

INDEPENDENT PRICING AND REGULATORY TRIBUNAL

**REVIEW OF PRICES FOR STATE WATER CORPORATION
FROM 1 JULY 2010**

Tribunal Members

**Mr James Cox, CEO and Acting Chairman
Ms Sibylle Krieger, Part-Time Member**

Members of the Secretariat

**Mr Richard Warner, Program Manager Water Pricing
Mr Adam Smith, Senior Analyst**

Held at IPART Offices, Level 8, 1 Market Street, Sydney

On Thursday, 3 December 2009, at 1.30pm .3/12/09 1

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1 WELCOME AND INTRODUCTION

2
3 THE ACTING CHAIRMAN: Good afternoon, ladies and
4 gentlemen. I think we might make a start. I would like to
5 begin by welcoming you to this public hearing, which is the
6 fourth in a series for us and for people like George Warne
7 and Lisa Welsh, who have been to every one of the public
8 hearings.

9
10 We are inquiring into maximum prices that the State
11 Water Corporation will be permitted to charge for bulk
12 water services in New South Wales for the period
13 commencing on 1 July 2010.

14
15 I would like, first of all, to introduce myself. I am
16 Jim Cox and I am acting chairman and chief executive
17 officer of the tribunal. I am joined on this review by my
18 fellow tribunal member, Ms Sybille Krieger, who is seated
19 to my left.

20
21 IPART last determined prices for State Water bulk
22 water services in 2006. That price determination covered a
23 four-year period and is due to expire on 30 June 2010.

24
25 As part of this investigation, the tribunal released
26 an issues paper in July 2009 which set out key aspects of
27 the review process. The issues paper outlined some of the
28 matters which the tribunal considers are important to this
29 review, the matters that its Act says it must take into
30 account in conducting an investigation and also a draft
31 timetable for the review. In the issues paper the tribunal
32 called for submissions from State Water, its customers and
33 other interested stakeholders.

34
35 The tribunal is grateful to those who have taken the
36 time and trouble to make a submission. A number of the
37 organisations that made submissions to the review will be
38 presenting their views to this hearing today. I note that
39 some of you have travelled some considerable distance to be
40 here and we are grateful for your interest and assistance.

41
42 All submissions received will be carefully considered
43 by the tribunal in developing its findings and
44 recommendations. The tribunal considers that is a most
45 important investigation.

46
47 At the last determination IPART determined a revenue

1 requirement for State Water of \$335m for the terms of the
2 price path. Of this total sum \$230m was expected to be
3 recovered from extractive user's tariffs. The balance was
4 to be effectively paid for by the state government on
5 behalf of the community. In its submission State Water
6 Corporation has argued that drought conditions have meant
7 that it has not been able to generate the revenue that was
8 forecast at the time of the 2006 determination and that a
9 continuation of this revenue situation will threaten its
10 longer term financial viability.

11
12 State Water suggested a range of matters that it would
13 like to see put into place to address the matter of climate
14 induced revenue volatility. These include changing the
15 manner in which future water supply availability is
16 estimated, changing the charging structure and adjusting
17 the allowed rate of return to reflect the increased risk.

18
19 We will be exploring these issues most fully over the
20 course of this review and I have no doubt they will be a
21 key feature of the presentations and discussions today.

22
23 State Water is forecasting an increase in operating
24 expenditure of almost 9 per cent in real terms over the
25 next four years. Much of this is due to what it terms
26 thematic expenditure items. We will be seeking to explore
27 the reasons for these additional costs today.

28
29 State Water is also forecasting a significant increase
30 in capital expenditure of some \$117m over the four years to
31 2009/2010 to \$342m over the four years to 2013/2014.

32
33 Compliance with pre-1997 dam safety requirements makes
34 up a significant proportion of this expenditure and this
35 expenditure will be met by the government if existing cost
36 shares are maintained. There is forecast, however,
37 significant capital expenditure planned on the renewal and
38 replacement of assets and upgrading and modernising water
39 delivery and operational aspects of State Water's business.

40
41 State Water is also proposing that a premium should be
42 introduced on high security entitlements to incorporate a
43 scarcity premium to reflect the value of water under
44 changing seasonal conditions. The scarcity premium would
45 change through time depending on the relative availability
46 of general security water.

47

1 State Water has proposed large price increases for
2 high security and general security entitlement holders as
3 well as a usage charge for the Hunter, North Coast and
4 South Coast valleys. These price increases are based on
5 State Water charging at full cost recovery level for these
6 valleys where previously prices were set at below full cost
7 recovery level.
8
9 For high security entitlement holders, we estimate
10 that for the Hunter Valley, State Water is proposing to
11 increase the entitlement charges by 31 percent over the
12 four years. For the South Coast valleys the increase would
13 be 336 per cent based on the State Water's proposal and
14 North Coast entitlement holders would also face substantial
15 increases under State Water's proposal.
16
17 General security entitlement projects are projected to
18 increase by 22 per cent in the Hunter Valley and by 193 per
19 cent in the South Coast. North Coast valley charge
20 increases would again be substantial based on a movement to
21 full cost recovery.
22
23 Water usage charges are projected to increase by
24 26 per cent in the Hunter, 214 per cent in the South Coast
25 and by a very large amount in the North Coast according to
26 State Water's proposal on the assumption that full cost
27 recovery to be achieved.
28
29 This hearing is a very important part of a broader
30 price review process. It provides an opportunity for the
31 tribunal to hear in a public forum from State Water and
32 other stakeholders and to question the propositions put
33 forward. The submissions made by State Water and by
34 stakeholders are available to the public through tribunal's
35 website.
36
37 Before we commence proceedings I would like to say a
38 few words about the process for this hearing. You have
39 available to you a timetable which indicates the order in
40 which the organisations will be presenting before the
41 tribunal. For each organisation appearing a presentation
42 time has been allowed and this is to be followed by a period
43 for questions by the tribunal.
44
45 Assisting the tribunal today are tribunal secretariat members
46 Richard Warner and Adam Smith. Richard Warner is
47 the program manager, water pricing, and Adam Smith is an

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1 acting senior analyst.
2
3 At the conclusion of the sessions I will make time
4 available for members of the public to express their views
5 and opinions on proposals that have put forward by State
6 Water and other stakeholders. State Water will then be
7 given an opportunity to respond to matters raised during
8 the day should it so wish.
9
10 The tribunal will consider all submissions received
11 and all that is said today when it makes its decisions on
12 bulk water prices for State Water. The tribunal plans to
13 release a draft report and draft determination for public
14 comment in March 2010, and interested parties will then
15 have a four to five-week period to make submissions for
16 consideration by the tribunal before it makes its final
17 decision. A final report and determination will be
18 released in June 2010.
19
20 I should point out that the proceedings are being
21 transcribed today to provide a record to help the tribunal
22 and the secretariat undertake their work - so a record is
23 being made. We ask people to introduce themselves and to
24 speak slowly and clearly for the benefit of the
25 transcribers.
26
27 We commence proceedings today with State Water and ask
28 the representatives from State Water to identify
29 themselves, state their names and positions for the record
30 and then to commence the presentation.
31
32 STATE WATER
33
34 MR WARNE: Thank you very much. My name is George
35 Warne from State Water Corporation. I have been the CEO of
36 State Water for two years. In that time I have got to
37 understand quite well some of the vagaries of the weather but
38 nothing quite to the extent that some of our customers along
39 the coast have endured.
40
41 What Lisa Welsh and I will try to do is talk about
42 some of the successes and otherwise that we have had during
43 the last few years. We will talk about the impact of
44 drought. Although I know it has been very, very dry on the
45 South Coast, it has been even worse, if that is possible,
46 in inland in New South Wales. We propose to talk about
47 financial viability, proposed changes to prices and how

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1 we might be able to manage the impact to customers.
2 Although can I say in the past, with regard to some of the
3 customers here today, managing the impact of price on
4 customers is extremely difficult if you take literally the
5 application of the prices we are proposing.
6
7 In terms of our business, IPART, after listening to
8 State Water at the last tribunal hearing, determined that
9 on average State Water would sell about 5.5 million
10 megalitres per year dominated by the Murray and
11 Murrumbidgee catchments. Our actual sales have been more
12 typically a quarter of that amount of water, which gives
13 you an idea of the sort of stress the organisation, and
14 particularly its customers, have been under. That graph,
15 as you can see, shows variances between 60 and 80 per cent,
16 which is very severe indeed.
17
18 When State Water was formed, it was predicted that the
19 worst possible year we would receive in future was
20 2.9 million megalitres with an average of 5.5 million. As
21 you can see there, in every one of those four years of the
22 determination, if this year doesn't get very wet very
23 quickly, there is going to be considerably less than the
24 predetermined minimum.
25
26 In terms of what the business has been trying to do
27 and what we're achieving: we were set a target by IPART to
28 reduce our expenditure by 20 per cent and we maybe were a
29 bit slow starting but State Water has certainly achieved
30 that target through reduction in our operating costs and
31 through a reconfiguration of business, which I'll talk
32 about in a little while. You can see that that culminated
33 in 2009/2010 where we are now actually heading slightly
34 below maybe 35.9 million in terms of our annual operating
35 expenditure as an organisation and that, I guess, is quite
36 a stellar achievement for the board and for the prior CEOs
37 at State Water.
38
39 The new organisational arrangements had three key
40 drivers. One was the shock of the IPART
41 determination: everyone said "My golly, how are we going to
42 do this?" Then some of the more positive people in the
43 organisation thought "Hang on, maybe we could be a more
44 efficient organisation. There might be a different way we
45 can go about our work and how we can come to work." Then
46 some of the very positive people in the organisation said
47 "If we do this properly, we could actually become a

