want to keep going?

14
15 MS WARD: Can I just see if anyone has any questions on
16 that very quickly?

17
18 THE CHAIRMAN: No, we'll pass.

19
20 MS WARD: I must comment that I do think it's a bit unfair
21 that the time gets tighter at the end of the day, and the
22 later --

23
24 THE CHAIRMAN: No, you're getting your hour, plus a bit.

25
26 MS WARD: Thank you. Everyone has been running late this
27 morning.

28
29 THE CHAIRMAN: Yes, but you are getting your hour, plus a
30 bit.

31
32 MS WARD: Thank you. Can I now invite Lyn Davies up to
33 speak on behalf of the Buddah Lake system, on fixed to
34 variable costs?

35
36 MS DAVIES: Thank you for allowing me to speak. I'll be
37 very brief because a lot of what I have to say I think
38 Michael Egan has touched on.

39
40 I represent Buddah Lake Irrigators' Association which
41 is a private scheme operated on the Macquarie, but I
42 probably speak for all the irrigators in the valley on the
43 issue of the fixed to variable ratio.

44
45 I have done a few notes on other utilities that we use
46 as a service for Buddah Lake. The calculation with Country
47 Energy, which is a similar service, is that we pay about 2

1 per cent fixed costs. In the drought I think that was very
2 pertinent because they received from us about \$2,400. In a
3 normal year they would receive probably about \$130,000 or
4 \$140,000, so they are managing the risk. Perhaps State
5 Water could look at the ways that they are managing that
6 risk.

7
8 The other utility we use is Telstra, not that we are
9 all favourably disposed towards Telstra, but their fixed
10 versus variable rate is 12 per cent fixed for the Buddah
11 Lake scheme and 88 per cent variable. I am wanting to
12 highlight the other utilities that we are customers of.
13 Perhaps State Water could really have a good look at how
14 they are charging. I have a few other points, but I don't
15 really think it will matter if I don't say them because
16 Michael has covered that.

17
18 There are a number of ways that State Water could
19 manage this with hedging, or probably commercial insurance.
20 As I said with the electricity industry, the Sydney Futures
21 Exchange would probably be only too happy to speak to State
22 Water and they could perhaps work out ways that this could
23 be achieved so that we are paying much less of that cost.
24 Even the 40 per cent that they are proposing, 40/60, I
25 think is probably a little high. That's about all I've got
26 to say. Thank you.

27
28 MS WARD: That was a bit quicker. Now Peter O'Brien will
29 finish off on return on investment.

30
31 MR O'BRIEN: Thank you, Mr Chairman. I'm an irrigator on
32 the Tenandra scheme and I'm on the customer service
33 committee. I believe 7 per cent is not an appropriate
34 figure to be expecting users to pay as the return on
35 investment. I pose the question as to what is an
36 appropriate figure for ROI for other utilities, and I
37 certainly don't think it would be as high as 7.7 per cent which
38 represents a private sector investment that is high risk
39 and generally doesn't offer capital gain potential. I just
40 don't think that a public water distribution utility fits
41 into that category at all.

42
43 The proposal is such that we are asking just one
44 customer with the least amount of rights to cover this
45 large return on investment as well as all the other costs
46 we are being asked to cover. In the recently instigated
47 installed river management plan irrigators ranked at the

1 bottom of the pile. The environment, local government, and
2 all of the stock and domestic entitlements come ahead of
3 us, yet we are being expected to pay all of the cost
4 recovery, and now you're asking us for a large return on
5 investment as well. We just think that's completely
6 unreasonable and it's exploiting a monopoly situation if it
7 happens.
8
9 In the Macquarie, water users only access about 28
10 per cent of the total flows, which is one of the lowest in
11 the state. In fact, the largest allocation by far is the
12 one for the environment. They are non-payers; they have a
13 20 per cent licence as well as all the other water that
14 Glen mentioned earlier that goes to the environment. Then
15 there's the other beneficiaries, being the people who
16 receive protection from flood by virtue of Burrendong,
17 being this city and the other towns on the valley. Again
18 we are seeing irrigators with lowest priority being asked
19 to support the costs and the high investment return as
20 well. In low allocation years the large amount of flow
21 that goes to the environment and the statutory requirements
22 on the river, none of those people pay at all.
23
24 We are being asked to pay on what we believe is
25 somewhat of a substandard asset. The point in question is
26 that the valve capacity at Burrendong is inadequate for
27 peak demand in years when the dam is getting a bit low. It
28 means water cannot be released fast enough to meet the
29 needs of the irrigators, and often times that's a critical
30 period in the year for farmers' crops. I might add that if
31 there's a release to the environment going on at that time,
32 then it takes precedence over irrigators' access to the
33 valve.
34
35 Start up, transition period, et cetera - we think it
36 would be inappropriate for State Water. It's only been
37 going for less than a year. They inherited some fairly
38 run-down infrastructure. They're still having trouble
39 getting their systems up and running and at this stage some
40 of the water accounts for last year haven't yet issued,
41 just as an example. We think there certainly should be a
42 transitional period where State Water gets on its feet.
43 In Queensland, for instance, the return on investment has
44 been waived for, I think, five years and payment for the
45 charge price for the first period has been extended from
46 three to five years. We think that's what should happen
47 here as well.

1
2 This one here, perhaps Michelle could comment on that.
3 It's not appropriate to be paying a return on investment on
4 some capital items.
5
6 MS WARD: Again, it's just a confusion with being able to
7 sift through the DNR versus State Water reports to
8 understand the conflicts that come up when you're changing
9 from the line in the sand and the legacy issues and where
10 we're being asked to pay a rate of return on assets when
11 their condition isn't adequate and they're not our
12 responsibility.
13
14 MR O'BRIEN: They're asking for a return on an asset
15 that's delivering an enormous community benefit. I touched
16 before on the flood mitigation of the whole valley,
17 particularly this city. That's the main reason the dam was
18 built when it was built. IPART and COAG have indicated
19 that where investment delivers good public benefits, then
20 the return on assets need not be required. We have a
21 little quote here from that organisation to illustrate
22 that. This was in the December issues paper on the pricing
23 of bulk water and it stated on page 19:
24
25 The current rate of return will depend on
26 whether or how public goods and services
27 are valued and paid for by government.
28 Where investments in the water industry
29 have been made for other than economic
30 reasons and a positive rate of return is
31 unlikely to be achieved, the expert group
32 says that if those currently benefitting
33 from services provided by the investment
34 are prepared to meet the cost of supplying
35 these services in the future, but without a
36 rate of return on assets, the minimum
37 financial viability test adopted by COAG
38 would be satisfied.
39
40 That means no capital return. This slide shows some
41 figures here and we are somewhat confused. In spite of
42 seeing the figures from the DNR's presentation earlier, it
43 appears here that the return on assets that's being sought
44 from the customer is \$20m, which to my way of thinking
45 represents roughly a 7 per cent return on \$300m, yet we
46 appear to have only a \$110m share in the RAB. I am just
47 posing that question as to something we are confused about.

1 The question is: is the government paying its ROI on its
2 share? It doesn't look like it. The irrigators certainly
3 are. While we argue that 7 per cent is too high a return,
4 it's certainly inappropriate if we are being asked to pay
5 on something that's not our share. Thank you.

6
7 MS WARD: Thanks, Peter. Thanks for the extra time.

8
9 THE CHAIRMAN: You can have a few more minutes. There
10 are just a couple of points. State Water is best able to
11 respond to RAB, rates of return, and things like that.
12 They can do that this afternoon.

13
14 I will just make a comment on rates of return. This
15 is a critical issue, obviously, in doing a pricing
16 determination. We have not come to a view on that at this
17 stage; we haven't even begun to come to a view on that.
18 But, if you look at rates of return by utilities determined
19 by regulatory authorities in other states and also by
20 IPART, there are instances as high as 7 per cent, but 7
21 per cent is probably near the upper end. To give you an
22 instance which is relatively recent on IPART's part, though
23 financial markets can alter it since then, we did Sydney
24 Water last year and we used 6.5 per cent for Sydney Water.
25 That was metropolitan water supply for domestic usage.
26 That gives you a little bit of background. Are there
27 questions from the secretariat?

28
29 MR COX: I have a question. I wonder if I can go back to
30 the less than average use issue that you raised. You
31 suggested there were a number of ways in which State Water
32 might be better able to manage that risk themselves, rather
33 than pass it throughout to customers - and that may or may
34 not be the case. If it is the case, there will be
35 additional costs to State Water from doing so. Are users
36 happy to pay a share of those additional costs?

37
38 MR EGAN: Yes, I think in the normal economic events that
39 happen on a yearly or daily basis. Most insurance premiums
40 are 1 or 2 per cent at the moment, so our main argument is
41 a 53 per cent risk premium is just way over the top. If
42 it's part of cost recovery, 1 or 2 per cent, that's fine.

43
44 MR WHITTAKER: I'll just make a quick comment if I could.
45 I guess it concerns me a little, the perception that the
46 irrigation industry or the building of the dam is a
47 negative impactor on the environment. I guess I'd like to

1 clarify that a little bit.

2
3 There are scenarios where the dam and irrigation are a
4 negative impactor on the environment; there are quite a
5 number of scenarios where the dam and irrigation is quite a
6 positive impactor on the environment. If you look at the
7 figures for the drought period, there are a number of
8 effluent creeks and wetlands that would not have seen water
9 for the last four years. Because of the dam and
10 irrigation, they have a twice a year call on getting water.
11 Also, you have the Macquarie Marshes. That has a number of
12 issues with regard to erosion, salinity, and a whole range
13 of issues that are being dealt with under this banner that
14 are not impacted at all by the dam or irrigation. I guess
15 at the end of the day the Macquarie Marshes are receiving
16 something like about 85 per cent of the natural flow, so we
17 can't put it all down to irrigation and the dam. Thank
18 you.