1 business that is able to earn extra income and create a
2 platform for future growth."
3
4 State Water replaced its geographical structure with a
5 functional structure and some of you in the room today have
6 complained about the making of the organisational structure
7 and its impact on your communities and the availability of
8 people you can talk to who make sense about your catchment
9 or your river. I am not here to tell you that it is a
10 perfect structure or that a geographical structure wouldn't
11 work a lot better but it was an organisation that
12 desperately needed to change the structure that had been in
13 place since the turn of the last century. I think the
14 structure we have got today is a better one but, as I said,
15 I am not here to tell you it is the perfect structure.
16
17 It resulted in substantial and ongoing efficiency
18 improvements and sometimes I've got to say that was at the
19 extent of local knowledge.
20
21 In terms of the results, we now have a new common
22 operating system, operations and procedures. We're not
23 there yet on all of those things but the introduction of
24 iWAS, which some of you may be using, in the demonstration
25 of improved systems that State Water is beginning to
26 implement. We are sharing information and using business
27 systems across the organisation. Now we can literally ask
28 the operator in Goondiwindi on a Saturday night to go and
29 look at weir levels in the Murrumbidgee River some 600 or
30 700 miles away. It is a demonstration of an organisation
31 starting to get to grips with the fact that it has a
32 state-wide focus and we don't need to have everyone
33 everywhere all the time.
34
35 We are also trying to introduce systems where not only
36 are we accomplished at developing skills maybe in valve
37 repair or whatever that can be used across the state but we
38 are trying to bring in some of those very basic business
39 improvement systems that relate to data entry once, not
40 data entry nine times and then faxed to someone else to
41 make a mistake when they copy. We are also trying to
42 centralise data so we develop a bit of corporate memory and
43 so that someone in Leeton who is new to the office would
44 understand how the business works, what the history of the
45 river is and what the hydraulics are like.
46
47 We separated the groups of our business for better

1 accountability and that is really about driving business
2 performance within the subgroups of our business and we
3 have restructured the corporate group in the business.
4
5 There have obviously been investments in technology
6 and we have come some way and those of you that are on
7 customer service committees now, I think would enjoy the
8 benefit of quite significantly improved financial
9 accounting on a value basis but, more importantly, it is
10 not about telling the story we've done, it is about
11 providing financial advice to our managers so they can
12 alter the behaviour mid-season and start to improve the way
13 we perform as a business.
14
15 In terms of customer service, we are hanging a lot of
16 our hopes on iWAS, which is an Internet-based system. We
17 are not attempting to be all things to all people. At
18 Murray Irrigation, where I was before, I remember at one
19 stage we were providing a new Internet service: text alerts
20 to farmers, fax service to everyone going out to 950 farms,
21 an advertisement in three local papers every week and some
22 of our farmers still demanded we write to them. I just
23 think that in the future the Internet is going to be State
24 Water's primary tool of contact with our farming
25 communities. In the meantime we are committed to a quite
26 interactive call centre based in Dubbo but really we have
27 got to work out ways to give our customers what they need,
28 not necessarily what every customer wants, if we are to
29 achieve further efficiencies.
30
31 State Water has envisaged that we will be able to
32 achieve a further 6 per cent efficiency over the four-year
33 period and as an operative business who has been through a
34 massive change, I think that is a realistic target for us
35 to strike at and those savings come really now not so much
36 from the operatives in the field or the dam operator in
37 your valley, but more likely to be in the ranks of our
38 management team and through savings in our IT and other
39 systems.
40
41 Turning to the capital expenditure program. It is
42 been patchy and as you can see we've overachieved, we've
43 overachieved, we've overachieved and a lot of it really
44 swings on this year's performance. On Tuesday this week we
45 completed a review of where we think we will end the year
46 and the current estimates are we will finish just over
47 \$117m, which is very close to target. So I think there has

1 been a terrific ramping up of the projects and very
2 interesting once the works actually start on the ground how
3 the contractors drive the business, not the other way
4 around. Once we get through the planning phase, once we
5 get through the tender phase, once a company like McMahons
6 or Leightons actually start work on site, they start
7 pushing you rather than the other way around.
8
9 In terms of the drought, I spoke earlier about the
10 inflow of the projections and here we have the financial
11 results of those inflow projections and notionally we were
12 to collect \$195m over the four-year period. It now appears
13 very likely we are going to receive more like \$112m and if
14 you deduct the explicit government cross-subsidy to
15 State Water, that means our revenue collection has been of
16 the order of \$56m less than was projected.
17
18 A lot of farmers have indicated that they reckon
19 that's about right. They'd say "Oh, well, you've had it
20 pretty tough, we've had it pretty tough. It's meant that
21 you as a business haven't been able to give many or in some
22 years any of your projected dividends to government but you
23 have managed to always break even or to keep breathing, so
24 it is not a bad result", and that may be true but I think
25 as a property provider with billions of dollars worth of
26 infrastructure tied up, it is a very poor contribution to
27 the shareholders who constructed the infrastructure.
28
29 This graph just highlights the severity of this
30 drought and I guess emphasised the point I made earlier
31 that the earlier projections are where the State Water's
32 sales of water would never fall below 2,900 gigalitres and
33 you can see here where we have been in the last few years.
34 And for those of you who are somewhat sceptical about
35 climate change or about land use affecting water
36 availability, I would ask you to take some care in thinking
37 about this and I guess just remember what we have been
38 through.
39
40 Having said all of that, that is the whole of
41 State Water and obviously impacts are patchy and some of
42 the client systems on the coast are so fickle and so
43 different - I heard the other day that the farmers near
44 Ulladulla have suffered five floods and a drought and that
45 is only in this year.
46
47 Look at it in context - and I am not asking you to

1 have enormous empathy for the poor blokes who are at the
2 other side of the divide but they are an important part of
3 our business - for the farmers in the Lachlan Valley who
4 are critical of State Water's planning and understanding of
5 water availability, this graph, particularly the blue line
6 at the bottom, just demonstrates that in the nine-year
7 period here, compared with the four other worst nine-year
8 periods ever recorded in the Lachlan Valley, they have got
9 less than half the water inflows. There's been not much
10 change up there. The land was cleared in the 1870s, the
11 dams were constructed and this modelled inflow just shows
12 you what it had running into that catchment during that
13 period and shows just how severe the drought has been.

14
15 In terms of our financial viability, the drought
16 conditions have exposed us to financial stress and they
17 have confirmed a credit rating deterioration. That is
18 quite an important issue for State Water because in terms
19 of the competition policy, we are assessed as an
20 independent trading organisation and they'd say, "If that
21 was a private business, what sort of credit rating would it
22 carry?" Lots of farmers have said to us "Well, so you
23 should, It has been a terrible drought for us too" but
24 unlike most of our farming community, with very significant
25 investments in assets to distribute water and farm
26 businesses, we haven't enjoyed the capital growth in any of
27 our farmland or any of our water entitlements that has been
28 very common during this period for other asset holders. We
29 have been unable to meet our obligations under the pricing
30 principles of full cost recovery and we've certainly been
31 unable to achieve any sort of rate of return on the very
32 significant investment by our shareholders.

33
34 We have an increased forward capital program adding to
35 our financial vulnerability and State Water has taken a bit
36 bite of that and just saying, really, it is driven by the
37 dam safety committee and we recognise it is a huge amount
38 of money and as an organisation we have got some
39 responsibility to make real efforts about making sure that
40 we are delivering value for money in that program.

41
42 In terms of our capacity, our forecast capital
43 expenditure: in 2009/2010 this is looking forward the next
44 four years. The dark blue is the investment on behalf of
45 government. The lighter blue or the lighter purple is the
46 investment on behalf of irrigators and you can see that the
47 lion's share of capex over the next few years is going to

1 be spent by State Water, with money we borrow on behalf of
2 the state government.

3
4 The proposed prices we've got are driven by the gap
5 between current prices and full cost recovery, increase in
6 the weighted average cost of capital, which reflects our
7 financial vulnerability and also reflects a lower gearing,
8 which is more in synch with an organisation like ours with
9 volatile income. It reflects the consumption forecasts.
10 As a farming community if you say: what are the key drivers
11 in your pricing? In the large part of New South Wales,
12 although less so on the coast, consumption forecasting is a
13 key driver in pricing. We have also taken a realistic and
14 very hard look at our long lived urban concrete and steel
15 assets and there are some reduced asset lines there which
16 have contributed to an increased depreciation charge. We
17 believe we can offset a lot of that by improving our
18 operating efficiencies and we have a responsibility to do
19 so.