19
20 MR O'BRIEN: Can I just respond there, Mr Chairman? You
21 referred to Sydney Water. Well that's fine for them to be
22 achieving a rate of return of 7 per cent.

23
24 THE CHAIRMAN: I said 6.5 per cent,

25
26 MR O'BRIEN: Okay. That's fine, if they're achieving a
27 rate of 6.5 per cent, but I'd suggest that they don't have
28 only about 28 per cent of the users paying for the amount
29 of water that flows through the system.

30
31 THE CHAIRMAN: I'm not sure where you got your figure
32 from. I would like to wind this up now. I think the point
33 is well taken that dams can have a positive effect for the
34 environment; I accept that point.

35
36 In closing this session, I would like to thank you. I
37 am particularly conscious of the point you made at the
38 outset, Michelle, that this process does make heavy demands
39 on people who, frankly, have other things to do - some even
40 perhaps more important things to do. We are particularly
41 grateful to you for making your time available today and
42 the effort you have put into it. It has been very helpful
43 for us to hear first-hand your criticisms and the critiques
44 of what's been put before us by the other authorities. I
45 am especially grateful for your contribution today. Thank
46 you.

47
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1 JEMALONG IRRIGATION

2
3 THE CHAIRMAN: We still have the Jemalong irrigation
4 scheme to hear from. I was wondering if Jemalong would
5 agree to going after lunch?

6
7 MR MOXEY: It will be quite brief.

8
9 THE CHAIRMAN: Would you like to go now?

10
11 MR MOXEY: Yes. Thank you very much. I do appreciate the
12 opportunity to present. Just for your information, I'm
13 also the chairman of Lachlan Valley Water, so the thoughts
14 Mary Ewing put forward on behalf of the Lachlan are
15 concurred with by the members of Jemalong Irrigation who I
16 represent here today. That's probably why my presentation
17 will be quite brief, because all I want to do is cover a
18 couple of the key issues that are particular to the
19 Jemalong private irrigation district.

20
21 Jemalong Irrigation is a small area. Probably after
22 all the presentations yesterday from Murray Irrigation and
23 the MIA, we will be fairly small in comparison to those,
24 but in our minds we are quite significant. With 300
25 kilometres of channel and 96,000 megalitres of irrigation
26 water, we think we provide quite a boost to the economy in
27 the Lachlan area.

28
29 One of the main points I wanted to deal with today is
30 the bulk water pricing discount and how it applies to
31 Jemalong Irrigation. A little bit of the history there was
32 that at privatisation we were advised to do a hundred year
33 business plan to justify the long-term viability of
34 Jemalong Irrigation. This was done under the premise of
35 this pricing policy continuing. Most of the basis of that
36 long-term budgeting was on the prices that were in place
37 and just CPI or natural increases that may occur.

38
39 The movement away from this pricing discount will have
40 a major impact on irrigation districts such as Jemalong and
41 the other private irrigation districts in that it will
42 actually take away their ability to be viable in the
43 long-term because we believe that the lack of clarity that
44 is there when you move from a bulk water price discount to
45 a discount for service is just not written into any of the
46 statements or agreements that we see before us at this
47 time. So it's very much a pie-in-the-sky sort of proposal

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1 that we will then move to a discount for service when those
2 discounts have not been specified or explained or described
3 in a detailed way. We need more clarity into that part of
4 it before we can have any confidence in moving from one
5 system to the other.

6
7 I suppose a pretty good example of that is State Water
8 saying that its costs are the same for reading one meter
9 against another, so the same price for all meters, when one
10 might read 10 megalitres and one might read 10,000
11 megalitres, and then their pricing structure is on a
12 megalitre basis. That was the main point we wanted to make
13 known. I am sure you are aware of that because it is
14 outlined in our submission.

15
16 Speaking to the DNR submission, we believe that DNR's
17 primary functions should be in licensing and those
18 functions should be reflected in true commercial licensing
19 charges. As far as Jemalong Irrigation goes, these
20 licences are issued and adhered to by Jemalong Irrigation.
21 The amount of monitoring that's done at a cost to the
22 levies on Jemalong Irrigation users and the CMA to make the
23 land and water management plan work are significant and at
24 no cost to the DNR for their monitoring and reporting
25 systems. So we cannot see that there's any other functions
26 there, other than the licensing, and, if that was kept to a
27 commercial rate, that would be much appreciated.

28
29 The only other point that I would like to make today
30 is the Jemalong Weir maintenance charges. We noticed that
31 State Water had it up there as some of their past works,
32 the Jemalong Weir. I would just like to emphasise the fact
33 that in the past Jemalong has been paying 92 per cent of
34 the maintenance costs for that weir and the work that's
35 been done on the weir. I don't think it's significant in
36 past budgets for State Water, so it probably shouldn't have
37 been highlighted there; it only muddies the waters.

38
39 It was indicated that we would move away from those
40 principles and the costs of maintaining the weir would be
41 spread over the whole valley. We would like to highlight
42 that the agreement when we privatised was that there would
43 be approximately \$29,000 a year average annual costs for
44 maintaining the weir, and up to date it's been \$69,000 a
45 year for the last 11 years. So to see this move from a
46 cost that is going to be spread over the whole valley and
47 taken away and State Water making it look like a real plus

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1 to the Jemalong irrigators I think is an unfair display
2 because it isn't. There's no reimbursement of what has
3 been paid; there's no consideration in our bulk water
4 discounts in the future to recoup any of those costs that
5 have been paid over the last 11 years at a much higher rate
6 than was in our business plans to start.

8 In closing I would just like to say that we believe
9 that State Water and DNR services should be open and fully
10 contestable. That's another one of the things that we need
11 to see as this process moves forward. Thank you.

13 THE CHAIRMAN: Thank you. Is there anything in
14 particular you wanted to raise?

16 MR SEERY: Just one question. The wholesale discount that
17 Jemalong has is 27 per cent. Do you have any understanding
18 as to why it was set at 27 per cent?

20 MR MOXEY: It's a long while ago. No, I haven't. I'd
21 have to research that more to try to get the information,
22 but proportionately less than the rivers in the south, but
23 I suppose it's maybe on the amount of megalitres, but I'm
24 not real sure of that.

26 MR SEERY: And do you pay for conveyance losses?

28 MR MOXEY: Yes, we pay for the conveyance losses.

30 THE CHAIRMAN: Thank you for your presentation. It might
31 interest you to know that, when you made the comparison
32 with the Murray and the Murrumbidgee schemes, nothing got
33 more debate yesterday than wholesale discounts, so the sort
34 of points you were making were made at enormous length
35 yesterday. Thank you for your presentation today.

37 We will now break for lunch. Having regard to the
38 time, we will resume at 2 o'clock when there will be an
39 open session for people from the floor to raise any points
40 that they would like to raise in terms of comment or
41 questions, or issues that have not been covered so far. We
42 will finish with the two authorities responding to those
43 questions and comments.

45 LUNCHEON ADJOURNMENT

46
47

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1 STATEMENTS AND QUESTIONS FROM PUBLIC

2

3 THE CHAIRMAN: Ladies and gentlemen, this is the moment
4 where you have an opportunity to have your say. Do I have
5 any comments or questions from the floor?

6

7 MS WARD: Michael, I just wanted to touch on Sydney Water
8 and their rate of return of 6.5 per cent. I suppose I'm
9 looking for the comparisons and the differences between the
10 businesses. One immediate thing I can illustrate is in
11 terms of variabilities of supply. I realise there's been
12 pressure in terms of droughts, and whatever, on urban areas
13 as well, but you can still actually turn on the tap and get
14 access to water. You might be paying for it, but it is
15 almost a 100 per cent reliability access system, as opposed
16 to bulk water supply, which is based on an allocation
17 system, as far as I understand.

18

19 I think Peter O'Brien mentioned that figure of
20 28 per cent to you. I'm not sure if you understood where
21 that came from, but Peter was referring to water customers
22 in the Macquarie Valley actually accessing 28 per cent of
23 the total flows in this valley, yet being asked to pay
24 7 per cent on the total customer share.

25

26 THE CHAIRMAN: I will just make a response to that. When
27 you decide to invest in a business you have to earn a rate
28 of return on that capital. I mean, if you are going to
29 invest in a farm, then you have to earn a rate of return on
30 the investment in the farm. The same applies for a
31 government. If a government isn't earning a rate of
32 return, there is a very significant risk of
33 over-investment. So that is where it comes from.

34

35 Now, the differences in rates of return between
36 businesses essentially reflect the riskiness of that
37 business - not the riskiness of their customers, but the
38 riskiness of the business - and, frankly, how volatile the
39 revenue is in relation to what is called economy-wide risk.

40

41 What you find with utilities is that there is some
42 variation between them, but generally they are somewhere in
43 the range of the high 5s to 7 per cent across Australia for
44 different utilities, and that is the point I was making.

45

46 In this case it would only apply to the
47 capital - well, the total capital is subject to a 7 per

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1 cent rate of return. However, only some of that is
2 recoverable from customers because the government, of
3 course, has to share it as well.

4
5 MS WARD: Thank you. There was just one more question,
6 which is to State Water. Making sure we are keeping the
7 IPART process rigorous as well, I'm putting the question
8 about the 2001 determination: how much money was actually
9 meant to be passed from DNR to State Water over the
10 three-year period versus how much actually came to
11 State Water? So that is a question to State Water which
12 IPART would be interested in, I imagine.

13
14 THE CHAIRMAN: Let me just add to that. A number of the
15 questions that are raised by people today point us in the
16 direction of areas where we should pursue answers ourselves
17 when we come to putting together our determination. So
18 even if we don't get a full answer right now, it certainly
19 helps to have these questions so we can follow up.

20
21 Also, I will just mention that State Water and the
22 department will respond to all questions and comments after
23 this session.