20
21 In terms of the water price, I think you can probably
22 just sit in there in shock when you look at these but you
23 have to understand State Water's charter is to talk about
24 what is the full cost recovery of water. And Lisa will
25 talk in some detail in a minute about why State Water
26 believes that we are applying all those principles of
27 efficiency and cost saving right across the State and the
28 people in the North Coast and South Coast are equally
29 benefitting from that, as everyone else in the State,
30 although, by golly, when you look at that chart you would
31 wonder how.

32
33 In the Hunter, which is a valley that is at full cost
34 recovery; is that right, Lisa?

35
36 MS WELSH: Yes.

37
38 MR WARNE: You can see a reflected change in prices and I
39 guess here it is probably worth stopping for a minute to
40 talk about the proportional changes and we are proposing a
41 slightly higher increase in higher security or to the
42 general security and I think it just reflects our
43 understanding in droughts of the huge benefit of high
44 security and its massively increased value and the fact
45 that in terms of, if you like, a matrix of cost recovery
46 analysis and understanding of scarcity and, if you like, a
47 fairness factor, there is a very good reason why high

1 security users should pay a little bit more.
2
3 In terms of managing the impact on customers, it was
4 previously legislated and it no longer is, that irrigators
5 should pay 60 per cent of the average cost of water as a
6 user based charge and 40 per cent as a fixed charge and in
7 our consultation and discussions with irrigation
8 communities that seemed to be a very important part of our
9 pricing principles.
10
11 In terms of conversion factors: in the majority of the
12 state out west water sharing plans have been suspended and
13 we would argue the conversion factors that were used to
14 convert general security to high security and vice versa
15 are not valid today, they have been suspended for so long
16 and such doubt exists about future likely average inflows
17 in the streams, that they are no longer appropriate to use
18 when looking at pricing factors. In addition, in terms of
19 our pricing proposals, we are including the 6 per cent of
20 that sufficiency reduction.
21
22 I will now hand over to Lisa, who will talk about some
23 of the details in our submission.
24
25 MS WELSH: What I wanted to do today was talk in a little
26 bit more detail about the thinking behind our pricing
27 submission, so I am going to cover a little bit on what we
28 are hoping to achieve with this determination. I would
29 like to go through a little bit of detail of this lengthy
30 consultation we undertook with our customers. I would like
31 to provide some more detail on our forecast opex and capex
32 and also touch on a little bit of the value-specific opex
33 achievements in the past. I won't bore you to death with
34 the woes of the financial viability but I will provide you
35 with a little bit more detail, just so that you can
36 probably understand what is behind our proposed increase in
37 the way that we've come to capital.
38
39 I wanted to then explain how those factors have
40 influenced our proposed tariff design and in particular
41 some of the proposed increases in our submission for the
42 coastal valleys and even touch on a few of the other issues
43 in our submission.
44
45 In going into this pricing submission our objective as
46 a state corporation was clear: as George has outlined, we
47 currently have under-recovered about \$56m dollars of the

1 user share of our revenue requirements. The one and only
2 thing keeping our business financially viable today is the
3 government's share, the fact that it has fully paid
4 100 per cent of its allocation of our revenue requirement
5 under the 2006 determination but what we need to do going
6 forward is ensure that we can be financially viable and the
7 current under-recovery of user share revenue says to us
8 there is something fundamentally wrong with the current
9 tariff design.
10

11 Having said that, though, we are not ignorant of the
12 fact that if we have gone through a hard time, so have our
13 customers. We want to be financially viable but we also
14 want customers who are financially viable. We have tried
15 to accommodate the customer preferences for tariff design
16 as much as possible, and I think you will see as we go
17 through that that is reflected in our pricing structure.
18

19 As many of you in the room would be aware, we did
20 undertake some substantial customer consultation going into
21 this determination. It was undertaken in three stages and
22 deliberately focused at our customer service committees,
23 our valley based committees. We also met several times
24 with the Irrigators Council.
25

26 The first stage of the consultation was to outline the
27 IPART process, let our customers know it was coming up and
28 that we wanted to engage with them. In particular at that
29 stage, we wanted to talk to them about discretionary
30 services. So in State Water's new organisational structure
31 we are providing just a baseline level of service that is
32 required by our legislative and regulatory obligations.
33

34 We wanted to talk to our customers about whether there
35 were any services over and above that level that they would
36 be interested in purchasing from us and that we were not
37 simply assuming that our customers wanted something and
38 therefore they wanted to pay for it.
39

40 The second round of consultation involved us outlining
41 the key issues and what we were thinking particularly in
42 terms of consumption forecasting, which is one of the more
43 contentious changes that we have proposed in this current
44 submission. We wanted to make sure that our customers
45 fully understood the reasons behind that and what we were
46 proposing going forward. It was also an opportunity to
47 provide them with some more information on the types of

1 discretionary services that they were looking for.
2
3 The final round of consultation involved us showing
4 some proposed prices and in particular a pricing model that
5 showed how those prices were generated and the assumptions
6 behind those. What we were hoping for there was complete
7 transparency for our customers.

8
9 We also provided draft opex and capex budgets to all
10 our CSCs, and that was a really important part of the
11 process in being able to show our customers what our costs
12 were but that we also wanted their feedback: "You guys are
13 on the ground, if we've got it wrong, we want you to have
14 the opportunity to tell us and provide a bit of a sanity
15 check." I have to say that that proved to be quite a
16 useful part of the process. That was also an opportunity
17 to finalise the discretionary services which hopefully
18 Arthur Burns will tell you a bit more about today.

19
20 Just looking forward, as George said we are
21 forecasting an increase in our operating expenditure. Our
22 approach in developing our budget was to say we know that
23 today we have achieved the IPART efficient opex for
24 2009/2010. Having said that, we think there is a little
25 more we can do. We can continue to improve the systems.
26 We can capitalise on the new structure. Once that is
27 consolidated, we think there are some management savings
28 there to be made and some ongoing systems improvements.

29
30 We have built in some efficiencies of around about
31 6 per cent going forward. However, having said that, there
32 are ongoing cost pressures coming from outside State
33 Water's business and we have therefore included some
34 additional thematic expenditure. That's not my term,
35 but --

36
37 UNKNOWN: Whose is it if it's not yours.

38
39 MS WELSH: It's not mine; however, it is about additional
40 expenditure. We are saying it will cost more to run our
41 business going forward. We obviously have an obligation to
42 minimise that cost and continue to challenge those new
43 regulatory obligations and we certainly think we have done
44 that, but there are increasing cost pressures on State
45 Water and, as a result, we are saying that it will cost us
46 about \$2.5m more to run our business in the next four
47 years.

1
2 Some of that thematic expenditure obviously has
3 garnered quite a lot of interest in our customers, as we
4 would fully expect. IPART has shown quite a lot of
5 interest. We think that it is really important that we
6 don't just continue to increase our expenditure. So what
7 we are saying is that there are some clear pressures, I
8 won't go into detail of all of those but some of the
9 largest areas of expenditure involve environmental
10 obligations. For example, as a part of our dam safety
11 upgrade program, we will be having to install a number of
12 fish passages across the state. We can incorporate any
13 learnings into the design of new fish passages, and we also
14 have to maintain those assets. That is a very real cost
15 driver for our business. As well on those thematic
16 expenditures, a very small part of our cost driver is the
17 discretionary expenditure that was endorsed by our CSCs.
18
19 On the discretionary expenditure, there was actually
20 not an awful lot for the coastal valleys. However across
21 the state there was quite a lot of interest in some gauging
22 stations for some of the longer systems and in particular
23 in the Hunter, after quite an extensive negotiation process
24 with the customers at that CSC, that has resulted in them
25 endorsing some seven day a week operations but not starting
26 until 2012/2013.

27
28 This graph actually shows some of the total operating
29 expenditure in each of the three coastal valleys over the
30 four-year period for the current determination and then
31 also forecasting forward. I notice that in some of the
32 stakeholder submissions there was some concern shown
33 about the level of expenditure that State Water was
34 forecasting. I want to take a moment to clarify what was in
35 our submission. As you can see the two green lines relate to
36 the axis on the left. You can see in the first year there
37 is a clear trend for all valleys trending down to
38 2009/2010 and it virtually flat lines for the North Coast
39 and the South Coast valleys because there is very little
40 additional expenditure proposed in those valleys. I think
41 we all understand that the cost pressures in those valleys
42 really need to be challenged given the ability to recover
43 costs in those valleys.

44
45 You can see in that slide that the Hunter is a much
46 bigger valley with three dams and you can see the impact of
47 the thematic expenditure in those valleys.

1
2 Just going forward, our total capital program as
3 George said, is forecast to increase significantly over
4 this regulatory period. We are forecasting a total capital
5 program of around about \$342m. That is dominated by a
6 quite sizeable dam safety upgrade program which is at the
7 moment 100 per cent funded by the New South Wales
8 government. Associated with that, however, is quite a lot
9 of expenditure on environmental compliance for both cold
10 water pollution and fish passages, so that really dominates
11 State Water's capital program. There is also a renewals
12 program as well as some investments in water delivery.
13 That is about improving systems we use to run our rivers
14 and the telemetry which ties in with generating some of
15 those efficiency improvements that we talked about earlier.

16
17 To show you what this looks like on a valley basis,
18 you can see that is the North Coast. There is a bit of a
19 spike in the first year but very modest amounts of capital
20 expenditure proposed. Similarly in the Hunter, there is a
21 little bit more there, but trending downwards. In the
22 South Coast again there is a fall. The details of that
23 obviously are in our submissions.

24
25 I wanted to touch briefly on cost shares. During the
26 consultation, it was quite evident that our customers were
27 passionately interested in cost shares and that there are
28 many and varied views. State Water takes the view that
29 this is an area where there is quite a lot of grey; there
30 is no clear right and wrong in determining cost shares. We
31 believe that the principles themselves need to be
32 challenged regularly. I think that is what we understood
33 from our customers, and it is also something we observed in
34 putting together our price submission. When we compared
35 the relative amounts that government and users were being
36 asked to contribute over the next four years, we found a
37 huge increase in the government share, compared with the
38 user share. We think that in itself merits IPART going
39 back and revisiting the principles of cost shares just to
40 make sure that they still are, I guess fulfilling the
41 original intention.

42
43 Not to labour this point, but State Water does have
44 some substantial concerns about its financial viability
45 going forward. As George said, consumption over the
46 determination period was only 29 per cent of the levels
47 forecast by IPART and due to our tariff design of 40/60

1 fixed to variable ratio, that led to an under-recovery of
2 the user share revenue by \$56m and that is endangering our
3 investment grade.

4
5 As a business we need to be financially viable, not
6 just to provide dividend streams to our revenues but so we
7 can continue to provide services to our customers and
8 continue to maintain our assets. What we are saying is
9 that the current tariff design really puts that in
10 jeopardy.

11
12 In terms of going forward and preparing for this
13 determination, the first and most obvious step to us was to
14 look at consumption forecasting and work out whether we
15 could come up with something that was better than the
16 current methodology which, as we all know, is the 100-year
17 IQQM model. It was quite clear to us that that was broken.
18 It wasn't working, and we don't have the \$56m to prove it.

19
20 Earlier in the process, together with the now Office
21 of Water, we jointly commissioned the Centre for
22 International Economics to look at alternatives to the
23 IQQM. We suggested that they start with the CSIRO
24 sustainable yields. What we asked them to do was to come
25 up with a viable alternative to the IQQM that would only
26 allow us to recover our revenue requirements. We weren't
27 interested in going back and getting the \$56m that was
28 gone, but what we wanted to do, I guess, was to have a
29 greater certainty of being able to recover our revenues
30 going forward.

31
32 They suggested a rolling 15-year average, which limits
33 price volatility for irrigators in the short term. It also
34 self corrects. We are saying we don't understand fully
35 what is going to happen with climate change, and we are not
36 climate change scientists ourselves. We think that the
37 15-year period represents a balance between the structural
38 break that we have seen occurring over the last seven
39 years, so it includes some of the dry years but it also
40 includes some of the wetter years, and importantly it will
41 keep correcting over a 15-year period rather than having to
42 wait 100 years for whatever fundamental shift is currently
43 occurring in climate and therefore water availability.

44
45 So what does this look like for consumption
46 forecasting? Across the state we are saying that we think,
47 over this determination period, on average water

1 availability and therefore extraction will be around about
2 20 per cent less than the current IQQM model. That has led
3 to some substantial changes on a valley basis up to 30 per
4 cent reduction for some of the currently terribly drought
5 stricken valleys.
6
7 The changes are actually a little less extreme in the
8 coastal valleys, and that certainly echoes what we have
9 seen over the current drought, although there is a not
10 insignificant reduction in the North Coast. Interestingly,
11 the Hunter is the one and only valley which will result in
12 a slight increase in expected consumption forecasting.
13
14 This slide shows a comparison as to how much would we
15 have actually under-recovered had we been applying what is
16 our proposed average. That first pie chart shows that we
17 under-recovered 29 per cent. Had we applied the 15-year
18 rolling average, we still would have under-recovered but
19 only by 64 per cent compared with the 71 per cent. We are
20 not planning for the current drought that we have seen over
21 the current determination to repeat itself, because if that
22 were to be the case, then we will all have much greater
23 concerns than State Water's financial viability, but what
24 we are saying is that we think this is a reasonable
25 approach going forward. We are not hoping to
26 under-recover; we just want to break even.
27
28 That was our first step, which was to get the right
29 consumption forecasting. The second step was to say,
30 "Let's look at the risk of revenue volatility to this
31 business and let's look at how we are currently compensated
32 for that and is that appropriate?" When we compared our
33 level of cost recovery with the metropolitan water business
34 we found that we were under-recovering substantially
35 compared with those businesses. They had a much more
36 stable revenue stream.
37
38 Our current weighted average cost of capital was
39 actually chosen in line with the metropolitan businesses
40 because we are a water business they are a water business
41 they must be similar, so we have been given their weighted
42 average cost of capital. However, what we have seen is
43 that we are a fundamentally more risky business. We have
44 more revenue volatility. As a result of that exposure, we
45 cannot be as highly geared as they can be and retain an
46 investment grade rating. We need to reduce our gearing,
47 our level of financial risk, if you like. We are saying

1 that change in the gearing assumptions will result in an
2 increase in the weighted average cost of capital to 7.9 per
3 cent. A WACC of 7.9 per cent, our modelling indicates will
4 allow us to retain the investment grade rating which is
5 required under the treasury commercial policy framework.
6
7 Importantly for customers, it also allows us to
8 maintain a substantial share of our revenues as usage based
9 charges. That is what we understood from our customers was
10 something that was really important to them.
11
12 As George has mentioned our operating licence, unlike
13 the last determination, no longer requires us to keep the
14 60/40 variable to fixed ratio, but we have heard our
15 customers. That message from customers was universal, that
16 that was something that they really valued it and it was a
17 natural hedge for them in times of drought. Obviously in
18 developing our tariff model going forward, that was
19 something that heavily influenced our chosen tariff design.
20
21 However, what we are saying is that if IPART is unable
22 to support a high WACC, then we believe we should be able
23 to directly reduce our revenue volatility to the same
24 degree that a metropolitan business has, and that would
25 imply a 10 per cent fixed water pricing, but I should state
26 that that is definitely not our preferred position.
27
28 One of the other things we have noticed over the
29 current regulatory period is that the high security users
30 have been receiving, as is expected, full or near to full
31 allocations, whereas in many valleys our general security
32 users have received very little and in some cases zero
33 water. Yet the way the current tariff design works, in
34 some valleys our general security users are actually paying
35 for most of the costs of running our business. We think
36 that is an inequity that should be addressed in the current
37 pricing determination. There are any number of ways to do
38 this; this is not a perfect science.
39
40 We examined a lot of those alternatives. We asked our
41 stakeholders if they could come up with some suggestions,
42 but this is quite a divisive issue, as you might imagine.
43 So what we have come up with is a methodology which will
44 allow high security users to pay more in times when their
45 water is more valuable and the resource is scarce; but
46 similarly when the water is more available and the value of
47 their entitlements is not as high relative to a general

1 security user, they should pay less.
2
3 To show what this looks like, we came up with a
4 formula that retains the current conversion factor under
5 the water sharing plan, which is what the current basis for
6 the high security premium is, but we have modified it by
7 the inverse of the average general security allocation. As
8 I said, the application of that formula means that high
9 security premium will rise in a dry year and it should fall
10 in a wet year. It also continues to pick up on the
11 information in the water sharing plan, but I have to say
12 that this is an area which is highly contentious and we are
13 absolutely open to alternative views on this one. In
14 particular, although it is an inequity and we think it
15 should be addressed, it does not make any difference to the
16 overall level for cost recovery for State Water so it is a
17 zero sum gain for us.
18
19 What does all of that mean for prices? This is a
20 slide that George showed you before. It means some fairly
21 staggeringly large increases for both the North Coast and
22 the South Coast. Not to labour this point, we all
23 understand that those valleys have high costs relative to
24 the volumes of water and the users downstream. That is
25 certainly something that we think IPART needs to seriously
26 consider; it needs to consider the ability to pay of those
27 customers. I think that is an issue that we will hear a
28 lot more on a bit later this afternoon. In the Hunter,
29 those price increases are a lot less marked because they
30 are at full cost recovery.
31
32 This graph actually shows a model bill for a general
33 security user who holds 100 megalitres of entitlement. It
34 assumes the average consumption over the last 15 years.
35 The blue that you see there is the current water prices.
36 That is how much they would pay with today's IPART prices.
37 The next bar there in the maroon is actually what their
38 bill would have been had prices been at full cost recovery
39 and had they not been subsidised by the New South Wales
40 government. Then the pale yellow is actually what their
41 bill would be today with the prices proposed for 2010/2011
42 under the State Water submission. What we are saying is
43 that while the prices we are showing look scary compared to
44 today, they are largely a result of the gap between full
45 cost recovery and water charges as opposed to underlying
46 increases in State Water's cost base.
47