24
25 MR CLEMENTS: John Clements, Namoi Water. This is
26 question to DNR. I'm probably not going to phrase this
27 question very well - it is a convoluted issue - but in
28 terms of your approach to IPART for a pricing
29 determination, that is a change on four or five years ago
30 brought about by a number of things, were there any
31 regulatory changes that allowed you or caused you to make
32 this direct approach to IPART in terms of regulation?

33
34 THE CHAIRMAN: We will give them an opportunity to
35 respond to all questions later on, unless you particularly want
36 to do it right now.

37
38 MR CLEMENTS: So to be clear, there have been significant
39 changes in the separation. What were the regulatory
40 changes that brought DNR to the point of making direct
41 submissions?

42
43 MR RUNDLE: So I can be clear on this, the separation of
44 State Water from DNR has required new pricing orders be put
45 out by IPART, and it requires DNR, through the Water
46 Administration Ministerial Corporation, which the pricing
47 of water relates to, to put in a separate submission.

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1 Similarly, we have a separate pricing submission for
2 State Water.

3
4 I guess the short answer to that is that basically it
5 is out of the control of DNR and State Water. It has been
6 imposed on both organisations, but they are separate
7 entities and they have separate functions and,
8 consequently, separate pricing audits relating to each. As
9 a consequence, we need to put in separate submissions.
10 That, of course, involves having separate types of charges
11 for each service. I don't know if that answers your
12 question.

13
14 MR CLEMENTS: We are getting there, and I don't want to
15 take too long. So it arises out of the amendments to the
16 Water Management Act and the amendments in terms of the
17 corporatisation of State Water. Those are the procedures
18 that have led to separate submissions?

19
20 MR RUNDLE: Well, originally it comes from COAG to have
21 separation of functions of water delivery operations and
22 regulation.

23
24 MR CLEMENTS: I'm more interested in the process in
25 New South Wales. The history, you're right, is relevant
26 and interesting, but in terms of the parliamentary process
27 of New South Wales and legislative process, there are
28 processes that have led to this separation and led to these
29 submissions. Is that correct?

30
31 MR RUNDLE: That's right, yes. In fact, State Water has
32 established under its own legislation, it is a separate
33 corporation, to undertake operations on regulated rivers
34 and a separate pricing order has been established through
35 IPART for the purposes of setting prices. Therefore, they
36 are putting a separate submission in.

37
38 Similarly, we are carrying on with the water resource
39 management function, which we did previously. Now, the
40 Water Management Act has come into it, but under the
41 Water Management Act I should mention it gives the power to
42 the minister to set fees and charges, but it has got a note
43 also saying that it is subject to determination approval by
44 IPART of those charges for 40 water administration
45 ministerial corporations.

46
47 MR CLEMENTS: Thank you.

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1
2 THE CHAIRMAN: Perhaps I can just give you a very simple
3 answer: when the 2001 determination was made there was one
4 organisation: the Department of Land and Water
5 Conservation. It covered both functions, both State Water
6 functions and water resource management functions, so it
7 put in one submission because it was one organisation. Now
8 there are two organisations, so we have two submissions.
9

10 MR MURRAY: Michael Murray from Gwydir Valley Irrigators.
11 A question mainly to IPART themselves, but also I would be
12 interested in State Water and DNR's response. Certainly in
13 the 2004 State Water submissions, but I think also in 2005
14 and also in the DNR submission there was a suggestion that
15 neither organisations ever actually received all the money
16 that they were actually due after the 2001 determination.
17 I'm just wondering is IPART making any effort to do an
18 audit and reconciliation of whether all charges that were
19 due have been paid and the response from DNR and
20 State Water as to whether they believe they have been
21 short changed in the process.
22

23 THE CHAIRMAN: Certainly a concern has been that not all
24 the moneys that were paid for the annuity approach were
25 then spent on capital, and that is something we are
26 checking out.
27

28 MR MOXEY: Dennis Moxey here from Lachlan Valley Water.
29 I just have a couple of points of clarification from our
30 presentations earlier this morning, I suppose, not so much
31 direct questions, but DNR made the statement that they were
32 involved in the customer service committees, and I'm the
33 chair of the customer service committee in the Lachlan and
34 there is no direct representation there from DNR, and we
35 only use them as a request for information.
36

37 The CMA now have a budget for the coordination of
38 programs and also monitoring, and this is a significant
39 part of the monitoring that will go on in our valleys from
40 now on. To date it has dealt a lot with vegetation, but as
41 we go through that process, it will deal a lot with the
42 monitoring of water and river systems, wetlands and a lot
43 of the functions that were outlined to us this morning in
44 the DNR presentation.
45

46 So I just wanted to clarify that because I felt that
47 the presentations this morning probably portrayed a larger

1 job that wasn't funded that DNR and State Water were doing
2 and I wanted to point out that the government has that
3 partially or significantly covered under the funding
4 through the CMA's budgets.
5

6 There was also a big emphasis on groundwater and the
7 debate that's going on at the moment about over-allocation
8 of groundwater and the jobs that that imposes on the
9 different departments - DNR particularly - and the work
10 that they have to do, but as we discussed, I would like to
11 emphasise the fact that the impactor pays and the impactor
12 at the moment, for most of the work that is going on, is
13 DNR from the over-allocation, because most of the work in
14 groundwater at the moment is the reissuing of licences for
15 reductions in groundwater sustainable yields because of
16 over-allocation and the work that is being done there.
17

18 A lot of the funding that is coming out of the
19 Groundwater Structural Adjustment Committee is actually
20 funded out of that NWI amount of \$110m, so there is \$1m or
21 so going towards the work that is being done by DNR for the
22 groundwater structural adjustments, so there's not a lot of
23 costs incurred there with that process.
24

25 Also, the lack of confidence that we probably have in
26 the State Water to reconcile the income at the end of the
27 period. Irrigators are not about making loans to
28 State Water without some justification and some formulas,
29 particulars, as to how that might be done and how it would
30 be impacted and why State Water won't just grow as an
31 organisation and consume the funds before they are
32 reconciled. Thank you.
33

34 MR WALSH: Tony Walsh from Macquarie Valley. I would
35 like to make a point of clarification: Michelle's question
36 earlier, I felt a little bit confused that in one sense it
37 was talking about the rate of return on investment, but the
38 reality in this valley is that irrigators actually draw
39 approximately 26 per cent of the valley water resource on
40 average, so that means that about 1 per cent is used by
41 towns. Seventy-three per cent of the water that flows
42 through this valley is actually available to the
43 environment in one form or another, and yet irrigators pay
44 far, far more than that 26 per cent of the cost of all of
45 that water.
46

47 So I just wonder whether those points were understood

1 by the tribunal and the reality that government, in one
2 form or another, through State Water and DNR is actually
3 asking for a far higher contribution from irrigators.

4
5 THE CHAIRMAN: The question is, yes, we do understand.
6 What I want to make clear is it doesn't affect the rate of
7 return. It may affect the cost sharing, but not the rate
8 of return.

9
10 MR WALSH: That is understood. The cost sharing was the
11 issue that I wanted to home in on.

12
13 THE CHAIRMAN: I think we are at risk of confusing the
14 two.

15
16 MR CALDWELL: Robert Caldwell, independent irrigator from
17 the Lachlan. I have about three or four problems with what
18 has been said here this morning, and I think I should draw
19 them to the attention of the tribunal.

20
21 The DNR establishing water titles and allocations have
22 been changed to a share of an unspecified resource. My old
23 licence has been changed from a figure in megalitres to a
24 share of the resource which is unspecified. I believe this
25 is a calculated deceit to avoid compensation and diminish
26 property rights. The forms for the titles are like that,
27 the new ones are like this, and it is just in a state of
28 limbo at the moment. There is more uncertainty now than
29 there was before, so I'm not sure that their claim that
30 there is more secure title is true.

31
32 I dispute State Water's claim of \$100m for Wyangala
33 safety upgrade. If they want to double the spillway they
34 should move Cowra because of the threat to life and short
35 warning times. In other words, the technical risk analysis
36 is in serious question there.

37
38 High security versus general security. On the
39 Lachlan, the conversion rate is 45 per cent. In other
40 words, you forfeit 55 per cent if you are converting.
41 Now, it is not a loss of capital value, but it is a loss in
42 volume in that if you convert from general security to
43 high security, you are diminishing the amount of water that
44 you will receive, so then you diminish the amount of money
45 you can earn from it. Then, after diminishing the volume
46 by 55 per cent and then increasing the charges by 2.4 or
47 3.9 is a bit of a double impact.

1
2 The last one is the fixed versus the variable.
3 State Water seem keen on the concept of increasing their
4 fixed charges, and there's a side which hasn't been brought
5 up in this issue, and that is if you have got environmental
6 volumes being increased or demand is coming for
7 environmental reasons and you're stuck on fixed charges,
8 then there is a - State Water, for example, are insulated
9 against that. It is not important to them to sell water
10 and make water available for productive use. They can give
11 it to the environment without compensation and they can
12 extract the charges from the irrigators even though they
13 are selling them less water, and compensation is not
14 forthcoming.

15
16 If you keep clawing back allocations, then
17 productivity will be reduced. A lot of the environmental
18 demands are technically questionable, and I don't think
19 that we can just tolerate the claims of Paul Wettin and
20 these sort of people when you have counterclaims coming
21 from environmental professionals saying that Gary Jones and
22 these sort of people that have been pulled up in parliament
23 have not substantiated environmental claims.

24
25 So that is a little background as to what some of the
26 hidden - I mean, the pricing is relevant in that what are
27 you pricing. If there is some question as to reliability
28 or availability, then the price has a relevance to the
29 situation. I just wanted to draw that to your attention.

30
31 THE CHAIRMAN: Thank you.

32
33 MR BRUCE: John Bruce, Lachlan Valley irrigator. I would
34 like to make a comment to the tribunal about the relativity
35 of high security versus general security charges. I think
36 that what State Water are trying to do is to increase the
37 proportion of high security charges too much, and that will
38 encourage the use of groundwater in times of high supply of
39 general security water, when people would normally go away
40 from using their bores because of the high cost of
41 pumping - that is, the high cost of water plus pumping
42 versus the cost of river water plus pumping.

43
44 So if you increase the price of high security too
45 much, high security water becomes cheaper to use than bore
46 water, which encourages an overuse of the groundwater
47 resource in a time when you should be giving it a rest.

1
2 MR CALDWELL: I would like to add a comment to that: the
3 price of water is set as a spot price each year, and it is
4 independent of the actual water charges, so in a plentiful
5 year the price of water is going to be down.
6
7 THE CHAIRMAN: Are there other comments or questions? Let
8 me say, obviously the presentations this morning made a lot
9 of comments and I would expect that State Water and the
10 department will be responding to many of those comments.
11
12 MR MIELL: Doug Miell, New South Wales Irrigators Council.
13 I have a question for State Water with respect to risk
14 management. I am wondering whether they'd like to share
15 with us some of the other options they considered and
16 discounted when they adopted the 1 per cent standard
17 deviation.
18
19 THE CHAIRMAN: Thank you for that question.
20
21 MR CLEMENTS: John Clements, Namoi Water. Given that this
22 process is, I guess, about a pricing regulator attempting
23 to monitor and take a role in the activities of monopoly
24 providers in New South Wales, and certainly we are dealing
25 with a monopoly in this situation, I would like to ask a
26 question of State Water that can be answered now or later
27 on. In terms of their original draft submissions, what
28 role did Treasury take in instructing or directing aspects,
29 particularly cost share aspects and other aspects in the
30 final submission that went to IPART? Given that we are
31 looking at a monopoly process, I think it's a relevant
32 question, Treasury being the major regulator and, indeed, a
33 regulator of SOCs, so I would like to know in terms of
34 direction and instruction what role they had in the
35 preparation of the submission to IPART of State Water.
36
37 THE CHAIRMAN: A question from the front?
38
39 MR EGAN: Michael Egan, Macquarie. I would like to ask
40 for the benefit of IPART whether we can ask State Water
41 whether they can separate the costs of operating the flood
42 mitigation zone - to be able to separate those costs out
43 for the future benefit of costings?
44
45 THE CHAIRMAN: If there are no further questions and
46 comments, I will ask State Water to come forward and
47 respond to comments and questions.

1 RESPONSE BY STATE WATER CORPORATION
2
3
4 MR IMMARAJ: Thank you, Mr Chairman. We'll cover off in
5 the first instance the presentations and issues arising
6 from the presentations this morning. Then we'll go to the
7 questions.
8
9 Lachlan Valley Water raised some questions with regard
10 to State Water's annual reports and the accounts. One of
11 the key issues for us has been the determination of the
12 regulatory asset base value for fishery or water supply
13 which the New South Wales Audit Office had some questions
14 on. They have come up with a value which is different to
15 that of State Water, so that issue is being currently
16 resolved. We see it being resolved soon. As soon as the
17 advice from the Audit Office is received, we will be
18 forwarding a copy to IPART as well as publishing it.
19
20 One of the questions related to the long-term average
21 one standard deviation below. As I mentioned, it is
22 intricately linked with the drive towards greater variable
23 costs. In other words, State Water has a requirement to
24 move towards up to 60 per cent variable revenue, as against
25 currently 70 per cent fixed revenue. So we have been asked
26 to take much more risk in our revenue base. That is why
27 the one standard deviation was proposed. We think those
28 two should be looked at in conjunction with each other,
29 rather than just in isolation.
30
31 We note there were a range of views on the
32 fixed/variable ratio, but there seems to be a consistent
33 view that the one standard deviation is not acceptable. We
34 think both of them should be jointly addressed. If the
35 requirement to move to a high variable revenue is removed,
36 then equally importantly the one standard deviation is not
37 required because it is there only as a risk management
38 tool.
39
40 I think Michael Egan raised this issue with regard to
41 risk management and the options that State Water looked at,
42 and shouldn't an insurance provider be able to cover that
43 risk, say, at a 1 per cent premium. When the operating
44 licence was drafted and State Water was given an
45 opportunity to comment on it, one of the big ones we had
46 difficulty with was this drive towards consultative
47 pricing. The government was keen to move to its 60

1 per cent variable. State Water was obviously very keen to
2 remain at 70 per cent fixed because it's a very low risk
3 position.
4
5 In the interests of checking the various options and
6 going back to government and arguing our case, we looked at
7 three scenarios. What if State Water moved to 100 per cent
8 variable revenue, in other words get rid of fixed charges
9 all together? Some of the submissions from the customers
10 and in particularly from the Lachlan valley after three
11 years of drought to the government said that they found it
12 ridiculous that State Water should be sending bills to
13 customers in a period of drought. Surely there should be
14 no bills when there's no water available for the
15 allocation. That was the general security. So we looked
16 at the 100 per cent variable option; the Minister asked us
17 to check that out.
18
19 The second option was to stay with the 30 per cent
20 variable. Thirdly, just to check off on sensitivity, we
21 looked at zero per cent variable, in other words all our
22 costs and revenues are fixed.
23
24 We looked at insurance providers and, as all government
25 state-owned corporations are covered by a Treasury
26 managed fund, we sought their views on what would
27 be the premium if we were to ensure against the revenue
28 fluctuations. Their response was: what is the long-term
29 average sales? The ratio premiums are largely linked to
30 the same percentages of the variable of the total. In
31 other words, a 100 per cent variable would attract a much
32 higher premium than a zero per cent variable. That stands
33 very much in logic.
34
35 Our objective was that we had to survive a drought
36 sequence of, say, three years roughly. At a value level we
37 couldn't afford cross-subsidies across valleys, and I think
38 the point Michael made was that we are a state-wide
39 operation, so therefore not all areas will be in drought.
40 But the other principle of the submission was that we had
41 to try to make transparent all cross-subsidies amongst
42 valleys, intervalley subsidies. The objective was to
43 survive a drought sequence at a valley level subject to a
44 60 per cent variable and 40 per cent fixed revenue base.
45
46 Following that, two option groups came up. One is
47 externally insuring, or internal insurance. Could we go to

1 an external insurance provider and cover that, in which
2 case all premiums, as long as there are no claims, that is
3 gone and it becomes an operating cost to the business and,
4 as IPART pointed out, would customers be willing to
5 externally insure given that the premiums could be quite
6 high?
7
8 The other option was internal insurance which is to
9 use the IPART process, so we will put in albeit a
10 conservative risk management approach, but at the end of
11 the price determination process IPART has a claw-back to
12 say: you've over-recovered for the past three years, so
13 the following price determination would offset that. That
14 was the decision of the corporation in moving towards
15 internal insurance, because it keeps the cash within State
16 Water Corporation and its customers.
17
18 I might just go to Geoff to comment on the issue of
19 State Water Corporation delivering services efficiently.
20
21 MR BORNEMAN: I think the question is more could we do
22 things more efficiently. What I would be hoping is that we
23 have created a culture within the organisation and a
24 culture with our customers of continuous improvement, that
25 we are always looking to move forward, not to accept that
26 we are doing everything efficiently. It was mentioned that
27 in times of drought there is a significant amount of effort
28 put into doing stock and domestic replenishment. In terms
29 of looking at how we do that, what is the most efficient
30 delivery of water, we have been actively looking at that
31 and we think we are making headway. It has been recognised
32 by the customers, the way State Water has managed the
33 drought, in conjunction with its customers in the Lachlan.
34 We certainly have clawed back our operational losses. We
35 have looked at how we can use the least amount of water to
36 provide the maximum to customers. We are now looking at
37 those lessons learned to see if we can translate them into
38 an ongoing strategy to minimise losses.
39
40 One of the other things we have done in the Lachlan is
41 to look at how we provide customer service. Previously we
42 had five offices in the Lachlan and six officers. We are
43 in the process of rationalising those offices. We have
44 closed two and are about to close a third, so we will have
45 gone from five to two. We have looked at numbers of
46 officers and are rationalising those from six to five.
47

1 One of the things we are particularly proud of in the
2 Lachlan, and we are moving this way in the Macquarie as
3 well, is the project we have undertaken of willow removal.
4 In the mid Lachlan we made substantial progress in removing
5 willows there. We spent about \$200,000 in the mid Lachlan
6 in removing willows and we've had substantial increases in
7 channel capacities and efficiencies as a result of that.
8
9 Another thing we are particularly proud of is we have
10 received in the central area - and my SCADA technical
11 officer has received, in conjunction with the rest of the
12 staff - a state award and a national award on the use of
13 technology in automation and how we control our structures.
14 As I said before, this certainly gives us efficiencies in
15 how we do things. It decreases the costs of how we do it
16 but, more importantly, it's a real time technology. We
17 should also mention CAIRO which is our process for running
18 the rivers, our computer-aided program, and we continue to
19 look at how we continue those efficiencies.
20
21 MR IMMARAJ: Peter raised the question on return on
22 investment, so I will ask Russell to comment quickly on
23 that.
24
25 MR SIMONS: Very quickly, Peter, you raised the question
26 about the equitability of the 7 per cent. I think that was
27 reasonably well answered by Michelle and the chairman in
28 comparison to Sydney Water where Sydney Water has quite a
29 low variability of demand in their water, whereas State
30 Water has quite a large variability. Therefore State Water
31 is exposed to much more risk which leads to higher costs
32 for State Water.
33
34 MR IMMARAJ: The next group of points or questions related
35 to the allocation or attribution of costs to other
36 beneficiaries, so the cost sharing type of questions. We
37 have grouped those.
38
39 Lachlan Valley Water raised this issue about stock and
40 domestic users, that during drought they are a very big
41 percentage of input costs. We recognise that and we have
42 been discussing with the natural resource regulators, DNR
43 as well as DEC, with regard to how we can get from the
44 current non-paying beneficiary and determine whether there
45 should be a cost share or contribution from them. Because
46 they are not licensed, there would have to be a CSO and
47 they would have to be supported across the board by all