1 In the South Coast we would otherwise be proposing a
2 reduction in those charges had those prices been at full
3 cost recovery.
4
5 I wish to refer to a couple of other issues that we
6 included in our price submission. We are not proposing any
7 change to the maximum fee for temporary trades. IPART
8 capped that in normal terms at \$150 in the last
9 determination and we are proposing to retain that, which
10 translates to an additional real reduction of 10 per cent
11 over the four-year period. We have been able to achieve
12 substantial efficiencies in how we process trades including
13 centralising the administration of those trades in our
14 Deniliquin office, and we think we can generate some
15 additional efficiencies down there as well.
16
17 We are also proposing a new information charge.
18 This is something that is new. It is quite standard for
19 water businesses; in fact it is quite standard for all
20 utilities. We are saying that we don't want to charge our
21 customers for reasonable information requests, that is a
22 cost of running our business. If you are not our customer
23 and we are running around gathering quite large amounts of
24 information, there is no benefit to us. We think therefore
25 that you should be sharing in the costs of running our
26 business and we will be seeking to apply that charge. In
27 addition, if you are our customer, we think you have a
28 responsibility to maintain your records accurately and to
29 keep the information that we send to you. So if you are
30 asking for something that's over two years old we think
31 that charge should also apply.
32
33 Finally we are also including a metering service
34 charge as a result of the regulated metering project which
35 is proposed in the Murray Darling Basin. At this stage
36 that project has not been approved so this is an
37 in-principle metering service charge. I also note that at
38 this stage that project does not apply to the coastal
39 valleys Murray Darling Basin. I will finish there. Thank
40 you very much for your time.
41
42 THE ACTING CHAIRMAN: We will now proceed to
43 questions, I will hand over to Richard and Adam in just a
44 moment, but I would like to ask a question for clarification. If
45 we look at what you have said to us this afternoon, it is clear
46 that reduced consumption is not so much of an issue here.
47 If we look at a valley like the Hunter, which is just on

1 close full cost recovery, yet it is still getting a 20 to
2 30 per cent price increase, can you give me a sense of what
3 is driving the price increase in that case?
4
5 MS WELSH: There are a couple of other factors. Obviously
6 the increase in the weighted average cost of capital is
7 certainly driving an increase, as well as the revised
8 depreciation expense to do with the reduction in our asset
9 lives, and there's also the impact of the estimated
10 expenditure.
11
12 MR WARNER: In proposing substantial price increases to
13 achieve full cost recovery, and I would suggest that it is
14 probably not in anybody's interest to put all users out of
15 business and leave stranded assets in some of these
16 valleys. Is it really feasible to achieve full cost
17 recovery in these valleys or do we look at some other
18 approach?
19
20 MR WARNE: I think your question is not fair because I
21 think that when you look at the price increases and you
22 look at the other two valleys, not the Hunter, and you look
23 at the efforts that have made to contain costs, you can see
24 we are asking for the same amount of money pretty much as
25 we did last time but we are fully cognisant that these
26 farmers are competing in national and international
27 markets.
28
29 We are cognisant of the fact that up until about the
30 1990s there was no thought that smaller areas with very
31 expensive infrastructure would pay some of the ordinary
32 premium, but at the same time I think we have to recognise
33 the very high value of these very keen farming businesses,
34 and somewhere between lies the answer. But in terms of our
35 charter and our responsibility to come to you today with
36 responsible costs, I do not think it is for us to say that
37 there should be an explicit subsidy by government and we
38 are actually forbidden to provide an cross-subsidy within
39 our business, even though it might be a relatively simple
40 thing to do go, given the very, very small amounts of water
41 are sold relative to the rest of State Water.
42
43 MR WARNER: You provided us with operating costs in
44 some of the information you have given us. What I don't
45 think we have is direct costs - a split between those operating
46 costs between direct and indirect or direct and overheads.
47 I take it you can provide us with that?

1
2 MS WELSH: Yes, absolutely.
3
4 MR WARNER: Do you know offhand what proportion of
5 costs in these valleys are direct costs?
6
7 MS WELSH: Actually, no, I don't, I'm sorry.
8
9 MR WARNER: Now, I understand you use EFTs to allocate
10 overheads; is that correct?
11
12 MS WELSH: That's correct. We use direct EFTs in the
13 valley to allocate overheads; that's correct.
14
15 MR WARNER: Have you looked at any alternative ways of
16 allocating overheads?
17
18 MR WARNE: We could do it per average megalitres sold,
19 probably. That might be a credible way of offering
20 overheads. You realise you are just talking here about
21 cost distribution design.
22
23 MR WARNER: Yes.
24
25 MR WARNE: And I would argue there could be a more
26 equitable outcome but the actual costs of the overheads are
27 probably best related to the number of EFTs driven to
28 achieve the service because employees do represent actually
29 a majority of our costs in operating costs.
30
31 MR WARNER: How many employees have you got up at the
32 North Coast, do you know?
33
34 MR WARNE: Some of the sites have gone from five down to
35 two and down south they have gone from two down to one,
36 so we are talking about very small numbers of people.
37
38 MR WARNER: Given that a number of these valleys aren't
39 achieving full cost recovery and haven't achieved in the
40 past and that substantial price increases would be required
41 to get there, how does State Water make its expenditure
42 decisions and, more specifically, do you undertake costs
43 benefit analysis of incremental additional expenditures?
44
45 MR WARNE: I think we have a couple of drivers and, as you
46 know, occupational health and safety, safety of our
47 infrastructure and that commitment to providing farmers

1 with the service that they need as opposed to, I guess,
2 what they want. But you're right, we probably would be
3 less likely to be gold plating a service where we are
4 losing a lot of money.

5
6 MS WELSH: I would also like to note that when you saw the
7 table there of the discretionary services there are none
8 proposed for the North Coast and South Coast, for obvious
9 reasons.

10
11 MR WARNER: The NSW Irrigators council has submitted
12 that full cost recovery should not be pursued in the North
13 Coast, South Coast and the Peel Valley because, in its
14 words, the price increases are unsustainable. I guess this
15 is very similar to that first question which you objected
16 to: do you believe that the New South Wales Government
17 should be continuing to provide operating subsidies to
18 those valleys?

19
20 MR WARNE: You are asking a question - I don't know if we
21 can add to the question but the only thing I would say is I
22 would take a long hard look at what is going on with regard
23 to the farm businesses because I think that if someone said
24 to me, "In 1996 you're going to see the value of irrigation
25 entitlements in the Murray Valley increase at 38 per cent
26 compound over the next 13 years", I would have said "You're
27 joking". If someone said to me, "You will see dairy
28 farmers prepared to buy water for \$250 a megalitre in an
29 open market just to water pasture to get it started", I
30 would have said "You're joking, they won't pay more than
31 10".

32
33 I think farmers' ability to use water has improved
34 dramatically because they have had to. The efficiency of
35 water use has improved dramatically and I think the
36 economics and the importance of water is a cornerstone and
37 IPART have got a responsibility to make sure that we are
38 doing everything that we can to provide the economic cost
39 of water and that farmers are paying their fair share.
40 Now, to what extent there is an explicit cross-subsidy in
41 there from the whole government I'm not sure but I think
42 somewhere between lies the answer.

43
44 MR SMITH: Thanks very much. My next question is similar
45 to the cost benefit question that Richard asked but focuses
46 more on cold water pollution. State Water is spending
47 significant amounts on cold water schemes at three sites

1 simultaneously. We recognise that some of this expenditure
2 may be required to meet environmental standards, however,
3 we note that there is a New South Wales cabinet-approved
4 state-wide strategy which states that State Water should
5 investigate and mitigate the impacts of cold water
6 pollution at high priority dams where it is technically and
7 economically feasible to do so. How does State Water
8 assesses the economic feasibility of its venture aimed at
9 addressing cold water pollution?

10
11 MR WARNE: Abatement of cold water pollution is a tricky
12 area. It is politically a pretty hostile view, actually
13 having been in the cabinet room in order to discuss this.
14 It is, however, part of our operating licence to address
15 cold water pollution and look at abatement programs and as
16 a reflection of that, we are actually now working on some
17 more cost-effective ways of addressing cold water
18 pollution.

19
20 For the benefit of people here today, the simplest
21 explanation is that the water that comes out of the bottom
22 of the dam is a lot colder than water that would have run
23 down the river naturally and, as a result, it leads to a
24 priority environment for introduced and exotic species,
25 often of European or North American heritage, and it leads
26 to a disadvantage to Australian native species and is
27 considered as a very important issue by a lot of
28 environmental and river health groups. So we can't ignore
29 it but we also recognise that some of the abatement
30 programs are very expensive.

31
32 Having said that, it is my understanding that none are
33 planned during this period in any of the coastal valleys
34 but there are three proposed to be reviewed and commenced
35 in the inland rivers and our three highest priority cold
36 water pollution sites. We could ignore it but I just don't
37 think it's going to go away and as a community of interest,
38 us, the water providers, and irrigators that use our water,
39 we have got to recognise the environment as a legitimate
40 user of our river and we have got to recognise that the
41 greater community has expectations of us to deliver some of
42 that environmental amenity. Addressing cold water
43 pollution is an important part of it.

44
45 MR SMITH: Thank you. Some stakeholders have also
46 argued that if State Water were run like private enterprise it
47 would contest more so the expenditures that environmental

1 and safety regulators require everyone to undertake. To
2 what extent does State Water negotiate with these
3 regulators on the level of expenditure on dam safety and
4 environmental works that they are required to undertake?
5

6 MR WARNE: I would actually disagree with that almost
7 completely, the assertion, and I just give you an example:
8 in a case where we are doing the safety works, which is by
9 far our largest approved - our largest dam safety program,
10 there is a requirement for a Heath Robinson-type
11 contraption on that dam as a fish elevator. The fish
12 elevator was estimated to cost about 40 per cent of the
13 cost of the works, being \$42m for a fish elevator, and we
14 approached Richard Sheldrake, the director general at the
15 Department of Agriculture at the time. He put us in charge
16 of his fishery experts and we sat down and tried to work
17 out a sensible solution.
18

19 As a result, as part of that three-day approval, we
20 have been given a concession to put fish ladders on three
21 downstream weirs which connects hundreds of kilometres of
22 river rather than the 15 or 20 kilometres of river that was
23 going to be connected by the fish lift. The cost is less
24 than a third of the cost of the fish lift and it is a
25 contraption that - these are methods that require much
26 lower maintenance. It is a very sensible trade-off that I
27 think State Water was able to negotiate, which would have
28 been extremely difficult for a private contractor in
29 similar circumstances to trade off. I just cite that as an
30 example of how we are trying to think smart about
31 addressing this issue of the environmental amenity rather
32 than taking a blind approach and saying, "It's okay,
33 someone else is paying". We realise we simply can't afford
34 to do that.
35

36 MR SMITH: Thank you. My next question is on customer
37 impacts. State Water, as you have noted in your
38 presentation, has proposed large price increases for some
39 valleys. Has State Water consulted with its customers on
40 the impact of these prices and their willingness to pay for
41 these changes, the increases in the charges?
42

43 MR WARNE: We have and they are not.
44

45 MR WARNER: Lisa, I think you said in your presentation
46 that State Water wants your customers to be financially
47 viable. How have you assessed the financial viability on

1 the coast and do you believe that the 1,000 per cent
2 increases on the North Coast and 200 per cent on the South
3 Coast that you're proposing are within the bounds of that
4 financial viability for customers?
5

6 MS WELSH: We actually undertook an ability to pay
7 consultancy as part of our submission to IPART and that
8 full report is actually attached. Unsurprisingly it
9 confirmed that the price increases which result from full
10 cost recovery in the Coastal valleys would not be
11 sustainable by those customers. However, it is quite clear
12 to us as a business that we are a state corporation, we are
13 not a social policy arm of government. It is not
14 appropriate for us to make a decision about the level of
15 operating subsidy that the government should or shouldn't
16 pay to subsidise water delivery in these valleys. So I
17 guess what we have put in our submission allows IPART to
18 fully identify the costs of running those valleys and we
19 look to you to guide us as to what is affordable to those
20 customers and consistent with the national water
21 initiative, to make transparent any subsidy.
22

23 MR COX: Thank you. Just one final question from me: I
24 think Lisa showed a chart in which there was a
25 discretionary project on the Hunter Valley. Either now or
26 later can you tell us what was the nature of that project
27 and what it might contribute towards price?
28

29 MS WELSH: Yes, I can tell you that and I also hope Arthur
30 will tell you in more detail about it. That project will
31 actually enable State Water to provide seven-day-a-week
32 operations in the valley. So when there is a supplementary
33 event - because the Hunter River, as I understand it, is
34 quite short, therefore it's really important that when
35 there is potentially going to be some additional water
36 downstream of the dam, that State Water is on the ground
37 and is able to announce that event, having received
38 approval from the office of water as soon as possible, so
39 that we can contact our customers and let them know that
40 there is available water in the system to take and that's
41 obviously a service that is extremely valuable to our
42 customers, particularly during the current drought and that
43 additional \$52,000, which is actually quite a modest
44 amount, I think that our customers agreed in the end, that
45 will allow us to do that.
46

47 MR COX: Thank you very much.

1
2 We now have a presentation from NSW Irrigators, so we
3 invite the representatives to come forward and introduce
4 themselves and proceed with your presentation.

5
6 NSW IRRIGATORS COUNCIL

7
8 MR GREGSON: Thank you very much for the opportunity to
9 address IPART again on this, the last hearing in the first
10 stage of this determination; we greatly appreciate it. We
11 don't propose today to reiterate what we have said to you
12 before. We don't propose to reiterate what was in our
13 written submission. We propose primarily to concentrate on
14 those issues that are relevant to coastal valleys, which I
15 understand is the point of this hearing. I should
16 introduce today with me is our policy analyst, Mark Moore.

17
18 NSW Irrigators Council, as you know, is the peak
19 body representing irrigators right across New South Wales,
20 not only in the Murray Darling Basin but on the coast as
21 well. We do that through a series of member groups who
22 take up seats on our council. In the coastal region we
23 actually have four member groups from the Bega, from the
24 Hunter Valley, from the Mid North Coast and from the
25 Richmond/Wilson catchment in the far north, so you can see
26 that we actually have quite a significant distribution of
27 membership on the coast and the inclusion of those groups
28 into our council means that we are able to provide you with
29 a reflective view state-wide of the wishes and indeed the
30 views of irrigators.

31
32 In light of some recent events, I would like to make
33 some comments in respect of the State Water Corporation and
34 our more general view on that corporation rather than
35 simply in terms of this determination.

36
37 I said to the tribunal in Griffith and we've said
38 during the course of our written submissions that
39 irrigators support State Water Corporation and I'd like to
40 reiterate that here. We think State Water Corporation is
41 an outstanding business, we think it has an outstanding
42 management team and it's delivered a very high level of
43 service for irrigators right across this state and we
44 sincerely hope that they have the opportunity to continue
45 delivering that excellent and high level of service.

46
47 We would suggest, in light of recent events, that

1 there is absolutely no need for fundamental change in the
2 way that the State Water Corporation exists or operates or
3 with whom it is aligned and, in particular, we cannot
4 currently see any benefit whatsoever in changing the
5 fundamental nature of the State Water Corporation. Whilst
6 we may have some argument with them in respect of the
7 current price determination, we have absolutely no argument
8 with their existence and can see no benefit in having
9 State Water Corporation not exist in its current role.

10
11 Can I also say the irrigators support the current
12 model of a split between fixed and variable charges; that
13 is, the 40/60 model. There has potentially been some
14 conjecture that irrigators don't support a fixed charge at
15 all. Not only is that not true, we recognise the necessity
16 for fixed charges. We recognise the necessity for
17 State Water to receive a form of revenue which they know
18 they can rely upon and we believe that the 40/60 model has
19 indeed met the objectives not only of State Water but also
20 of its customers.

21
22 Can I reiterate one thing that I did say to the
23 tribunal in Griffith and that is that we believe the status
24 quo, that is the current determination, the current model
25 for State Water, works for everybody. It works for
26 State Water and it also works for irrigators. That
27 includes not only the existence of the corporation but the
28 funding model of 40/60 and, indeed, the current consumption
29 forecasting model using IQQM.

30
31 With your indulgence, Mr Chairman, is it permissible
32 for me to ask two questions of IPART in this process?

33
34 MR COX: You can ask them but you may or may not get
35 answers.

36
37 MR GREGSON: My first question is pretty straightforward.
38 Can I ask: has the NSW Office of Water now lodged their
39 submission which they stated they would lodge on 1
40 December?

41
42 MR COX: Not to my knowledge but I expect they will in the
43 next day or so.

44
45 MR GREGSON: My second question then, given the process
46 that's been going on and the significant expense that's
47 been incurred in this determination process to date: has

1 IPART received any correspondence from the Minister for
2 Water or his department in respect of the proposed deferral
3 of this process?

4
5 MR COX: No.

6
7 MR GREGSON: Thank you. So I did get answers to both.
8 I might say they weren't the expected answers but be that
9 as it may.