1 government agencies. So it's not something unilaterally by
2 State Water to determine that stock and domestic
3 beneficiaries are going to be paying the cost of water
4 delivery.
5
6 They do have a high priority access right under the
7 water sharing plans, the Water Management Act, so that's
8 been recognised by the other agencies, and it is currently
9 looked at by agencies such as DNR, for example, as an
10 externality of running the rivers. We have also seen that
11 there is an opportunity for State Water to maintain the
12 opportunistic basis or, as Michael Egan pointed out,
13 delivering water to them on an opportunistic or efficiency
14 basis. In other words, only provide stock and domestic
15 twice a year when it's most appropriate to do so with the
16 least amount of losses.
17
18 That introduces a new level of service and an
19 opportunistic basis on which they access their water. That
20 will introduce a new level of pricing to cater for that.
21 Given the percentage of volume that is actually
22 attributable to stock and domestic - not the total amount
23 of water required to deliver that, but what is attributable
24 to stock and domestic users - it is very small in most
25 valleys. In drought years that might constitute a big
26 percentage, but in most years it's very small. Therefore,
27 it introduces a level of complexity that we are not sure is
28 efficient in trying to calculate and also trying to
29 recover. You get almost to the stage where, if you use the
30 current pricing where you use unregulated usage charge, you
31 might end up with the vast majority of 80 per cent of the
32 stock and domestic users being billed \$10. So it
33 introduces a question of efficiency.
34
35 With regard to your point of the high security,
36 general security premium, sitting at 2.4 rather than what
37 State Water has proposed, we would like to meet with you to
38 discuss how Lachlan Valley came up with the 2.4 and, if it
39 is far more substantial in its veracity than what we have
40 come up, which is the water sharing plan multiplied by the
41 number of years of storage, then we would certainly concur
42 with your position, but at this stage we don't have the
43 detail.
44
45 IPART asked the subsequent question, whether it should
46 be a differential across the state. Our submission
47 proposes differential premiums across the state, so each

1 valley which has a water sharing plan, we've taken the
2 water sharing plan premium and multiplied it by the number
3 of years of storage in the Murray and Murrumbidgee. That
4 number of years of storage is actually minimal. We don't
5 store more than a year's supply of high security because
6 it's guaranteed by the Snowy minimum release requirements.
7 Therefore, the water sharing plan premium is basically all
8 that is attributable to those valleys.

9
10 I will go on to the points with regard to the CSOs,
11 that they're not evident in State Water's submission,
12 although we do identify that there are other beneficiaries.
13 That was a considered position that we took, and this
14 relates also partly to what John Clements asked right at
15 the end.

16
17 The government's view is that the current principle in
18 the cost sharing, which is assets which have been upgraded
19 for dam safety compliance purposes, should remain a
20 government regulatory asset base and the government capex
21 contribution is in fact a government contribution to the
22 business. So in a way there was a direction that that need
23 not change, so there are some guidelines with regard to
24 that. Once the IPART determination is finalised, that may
25 lead to State Water then putting out the CSOs. There's a
26 need now for government to fund certain activities that are
27 still required which are not recovered through prices.

28
29 The flood operations capex is a government share. We
30 haven't budgeted for any costs, so therefore there are not
31 costs included in the IPART submission for flood
32 operations. If we go to flood operations mode and we start
33 incurring costs for flood operations, we intend to recover
34 those from the government. So there are no operating costs
35 in our budgets for flood operations.

36
37 You also made the point about scrapping the one
38 standard deviation below the average. I think we have
39 addressed that one.

40
41 The chargeability of other beneficiaries such as the
42 environmental flows, the risk of providing definite access
43 to operations for environmental flow of delivery needs to
44 be assessed before we head down that path. State Water is
45 aware that there are some concerns with regard to making
46 and charging, and also then beginning to define what level
47 of services are committed for those charges. It's

1 something we have not got around to yet. As soon as you
2 start making someone pay for services, you have to define
3 what level of service they are getting. Do they place an
4 order, for example? Do they have access so weirs and
5 infrastructure and capacities?
6

7 We'll come to questions raised at the end, but I'll
8 make a quick comment first. A key difference between
9 Sydney Water's operations and their variability in delivery
10 is that Sydney Water has an average of roughly around 600
11 gigalitres per year of delivery. In drought conditions
12 they might deliver 520, so the level of variability for
13 Sydney Water is fairly low and therefore it's seen as a low
14 risk. The other big difference is there is no government
15 regulatory asset base for Sydney Water's RAB. We are also
16 aware that Sydney Water doesn't have an operating subsidy,
17 so there are some issues in recognising the differences
18 between Sydney Water's WACC and State Water's WACC.

19
20 There was a question regarding whether, based on the
21 2001 determination, State Water has received its share of
22 the revenue. We will certainly give you the numbers to
23 justify what we have received and as soon as the accounts
24 are finalised you will also get the post-reorganisation
25 accounts. That was consistent with Michael Murray's
26 question with regard to whether all the revenue was
27 received.

28
29 There was another discussion regarding how the waiver
30 was funded. The waiver in the Lachlan was funded as a
31 community service obligation, so there was no subsidisation
32 from any other valleys. I might ask Geoff to comment on
33 Robert's question on \$100m for Wyangala and whether that's
34 a reasonable cost estimate.

35
36 MR BORNEMAN: Actually, Robert, I was slightly
37 conservative. The estimate currently is 120 to 160, but
38 the bottom line is that what I was trying to emphasise in
39 my presentation is that we are not a long way down the
40 investigation phase here. We have some ideas of the
41 alternatives, but by no means do we have all the
42 alternatives locked in. We are proposing to proceed to
43 look at the alternatives, whether those initial estimates
44 are realistic figures, whether there are ways of staging
45 and reducing risk at much lower values. We are very much
46 in the initial stages of investigation
47

1 MR IMMARAJ: I wasn't quite clear with your question
2 regarding the fixed and variable ratios. I didn't catch
3 whether you are pro increasing the fixed or supporting the
4 increased variable, but certainly State Water's position is
5 we want to try and comply with the operating licence
6 requirement to move to a higher variable charge. We are
7 certainly pursuing the requirement of the operating
8 licence.
9
10 John Bruce raised the question with regard to high
11 security and general security. We have not taken into
12 account the potential impacts on what might happen with
13 groundwater usage as a result of high security. We didn't
14 have enough information on pumping costs from rivers versus
15 pumping from groundwater, for example, so we acknowledge
16 there is lack of analysis in that area. If its potential
17 is to cause further degradation of the groundwater
18 resources, then we certainly need to review that.
19
20 MR BRUCE: One thing I didn't mention, it sort of followed
21 on from the situation where conjunctive licences were
22 changed to normal licences. In the conjunctive licence
23 situation you were encouraged to draw from the river in wet
24 times and vice versa in dry times, but without the
25 conjunctive thing, and if you increase the proportion of
26 charges for high security, it will encourage irrigators to
27 draw more from groundwater than from the river, which is
28 not effective, I imagine
29
30 MR IMMARAJ: We will try and analyse a little more on that
31 and provide the information to IPART as soon as we can. I
32 think we have addressed Doug's question with regard to
33 whether we looked at any options for internal or external
34 risk management. Certainly the issue of reducing our
35 operating expenditure in drought years has been looked at.
36 We analysed what happens in a reasonably dry year but not a
37 drought year.
38
39 In a reasonably dry year when there is a potential for
40 varying the discharge from the dams, we do take the
41 opportunity to doing opportunistic maintenance on
42 structures that are normally submerged. So in the last few
43 years we've done a lot of remedial work on, say, Split Rock
44 where we noticed slab movement. That slab had not been
45 exposed for nearly 10 years, so in dry years we do kick up
46 our maintenance and remedial work to try to take advantage
47 of that, without having to build coffer dams, so it's a

1 good time to be doing that work. There is a bit of a
2 counterargument in terms of reducing your costs in dry
3 years.
4
5 However, in really bad drought years we have found
6 that, when you have to keep providing basic rights and
7 riparian flows, we cannot often shut down the valves, so
8 valve maintenance becomes extremely difficult to undertake
9 in a drought situation because the valves are running
10 continuously, so there's a very short window of opportunity
11 to do some of that work. The most obvious risk mitigation
12 strategy when your income is down is to reduce your costs.
13 It does have some difficulties.
14
15 MR BORNEMAN: One of the exercises we did in the Lachlan -
16 it's the only valley that's in a new drought record - was
17 that with vacant positions, we analysed whether they were
18 necessary, given the drought conditions, or whether it was
19 possible to not refill them at that time. In the Lachlan
20 and the Macquarie in the drought period there were a number
21 of positions that we didn't fill or only partly filled, or
22 outsourced part of the provision by contract. So there was
23 action taken to try to minimise our costs during that time.
24 I explained before, in terms of efficiency of the customer
25 service officers and the offices, while that is a
26 longer-term strategy, it was initiated through that drought
27 period in terms of looking at reducing costs, although I do
28 support Abel's comments fully, that some things are more
29 difficult and require greater resourcing during a drought
30 than during normal operations
31
32 MR IMMARAJ: Michael Egan asked a couple of questions, one
33 in the presentation and one during question time. The
34 first was a question with regard to separating the costs of
35 operating a flood mitigation zone. It is not an annual
36 event. Therefore, we haven't provided those costs in the
37 submission. We have included those costs in the flood
38 operations costs in our submission.
39
40 Whether it is efficient to identify those costs is
41 another issue. Whether it is a pro rata of total
42 operations and a percentage of time that we operated in
43 flood mitigation, and so on, so we will examine that, but
44 so far we haven't thought it was efficient to be going into
45 that level of detail to ascertain costs.
46
47 The second question raised was whether in low water

1 years as a result of the State Water submission we get
2 large bills. I think I'm making some assumptions. I have
3 to say no because the more we move towards variable cost
4 recovery the low water years will result in lower bills
5 than we currently have. So that is one issue.