10
11 Can I point out that there are several coastal groups
12 here today who will make their own submissions and can I
13 also point out that a number of other of the NSW Irrigators
14 Council members will make their own submissions. Can I
15 point out that our submission was in fact supported by all
16 of our members and that is 28 of them.

17
18 As you are well aware, the coastal systems which we
19 are speaking about today are very much discrete systems.
20 They're not part of the larger systems out to the west and
21 as a result they form something of a conundrum in the
22 pricing determination process that you have before you.
23 Except for the Hunter, it's pretty obvious that these
24 valleys are unable to meet the full cost recovery principle
25 and we would suggest that any increase in the costs that
26 they're required to pay beyond a profitable level for the
27 operators in those areas, result in a negative outcome for
28 everybody that's involved.

29
30 It's probably important to point out that the assets
31 that State Water run are not only for the benefit of the
32 irrigators in these particular valleys and if the
33 irrigators in those particular valleys were to disappear,
34 you'd not find that the need for the State Water services
35 would disappear. Indeed, they're obviously providing water
36 for stock for domestic purposes, for recreational purposes
37 and for the range of other uses that this water provides.
38 So to move to full cost recovery or to move beyond
39 profitability for irrigation operators is going to be a
40 negative result, not only for irrigation operators but for
41 everybody involved, not least of which the industries that
42 irrigators support and its individual valleys.

43
44 That said, we do recognise a necessity for everybody
45 to pay their fair share and to keep State Water as a viable
46 and operating entity. We recognise, and our coastal groups
47 all recognise, that they face increases in the same way

1 that increases are faced by every business operating
2 everywhere and in particular they recognise that they
3 should face increases at an equitable level of those that
4 are happening inland. The irrigators Council does not
5 support cross-subsidy.

6
7 We do not support a subsidy of the coastal valleys
8 being paid for by the inland valleys. We do, however, seek
9 the support of tribunal for a community service obligation
10 subsidy to limit increases in the prices that are paid by
11 the North and South Coast valleys. You'll notice in our
12 submission that we have sought a subsidy that would limit
13 increases to 5 per cent per annum on a compounding basis.
14 I would like to point out that the increase we are seeking
15 is obviously above and beyond projected consumer price
16 index increases and as a result there's an implicit
17 recognition that prices will go up and that coastal
18 irrigators are prepared to pay their share of the costs
19 above and beyond what's happening at the moment.

20
21 I would like to make just two quick comments in
22 respect of what State Water have said here today and
23 they're not necessarily limited to the coastal valleys. In
24 particular, I notice the issue of conversion factors and
25 the proposed increases in high security charges offset
26 against general security charges and the fact that Lisa
27 noted that this is a divisive and contentious issue. In
28 our submission it's not a divisive and contentious issue
29 and, indeed, in our written submission we suggested a way
30 of dealing with this process: that is, to look at the
31 variance between the two based on the cost variance between
32 the two; in other words, assess the costs and attribute
33 those costs against who's using it. I again point out that
34 we have 28 members across both general and high security
35 and that that proposition, to base it on costs, was
36 supported by our council.

37
38 In respect of cost shares, State Water suggested that
39 you should review the cost shares between users and
40 government on the basis that the current submission would
41 see prices, the quantum of contribution paid by one party,
42 increased to a level not matched by the other party and, as
43 a result, IPART should check to see if this meets the
44 original intentions.

45
46 In our submission, the original intentions were based
47 on percentages not quantum. There was an assessment made

1 of who was responsible for incurring the cost and, as a
2 result, who should pay it. As we said in both our written
3 submission and to you in Griffith, and I'd like to
4 reiterate it again now, we don't see that there has been
5 any fundamental change in the reasons. We ask what has
6 changed to suggest that there should be a reopening of the
7 cost sharing arrangements? Our submission says there has
8 not been any change and, as a result, there should not be a
9 reopening of it and you should rely on the in-depth
10 examination that you went through during the course of the
11 last determination and leave those cost shares in place.
12 With that, we are happy to take any questions you might
13 have.

14
15 MR WARNER: Thank you, Andrew. As you know, in our
16 other hearings we have addressed the issue or sought to
17 address the issue of State Water's financial viability. They
18 have put forward a number of propositions for dealing with
19 that including increasing the RAB and changing consumption
20 forecasts and those sorts of things. I think in your
21 submission you are opposed to all of those. What other
22 options do the Irrigators Council consider might be
23 suitable for addressing this issue of State Water's
24 continued financial liability?

25
26 MR GREGSON: With respect, I think that there is an
27 assumption underlying the question and indeed an
28 assumption underlying the State Water submission that there
29 is a major and significant problem in the long term. We have
30 no hesitation in saying that State Water has faced four pretty
31 trying years and indeed a bit longer than that in terms of
32 the drought it has faced. Its customers have faced exactly
33 the same problem, but the underlying assumption is that
34 that problem continues and, as a result, State Water as a
35 business is in some jeopardy.

36
37 As we said in Griffith, if the current conditions were
38 to continue, not only is State Water in a lot of trouble
39 but so is every single one of its customers. There is,
40 however, no evidence to suggest that what they and their
41 customers have endured in the last four years is the new
42 normal; in fact there is some scientific evidence to the
43 contrary of that. So rather than suggesting a method to
44 get around the current problem, I suppose our submission is
45 in fact questioning whether there is a problem. We have
46 questioned that based not only on the evidence that State
47 Water has provided but also based on their financial

1 performance to date. We have recognised that they have not
2 provided a return to their shareholders, but they are
3 certainly not alone in that situation. However, at the
4 same time at an operating level, they have managed to
5 achieve what so few others have managed to achieve in the
6 last four years - they have delivered a profit.

7
8 MR WARNER: I think you mentioned that your view is that
9 irrigators on the coast would be prepared to accept 5 per
10 cent real increase per annum and they would be able to
11 absorb that through time. As an extension of that
12 question, has the New South Wales Irrigators Council
13 conducted any additional analysis of irrigators willingness
14 to pay for price increases and what the impact of such
15 increases would be on members?

16
17 MR GREGSON: It might be an idea, in the context of that
18 question, to distinguish between willingness to pay and
19 ability to pay. Are they willing to pay more? Absolutely
20 not. Are they able to pay more? We actually had
21 something to say very briefly in our written submission in
22 respect of ability to pay.

23
24 You may recall that we said that that is, in our
25 opinion, not a relevant criteria because ability to pay is
26 not valley specific; it is individual business specific.
27 So it would come down to an assessment of every one of the
28 12,000 individual water access licence holders as to
29 whether they were able to pay; but to reiterate our written
30 submission, we don't see that is a relevant criteria.

31
32 MR SMITH: You said that full cost recovery in the North
33 Coast, South Coast and Peel Valley would be, as you put it,
34 unsustainable. You have also said that you support the New
35 South Wales government providing an operating subsidy or a
36 CSO to State Water to make up the difference. Could you
37 explain the rationale for providing a CSO and would you say
38 it is appropriate for the taxpayers to support these
39 valleys?

40
41 MR GREGSON: The answer to the second part of your
42 question is absolutely. The answer to the first part of
43 your question goes to what we reiterated a moment ago;
44 namely, that the services of State Water are vital not only
45 to irrigators but to a broad number of users within any
46 individual valley, be that for recreational uses, be that
47 for stock and domestic water and indeed in a number of

1 valleys for critical human needs - town water consumption.
2
3 If, through removal of the subsidy or seeking full
4 cost recovery from irrigators, you in fact make them
5 unviable, then you are effectively removing part of the
6 revenue base without removing the obligation on State Water
7 to continue its operations in those regions. Let me put it
8 to you this way: you should shut down irrigation in the
9 Bega Valley, but that would not stop the necessity to
10 continue operating the Brogo Dam or indeed the rivers there
11 that State Water is currently involved in. You still need
12 to ensure that Bermagui has drinking supply. You still
13 need to be able to supply a stock and domestic supply.
14
15 Not providing a community service obligation, not
16 providing a subsidy actually has a negative result on
17 government rather than a positive result. That sets aside
18 all of the obvious social benefits of providing employment
19 in the town, providing industry in the town and providing
20 the sorts of services that a town needs to continue to
21 exist.
22
23 So is it reasonable for taxpayers to cover that? Yes,
24 it is, and as a result, that is why we have suggested that
25 there should be a limitation by a subsidy to a level of
26 price increase. I note that that level of price increase
27 is not dissimilar to the price increases that are faced
28 elsewhere at 5 per cent compounding.
29
30 MR SMITH: Thank you. Some stakeholders have proposed a
31 state-based pricing scheme where all irrigators essentially
32 pay the same price for water. This has been a particularly
33 strong theme that came out of the Peel submissions. The
34 NSW Irrigators Council has said that it would support
35 cross-subsidies. What are your thoughts on this proposal?
36
37 MR GREGSON: I think we said we don't support
38 cross-subsidies.
39
40 MR SMITH: So you don't support uniform pricing?
41
42 MR GREGSON: No, we don't support cross-subsidies
43
44 MR SMITH: Well, what are your views on uniform pricing?
45
46 MR GREGSON: Uniform pricing would result in a
47 cross-subsidy; so, no, we would not support it.