6
7 I think I might have actually missed one question from
8 Mary in the very beginning which related to the increase
9 from the full cost recovery levels. The CSCs have been
10 provided with information on the increase in the operating
11 costs in the Lachlan. There are two particular reasons
12 that are highlighted - one is in the cost of hydrometric
13 services in the Lachlan and, secondly, in the area of dam
14 safety surveillance.

15
16 Once the flood safety compliance issue has been
17 identified as a major structure, then the immediate
18 response is to increase the surveillance of that structure
19 under the dam safety guidelines, so there has been an
20 increase in the surveillance costs for bulk structures.

21
22 In our submission we have removed the operating
23 subsidy currently received from the government. Therefore,
24 there are increases in the cost recovery for the users as
25 against what was previously determined as full cost
26 recovery. I will ask Russell to answer one more question.

27
28 MR SIMONS: Just to pick on a subject that was a fairly
29 hot topic yesterday in response to a comment that Dennis
30 made, Dennis you seemed to say that there was a lack of
31 clarity in the level of discounts that are provided to
32 Jemalong. In fact, State Water would agree with that
33 comment, which is why we have proposed to get rid of the
34 discounts and to have a fee for service on any services
35 provided by Jemalong to State Water so that there is
36 clarity and there is transparency in the costs transferring
37 between businesses.

38
39 MR IMMARAJ: We only have two more points to go,
40 Mr Chairman. Lyn Davies raised a question with regard to
41 whether we have looked at how other utility businesses
42 manage their risk revenue. We have spoken to Country
43 Energy very early in the piece with regard to how they
44 manage their revenue of risks. Country Energy has
45 a postage stamp at a state level of their costs and
46 Telstra, I believe, is postage stamped nationally, whereas
47 State Water's requirement is to make sure that the costs

1 and the revenues are identified at a valley level, so we
2 don't have the advantage of being able to trade off overs
3 and unders across the state. So there is that issue.

4
5 The variability of revenue or usage of these services
6 is also fairly small, so both Country Energy and Telstra's
7 variability is nowhere near what we face. Even if you
8 look state wide, our average deliveries across the state,
9 if you use the water sharing plan limits, would be
10 5,500 gigalitres. We have been delivering around
11 3,000 gigalitres per year, so it is a considerable revenue
12 variation as a result of the 60 per cent revenue from
13 variable.

14
15 For both those utilities, I believe, their primary
16 means of managing risk is through their variable charge or
17 recovery through their variable charge. So the fact that
18 electricity has a 98 per cent variable and Telstra has
19 88 per cent - I'm using your figures - does mean that the
20 variable charges are adequate to cover their risk, but then
21 it is postage stamped across the country or the state.

22
23 I think the only other points related to Geoff's
24 comments on Dennis's questions.

25
26 MR BORNEMAN: Dennis made reference that in my
27 presentation I included Jemalong and that was a cost to
28 Jemalong. In this particular case, the automation was a
29 valley-based cost on Jemalong. The portion in the ratio
30 that was agreed for Jemalong Weir - the automation is a
31 controlled function for the regulation of the river, not
32 for correctly supplying the water to Jemalong irrigation.

33
34 The other comment is in line with that, that
35 State Water's proposal in terms of moving the weir and
36 moving that funding arrangement across the valley is just
37 to be consistent with the rest of the state.

38
39 THE CHAIRMAN: Thank you, Abel. I believe we have had a
40 very conscientious attempt to identify all the comments and
41 questions that have been raised during our hearing.
42 However, there is the possibility that inadvertently you
43 may have missed one or two. Whilst I am not reopening the
44 questions for further debate about the answers - some
45 people may not agree with the answers - if someone feels
46 that their question was completely overlooked, I'm giving
47 you the opportunity just to remind State Water.

1
2 MR CLEMENTS: You touched in part on my question, Abel,
3 but only a very small part of the question, so just to
4 repeat it: in terms of the original draft in State Water
5 of the submission to IPART on this determination, at any
6 point did treasury direct or help or assist or instruct on
7 any changes? Let's talk about the cost shares for
8 instance, but in any other area, and I think it is a
9 relevant question because treasury is the major shareholder
10 and a regulator of SOCs and this process today is
11 principally about regulating monopoly business.

12
13 THE CHAIRMAN: And the other question.

14
15 MR CALDWELL: This is to Geoff Borneman to clarify
16 something that I believe he either misunderstood me or was
17 misled. I was questioning the need for upgrading the
18 safety requirements on Wyangala Dam. I wasn't questioning
19 the cost. I mean, you're presuming that they're needed and
20 I'm saying maybe they are not needed.

21
22 THE CHAIRMAN: Abel?

23
24 MR IMMARAJ: I will take the first one and Geoff can take
25 the second one. John Clements' question with regard to
26 treasury's role and instructions to State Water. Certainly
27 we have been consulting with treasury on some of the key
28 principles in the submission. I have got to say, though,
29 that they didn't get a copy of the submission before it was
30 lodged with IPART, so there were some surprises in there
31 for them in a way - unpleasant surprises, if you like.

32
33 What were their instructions? A couple of things.
34 One was the range of the weighted average cost of capital
35 to use, so we were given 5.9 to to 7.7 as a range for state
36 owned corporations across New South Wales; that the
37 operating subsidy should be made absolutely clear, that
38 there is an operating subsidy from government to
39 State Water and that there should be some glide path to
40 removing that operating subsidy. So our submission is
41 structured along the lines of removing the operating
42 subsidy.

43
44 Certainly there was a discussion of the cost shares,
45 and I alluded to that earlier, that treasury wasn't
46 particularly keen on changing the cost shares for the
47 legacy and safety upgrades.

1
2 MR CLEMENTS: I'm not referring to the safety upgrades,
3 Abel, but the cost shares in general.

4
5 THE CHAIRMAN: I don't want to specifically talk about the
6 safety upgrades. We are all aware of that process; it is a
7 well-documented process and long standing, but in terms of
8 the cost shares in general, of which there are many, did
9 State Water have a viewpoint - that differed to treasury?
10 Did treasury direct or instruct in terms of --

11
12 MR IMMARAJ: No. As far as the other cost shares that
13 have been proposed in the submission, they are
14 State Water's views. Treasury had no preference one way or
15 another, so they neither told us what the cost shares they
16 wanted were nor did they direct us. But certainly the only
17 one that we talked about was dam safety, because they are
18 basically funding them so we had to go and speak to them
19 about the fact that these dam safety costs were going to be
20 included in our submission and that they were going to have
21 to pick up 100 per cent of those current dam safety upgrade
22 programs.

23
24 MR BORNEMAN: I think to a certain extent your question
25 has been answered, Robert, and I do apologise for
26 misinterpreting your comment, but it is a regulatory
27 requirement that has been funded 100 per cent by government
28 for the upgrades.

29
30 THE CHAIRMAN: Thank you for that. I would again like to
31 thank State Water for its participation in the hearings
32 today. I think it has probably helped the audience as well
33 as the tribunal. Thank you very much again.

1 RESPONSE FROM DEPARTMENT OF NATURAL RESOURCES

2
3 THE CHAIRMAN: I ask the Department of Natural Resources
4 to come forward and respond to the various comments that
5 have been made during the day and the issues that have been
6 raised.

7
8 MR O'NEILL: We would firstly like to thank the
9 stakeholders for their many and varied questions. We went
10 away and tried to categorise them into about half a dozen
11 questions to try and cover all your issues. We will try to
12 respond to them as best we can. Of course you are going to
13 get a second opportunity to ask us if you don't feel we
14 have.

15
16 We will just run through our interpretation of what
17 the questions were. There were a few questions on the
18 double dipping issue between State Water and DNR costs.
19 I will pass that over to Rick to answer that one.

20
21 MR RUNDLE: I think the issue of double dipping has come
22 up over the years, and now State Water Corporation has
23 separated from DNR and in fact is operating under its own
24 financial system, but certainly State Water Corporation has
25 been a separate entity in DNR's accounts. We can say
26 emphatically that there is no double dipping of costs, and
27 I suppose we would need to see examples, or be given an
28 example of an activity where it is felt that there is
29 double dipping, because I guess can we can confirm that
30 both organisations operate separately, just as two separate
31 government departments.

32
33 Just on the issue of costs, on the subject of WRM
34 costs, the way the forecast costs were developed was we
35 looked at activities for 06/07 and we based those
36 activities on rates in the current year - rates for
37 salaries and rates for other costs in the current year. We
38 didn't build in any salary increases or other price
39 increases.

40
41 Effectively, therefore, what we have come up with is
42 if you are approaching an efficient costing exercise from
43 an economic perspective, that's the way you would do it.
44 All you would do is inflate the costs by CPI. We have
45 developed those costs for 06/07, as I said, based on the
46 05/06 actual rates and the activities in 06/07 onwards, and
47 we have projected those forward.

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1
2 If you look at the future years going forward from
3 06/07 to 09/10, those four years, you will see there is not
4 much variation. They are basically expressed in quantum of
5 dollars. So, effectively, that is a good base as well as
6 efficient costs, having allowed salary increases.
7
8 The other thing about that is if you go back to the
9 last submission where we did actually put in original costs
10 in 2001, those were actually based on 99/2000 costs and
11 then we projected them forward. So between 1999/2000 and
12 2006/07, which is eight years, you would expect things to
13 change, and that is one of the issues that came up from one
14 of our speakers, that why should our costs change or our
15 cost structures change. Now, you would expect to do that
16 in eight years, and that is the start of the price path.
17 If you take it to the end of the price path, it is
18 12 years.

19
20 Things have changed. The organisation has changed.
21 Everything else has changed in the world. So you would
22 expect that situation to eventuate where you did have a
23 change in costs, and that is purely why we have gone around
24 to developing our costs for 06/07 onwards on our new
25 activities from that point in time based on, if you like,
26 the equivalent of a zero base.

27
28 MR O'NEILL: I would also like to call on Sheridan to make
29 some comment on one of the questions about CMAs and the
30 potential double dipping.

31
32 MS MAHER: It was just with respect to the monitoring
33 component, and all the natural resource condition
34 monitoring and the water sharing plan monitoring as far as
35 data collection and analysis goes is the responsibility of
36 the department and not the CMAs. That is just a point of
37 clarification.

38
39 MR O'NEILL: There were also a lot of questions about the
40 cost recovery ratio. Rick has just commented on some of
41 that. Without fully reiterating everything I said earlier
42 in my presentation, you have to recognise there are a
43 couple of levels of exclusion, first of all, as I
44 indicated.

45
46 The second main thing to talk about there is in the
47 old system of the impactor pays system there was a

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1 philosophical debate about who is the impactor. What we
2 wanted to try to do is get away from philosophical debates
3 and subjective debates and try to come up with a
4 non-subjective way of establishing a divide between
5 irrigators pay and environment pays. That is where we came
6 up with the minimum standard concept, which we assert is
7 the water sharing plans, and then our cost recovery ratios
8 follow on from that assumption.

9
10 Just as an addendum to that comment as well, I thought
11 it might be useful to indicate that there are new
12 activities, as we have been saying, that are 100 per cent
13 attributable to users. Just by way of example, in activity
14 group 7 there is a number of activities that are new
15 activities and are 100 per cent attributable, and the end
16 result of all the new activities in combination with the
17 user shares that we have stipulated is where we get to the
18 85 per cent figure.

19
20 I will pass over to Paul to add some comments to that.
21 He will also then move into talking about the absolute
22 increases in the water resource management activity costs.

23
24 MR WETTIN: The number of the 26 to 28 per cent extraction
25 in the Macquarie has been raised a number of times. I just
26 thought it was important to try to clarify another
27 perspective on that. That extraction figure is in fact
28 correct. The average annual flow in the Macquarie is in
29 the vicinity of 1400 to 1500 gegalitres per annum, and the
30 average extractions in the Macquarie are around about 395
31 gegalitres per annum. Effectively, that is water that
32 comes from Burrendong Dam. So there is around about
33 another 1,000 megalitres that comes from other sources.
34 Now, that is flood events, flows down the tributaries that
35 are unregulated, et cetera.

36
37 Now, those flows are largely unmanaged flows. One of
38 the reasons that we have water resource management is
39 because there are natural flows that have been controlled
40 and they have been extracted. That is actually the
41 fundamental driver as to why you require management of
42 that water. So I think that is an important principle to
43 understand.

44
45 There was an issue raised about the CSO that might
46 apply to the environment, and it is almost implied that the
47 additional 75 per cent should be applied to the

1 environment. Well, the bulk of that water comes free
2 through rain fall, flooding and run-off. The water that is
3 controlled in Burrendong dam was mentioned. 160,000
4 megalitres is the maximum total allocation that can be
5 stored in Burrendong dam. But of that - going back to
6 average annual figures - that converts into about 80,000
7 megalitres per year. If you compare that with the
8 roundabout 400,000 for extractive use, that is about
9 20 per cent of the regulation storage which is actually
10 used for environmental purposes.

11
12 I think it is important to recognise the distinction
13 between the water resource management costs incurred by
14 regulation and extraction versus effectively free services
15 provided by natural events - floods and tributary flows.

16
17 MR O'NEILL: The next category of questions, if you want
18 to call it that, relates to the criticism levelled at DNR
19 in terms of outputs versus activities. Now, clearly we
20 have used the terminology "activities" in our submission.
21 You could argue it is a matter of definition. Some of
22 these activities you could probably call outputs. That's
23 the first part of the response to that.

24
25 The second part of the response is we do recognise
26 that we could more explicitly list the outputs from these
27 activities. By way of example, activity group 6, which is
28 the water sharing plan group, the output from that is a
29 water sharing plan which has security of entitlements in
30 perpetuity and it has also security of water for the
31 environment.

32
33 As another example, activity 5, which is the water
34 modelling activity, and a specific output from that is our
35 river basin models that are in place around the state.
36 These have to be peer reviewed and signed off by the water
37 audit working group.

38
39 So I guess what I'm saying is we do acknowledge we
40 could more explicitly state what our outputs are for each
41 of those activities, and I would like to request that we
42 take it on notice to provide that sort of information to
43 you.

44
45 There were a couple of questions about reporting
46 arrangements for DNR. I think it is important to recognise
47 that we have a number of reporting requirements. I think

1 the best way to give you an indication of those is to just
2 go through a quick list of the organisations that we report
3 to. We report to the National Water Commission in terms of
4 our national water initiative implementation. Our reports
5 to the National Water Commission are effectively publicly
6 available. We also report to the MDBMC via the IAG in
7 terms of CAP auditing. We report to the water audit
8 working group which in turn reports to the MDBC, and that
9 is in terms of our water modelling performance. We report
10 to the NRC via the CMAs. This, of course, is also publicly
11 available information, and that is regarding our water
12 sharing plan implementation and performance.
13
14 There is a number of other reporting things that we do
15 that we are not actually obliged to do but we do do - for
16 example, attendance at CSCs and reporting to them. That is
17 not an obligation of ours, but we do do it.
18
19 There was a comment raised about industry provision of
20 services and it being potentially a lot cheaper than the
21 department. We support the concept in principle.
22 Certainly some of the monitoring proposed and the cost
23 savings for travel are definitely justified. We would like
24 to work through those proposals. Of course there is a
25 number of issues to resolve there, and one of them would be
26 to make sure we achieve metering standards in those
27 systems.
28
29 Another question was raised about the transparency of
30 our costs in the submission. There are two parts to the
31 response to this, I guess. The first part is that we are
32 meeting our obligations stipulated by IPART to cooperate
33 with PB Associates in their study. That is our first way
34 that we see we are meeting the transparency requirements.
35
36 The second way is it has been requested that we break
37 down our costs into valley-specific costs and
38 activity-specific costs. We are not against this in
39 principle, but we would have to take it on notice to decide
40 whether that information should be made publicly available.
41 So that decision will be made outside this forum.
42
43 I'm getting close to time, so the final one that
44 I have got on my list - I think I was going to actually
45 hand that over to Paul to talk about. There were a number
46 of comments made about passing on groundwater costs to
47 users in terms of the structural adjustment package.

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1 I think it has been answered already.
2
3 MR WETTIN: Thank you, Dennis.
4
5 MR O'NEILL: But, basically, the short answer is we do
6 have a groundwater structural adjustment package in place,
7 so the government is paying for that adjustment. We are
8 not passing the costs of that on to users.
9
10 That ends the list of the questions I have got written
11 here. Would anyone like to add anything to the bottom of
12 that?
13
14 MR RUNDLE: Just to clarify a couple of points with
15 respect to tariffs, the removal of security premiums was
16 raised earlier as was the issue of cost reflectivity.
17 That, in itself, is something which will improve cost
18 reflectivity from a WRM charging perspective.
19
20 On the activities profile, I'll just run through a
21 couple of points quickly. The profile was developed in
22 terms of a water resource management water cycle. We felt
23 it better matched what we do against our costs as opposed
24 to some products, and certainly better reflects the current
25 framework of WRM in DNR.
26
27 Rob has already talked about how it doesn't measure
28 outputs, and we have acknowledged that it doesn't directly
29 measure outputs, although they can be equated, but as a
30 costing tool it is the most pragmatic way we see forward.
31 Certainly if you have been involved in cost accounting and
32 ABC accounting you would sort of head down that direction.
33 But what it does do, which you can't do with a product
34 costing system or a service costing system, is it provides
35 a mechanism for measuring efficiency by activity, and that
36 is very hard with an output-based system.
37
38 It also provides a mechanism to improve productivity,
39 as you can drill down to the individual activities or work
40 units for those activities and sort of look at how you're
41 going and what activity levels you're at. You could not do
42 that with a product costing system because it would draw in
43 individual bits of costs, job costs, from a range of
44 sources throughout the organisation, and to try and sort of
45 then say, "Well, how are we going to improve on
46 productivity" is virtually impossible. I think it would be
47 virtually impossible with most output-based systems.

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1
2 Having said all that, it is still largely input based,
3 but it will be linked to outputs, and I think we have given
4 examples of that already. One of the most pragmatic ways
5 to do that is to link it to the business plans in various
6 work units throughout the organisation. Certainly we see
7 it as the most pragmatic way forward in measuring our
8 costs.
9
10 Just another thing on wholesale discounts which came
11 up: we weren't proposing a discount for provision of WRM
12 information off the water charge. We were proposing a
13 separate fee for service arrangement - entirely separate
14 from the water charge.
15
16 In terms of the price path, certainly DNR supports a
17 long-term price path for stability and, if nothing else, to give
18 DNR the space to develop the water resource management
19 business over the next few years. So we'd certainly be
20 supporting at least a four-year price path.
21
22 A question also came up about the unit costs. To
23 clarify, the costs we have created in the submissions are
24 total unit costs, they are not the user share unit costs.
25 I don't know if that question was sort of actually thinking
26 that those total costs were the user share of costs.
27
28 DNR doesn't make pricing submissions in the current
29 regime, at least, by submitting prices, we only submit
30 costs, and, therefore, because we do that we are not in a
31 position to do impact assessment or gross margin studies.
32
33 Service level agreements was another thing that was
34 mentioned. They are in draft form at the moment. We do
35 have a review under way now which is to finalise those
36 service level agreements as quickly as possible - within
37 the next two or three months, I understand.
38
39 Finally, externality pricing. That is an NWI
40 requirement. It is certainly not something that has been
41 imposed by DNR or the state government. A review is under
42 way to resolve what to do with regards to externality
43 prices for all states. That is under the National Water
44 Commission.
45
46 Of course, one of the difficulties with externality
47 prices is quantifying what the amounts of the cost would be

1 and then applying the prices. From the CSOs, with DNR, we
2 recognise the subsidy we get as sort of a quasi-CSO. DNR
3 is certainly not proposing that additional components of
4 its costs be included as a CSO. Any CSO would be in that
5 existing subsidy per se.
6
7 On reporting, the issue was raised that we are looking
8 at 85 per cent cost recovery and, therefore, we are not
9 actually reporting to customers. I guess that's a valid
10 point, but the current level of cost recovery is nowhere
11 near that. It's not near 65 per cent. It's notionally 65
12 per cent, but by the time you take the subsidy off it's
13 around 55 per cent, and then, by the time you take the
14 actual receipts collected, it's somewhat lower again - in
15 fact, substantially lower. In fact, we probably would be
16 in the order, if you like, of 40 per cent recovery of our
17 WRM costs. That's not to acknowledge that customers should
18 not be reported to.
19
20 I am just trying to make this point, merely that the
21 85 per cent is not actually there. Sure, if it's there in
22 the future, it will become a larger issue in terms of
23 reporting. As DNR develops a water business framework,
24 it's that sort of issue that will be looked at more
25 closely. I think that about covers it.
26
27 MR O'NEILL: I think that concludes DNR's response to the
28 questions.
29
30 THE CHAIRMAN: Thank you very much. If I can comment
31 on Greg's last comment, the proposal to get to that figure, I
32 don't know how good the information is there. I think you
33 recognise that you have an obligation to provide more
34 information.
35
36 Does anyone think their questions have not been
37 answered? I am not asking for debate on the answers, even
38 though I have just broken that rule myself.
39
40 MS WARD: There were two issues that I wasn't quite
41 comfortable with. I understood that IPART requires DNR to
42 move towards valley-based financial reporting in terms of
43 providing transparent information; in other words, for us
44 to be able move forward for our sake and from the
45 customers' point of view. Rob touched on the ability to
46 provide more information on output. The whole line that
47 you're running about service delivery, well you'd have to

1 demonstrate if it were done. I think it's fair enough for
2 us to expect you to demonstrate the output in service and
3 to know that the service levels are going to be finalised
4 and that there will be more rigorous costings with activity
5 based costing. That might work in business, but at the
6 same time you cannot say they are your costs, so I suppose
7 it gets back to financial reporting and providing the
8 detail of the actual products that predominantly are of
9 benefit to the water user, which is why we're attributing
10 the costs to them, and it's that that we need more
11 information on.

12
13 I think I have wrapped two questions up in that issue.

14 One is the value of financial reporting and the second is
15 providing more information. I understand you're serious in
16 meeting the minimum standard in the water sharing plan, but
17 we all know there are lots of beneficiaries to the water
18 sharing plan. I would need more information about how that
19 equates to water users being responsible.

20
21 THE CHAIRMAN: In asking if there are other questions, I
22 observe that that question is very close to debating
23 previous answers, so it is really a matter of whether a
24 question has not been answered.

25
26 MR MIELL: On a point of clarification on groundwater, I
27 want to make it clear on the subject of the allocation of
28 funding for groundwater that it is notionally a \$165m
29 program, but that it is shared three ways: irrigators, state,
30 and federal government. The two main ones put \$55m on the
31 table, and it is split into three components. Of that fund,
32 \$100m is to be allocated to structure, to be shared
33 depending on how the valuation basis works out. Of the
34 remaining amount, \$9m has been allocated to a community
35 development fund to go to small businesses who can
36 demonstrate some impact on the groundwater adjustment.
37 Then the remaining \$1m is for administration costs, some of
38 which goes to DNR, and there will be offsets in that
39 because the federal government is paying half of it. We
40 have to look at the whole process. One issue is the state
41 government's imposition of the 10 per cent discount rate
42 and the other is the federal government's insistence at the
43 moment that it is going to tax it as income, as a
44 reduction. So I wanted to make IPART is aware that it's
45 not fully-funded to 100 per cent of that program, because
46 it's certainly not the case.

47

1 THE CHAIRMAN: Thank you. Are there any questions that
2 were not properly answered? I will hand back to the DNR.

3
4 MR O'NEIL: Michelle, I just reiterate that DNR will
5 endeavour to provide some outputs attached to those
6 activities and give you details of how they benefit the
7 users.

8
9 THE CHAIRMAN: Thank you very much for your answers to
10 the various questions and your participation.

11
12 It remains for me to make a few concluding remarks. I
13 do so to give you some idea of where we go from here. In
14 doing that, I must say that we are not in a position to
15 reach decisions on matters of substance. That would be
16 quite improper and unfair. People are still to be heard
17 and we need to reflect on what we have heard.

18
19 It might help if I pick up on a few things we have
20 heard today and just give you some response to them.

21
22 Typically in a pricing determination two critical
23 ingredients are the opex and the capex, and there has been
24 quite vigorous discussion on that issue today.
25 Fundamentally, it would have been better if we had the
26 consultants' report - I think everybody would agree with
27 that. That is something we will depend on quite heavily in
28 coming to our judgments about what is the most efficient
29 and prudent level of opex and capex over the next few
30 years.

31
32 A second critical issue is whether we should proceed
33 on the basis of the annuity approach which has been the
34 approach used, or whether we should introduce a RAB
35 approach, and, indeed, if we introduce a RAB approach, what
36 is the appropriate level for RAB? I can't go very far in
37 terms of teasing that out at this stage. I just want to
38 make one point, that we are conscious of the distinct
39 possibility that the shift as proposed by State Water would
40 lead to a faster rate of cost increase in the future than
41 if the annuity approach is maintained, all other things
42 being equal - and I emphasise, all other things being
43 equal, because there are all sorts of variables and there
44 is some discretion to change variables in recognition of
45 that possibility. Because of that, we have to be very
46 conscious about that, but the critical issue we are
47 concerned with is the fairness of a change if a change is

1 made. I think that was contained in the question from my
2 colleague Jim Cox.
3
4 The rate of return on capital investment is, of
5 course, a critical issue. I don't wish to add to what has
6 been already said on that. Interestingly for me perhaps
7 the issues that have most emerged in our discussions here
8 today have been the issues of cost sharing and risk
9 sharing, or what I will call risk sharing or risk
10 apportionment. I think, Michelle, you practically
11 suggested to us that, if we got the cost sharing right, we
12 could probably get reasonable pricing. That indicates the
13 importance of cost sharing.
14
15 We certainly have been impressed by the points that
16 have been made today in terms of different users pay or
17 what are community service obligations and so on.
18
19 On risk sharing, which was also pressed heavily, in
20 effect State Water's customers share some of the risk. It
21 is inevitably a somewhat uncertain revenue stream when
22 selling bulk water. It is more uncertain than selling
23 telephone bills or electricity.
24
25 One thing that occurs to me is I'm not aware in a
26 competitive market of customers ever being asked to share
27 the risk. It would only be in a monopoly that you could do
28 that, and that does mean that there is some interest on our
29 part in exploring other ways that State Water can better
30 manage its risk, including managing financial risk. That
31 doesn't only mean sharing the risk, although that is
32 obviously one consideration.
33
34 Other issues that have been touched on include
35 discounts and the issue of fixed versus variable charges.
36 One of the issues there - because in a sense governments
37 have legislated I think to ensure that variable charges
38 rise - but one of the things we need to think about is the
39 implications of doing that. High security and general
40 security premiums in terms of price structure will be an
41 issue for us.
42
43 Last but not least in terms of the issues is the
44 impact on irrigators. In relation to that I should
45 mention, because I don't think it's come up so far, that we
46 have commissioned ABARE to do a consultancy study on the
47 implications of the cost and price changes on the

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1 irrigators. That will probably be available in about two
2 weeks. No doubt you will be interested in that. It will
3 be posted on our web site. If there is a need to respond,
4 the critical issue will be price changes, and, in that
5 context, the determination.
6
7 Finally, as I mentioned earlier, the next stage for
8 us, after we have finished our hearings and have our
9 consultancy reports, will be to try to reach a decision on
10 these various issues that have been identified, with a view
11 to releasing a draft report in the last week of March. We
12 will then be calling for written submissions in response to
13 that draft determination and, indeed, the consultants'
14 reports that accompany that.
15
16 We would expect to have another round of workshops
17 with stakeholders et cetera before finalising our final
18 report and our final pricing determination. Let me just
19 say, there is a deadline to the end of the process. The
20 determination has to take effect from 1 July 2006, so the
21 final determination has to be made in final form for it to
22 take effect from 1 July 2006.
23
24 The last thing I want to do is once again to thank all
25 for their participation today. It has been extremely
26 helpful for us to get a first-hand idea of what's important
27 to you. The manner of your questions and the tone of your
28 questions indicates to us the things that we need to watch
29 when we look at each of these issues, so today's session
30 will be extremely helpful to us from that point of view.
31
32 In fairness, one should acknowledge, and I have great
33 pleasure in acknowledging, the contribution of the two
34 authorities, State Water and DNR. We couldn't conduct this
35 process as well as I think we have without their
36 willingness to participate in this process. Thank you all
37 for your participation and I declare this meeting closed.
38
39 AT 3.45PM THE HEARING ADJOURNED ACCORDINGLY
40
41
42
43
44
45
46
47

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