1
2 MR SMITH: Thank you.
3
4 THE ACTING CHAIRMAN: Thank you very much for coming.
5
6 MR GREGSON: Thank you.
7
8 THE ACTING CHAIRMAN: We now have a presentation
9 from the Hunter Valley Water Users Association so we invite
10 you to come forward and make your presentation.
11
12 HUNTER VALLEY WATER USERS ASSOCIATION &
13 SW COASTAL VALLEYS CUSTOMER SERVICE COMMITTEE
14
15 MR BURNS: Thank you for the invitation to come along
16 today. My name is Arthur Burns. I chair the Hunter Valley
17 Water Users Association. I also chair the Customer Service
18 Committee for State Water for the whole of the coast of New
19 South Wales. I did in fact put in two submissions, very
20 similar, but because we now have present some
21 representatives from the South Coast and the North Coast,
22 most of what I cover will be just the Hunter.
23
24 To start with, this issue of the high costs to the
25 North Coast and South Coast is a critical issue. I will
26 cover that a bit further, but I know that my colleagues
27 will emphasise it further still. Unfortunately I don't
28 have a PowerPoint presentation for you today so I will
29 quickly run through some of the issues that are in the
30 submission and probably enlarge on some aspects. I am
31 quite happy to take questions on anything in the
32 submission.
33
34 One of the things I tried to do is to point out the
35 differences between the coastal irrigation areas and the
36 Murray Darling Basin, which is all we seem to hear about in
37 the news these days. We realise and accept that they are
38 having tremendous problems but we have our own as well.
39
40 The major differences include the relatively smaller
41 size of the irrigation enterprises. Even though they are
42 smaller they are just as critical to those people who use
43 them. It is an essential part of the farm businesses. It
44 is, in many cases, an essential part of the whole
45 district's businesses.
46
47 One of the major costs that we have is that most of

1 the coastal irrigation - I would say probably 99 per cent -
2 is through a pressurised system; it is not flood
3 irrigation. That incurs quite a lot of additional costs.
4 I note your recent decisions on electricity pricing and one
5 can imagine what that will do on top of the water.

6
7 THE ACTING CHAIRMAN: Recent but not yet implemented.

8
9 MR BURNS: We all know what it is. That has to be taken
10 into consideration as far as ability to pay.

11
12 One of the reasons that the costs in the coastal areas
13 are higher is because of the relatively small size of the
14 storages. The Hunter is not too bad in that case. We have
15 Glenbawn Dam and Glennies Creek Dam, which has a million
16 megalitre storage, but you come down to Toonumbar with
17 only 11,000 megalitres and Brogo with 9,000 megalitres.
18 Obviously there are still a lot of costs regardless of the
19 size of the dam, and that is one of the drivers for this.

20
21 The other thing that is happening on the coast is the
22 urbanisation and the industrial pressures creating demands
23 for water. Whether it be coal mines cracking streams and
24 taking water and not being charged, whether it be big
25 industries coming in, whether it be farms being subdivided,
26 where you had one riparian right you might get a
27 subdivision of 50, that is taking water away and again that
28 is not charged for.

29
30 That leads me into the user/government shares issue.
31 I have noted some of the replies already. When I spoke to
32 you, probably four or five years ago - I think that was the
33 last time - we did talk about this and the differences on
34 the coast. The example I have given in the submission,
35 which I hope has been looked at and I am sure it has been,
36 is that in the Hunter alone, some 21 per cent of the
37 storage in the dam or the annual allocation of the storage
38 in the dam is taken up by non-chargeable users. That is
39 just over 20 per cent. I can go through the exact details
40 of those, if you need me to later. It is not only the fact
41 that it is 20 per cent of the allocation or just in excess
42 of 20 per cent; it is in fact 40 per cent of the area in
43 the dam or more, because all of that water has priority,
44 and this brings us on to the general security/high security
45 stuff.

46
47 Under the water sharing plan for the Hunter regulated

1 river, when the allocations are worked out each year, at
2 least two years supply of those essential supplies is put
3 aside. So when you say it is 20 per cent of the allocation
4 it is actually 40 per cent. In our case, and it happened
5 in 2007, I think it was, we had 37 per cent capacity in the
6 dams. We got an 8 per cent allocation. The next year I
7 think it was down about 35 or 36. We got a zero
8 allocation. That again shows the percentage of the dam
9 that is put aside before general security irrigators can
10 get a look at it, and that comes back to the high security
11 issue too.

12
13 I don't have the exact figure in my head but the
14 percentage of allocations for the high security in the
15 Hunter is so much higher because of the power stations.
16 They use half as much water as all the irrigators combined,
17 and they use it each year. That is fine, but we think you
18 do need to look very carefully at the balance between high
19 security and general security entitlement charges to
20 reflect the major costs in the dams.

21
22 I am sure Lisa and George will agree that the major
23 cost for State Water is the maintenance and operation of
24 the dams, and we can charge it according to the percentage
25 of the bucket that is used. That is probably one way of
26 looking at it. Of course, the downside of going to that
27 completely is when there is no water for general security
28 use, they are still paying for their shares.

29
30 One issue that I have raised concerns the Hunter; it
31 is not so much for the coastal areas, but it has certainly
32 been discussed as a coastal valleys issue. We talk about
33 Toonumbar Dam on the North Coast and we talk about Brogo
34 in the South Coast. In the Hunter, we have Lostock Dam.
35 Lostock Dam, for some reason or other, is linked into the
36 Hunter charging. Lostock Dam is also a very small dam. In
37 fact what happens is the Hunter irrigators do subsidise the
38 cost of Lostock. Perhaps the users understand that. The
39 two regulated streams are not linked. At the end of the
40 regulated streams, yes, they are linked - the Paterson does
41 eventually run into Hunter but it is not in the regulated
42 section.

43
44 Whilst we would hate to think that the Lostock people
45 would be in the same position as Toonumbar and having to
46 pay hundreds of dollars a megalitre, we do think there is a
47 CSO for those areas. One way for that to be worked would

1 be to take the cost of the Paterson out of the Hunter which
2 would mean a reduction in the prices in the Hunter.
3
4 These are not my estimates, these are estimates that
5 have been given by senior people in State Water, but they
6 do not have a separate account. The subsidy that the
7 Hunter irrigators are paying for the Paterson irrigators is
8 about \$350,000 a year. I reiterate that we would sooner
9 pay that than to see them stranded but provided that can be
10 picked up as a CSO, we think that the government should do
11 that not the Hunter irrigators. That is the issue.
12

13 There is another cost factor that is very particular
14 to the Hunter and it relates to Macquarie Generation, which
15 is the biggest user of water. They also use Glenbawn Dam
16 for storage of water. They pump across from the Manning
17 Valley from the Barnard River. There are very strict
18 conditions involved in that. There are a lot of costs
19 involved in it, but there is no charge made to Macquarie
20 Generation - no money, to the best of my knowledge.
21

22 Maybe State Water can answer this better, but I have
23 been able to find no record whatever that any charge is
24 made to Macquarie Generation for the storage and releases
25 and accounting for that water in Glenbawn Dam. The
26 estimates I have had for that is another \$240,000 a year.
27 What I am virtually saying is if you put the \$350,000 from
28 Lostock and the \$240,000 for the Barnard water, we would
29 have a big cut in pricing, not a 30 per cent increase over
30 the four years and I would like those things to be looked
31 at.
32

33 We have some concerns about the accounting for
34 non-IPART revenue items by State Water. I have asked the
35 question a number of times. I must reiterate that as
36 chairman of the Coastal Valleys Customer Service Committee,
37 I have found that they are open with us, but there are
38 certain things you never seem to find out. There do appear
39 to be many occasions where there is income coming into
40 State Water which is not an IPART thing. We are not
41 comfortable as to whether some of the costs of providing
42 that are not being paid for by the irrigators. I could
43 probably give some examples. The costs of metering and
44 testing for water for salinity trading schemes should be
45 shared and we are not positive it is, but there are a few
46 issues. We think IPART should look into that for us.
47

1 With regard to State Water overhead costs, given
2 that has been raised already, it is my understanding that
3 the corporate costs are shared on a per person per employee
4 basis. I am sure that we would be a lot better off if it
5 was on a per megalitre basis. I don't know what the right
6 answer is to it all, but I would be very surprised, given
7 the hassles in the Murray Darling Basin, et cetera, that a
8 lot bigger proportion of the overheads, particularly the
9 corporate overheads, in State Water are not used in the
10 Murray Darling Basin at a higher rate than they are used in
11 the coastal areas, and I am talking per person. You must
12 to look at what is happening and it is fairly obvious where
13 the time is being spent.
14

15 I think I have already covered high security versus
16 general security. As to the discretionary charges, Richard
17 Warner asked Lisa about them. There was one issue that
18 came up there. It is a short flowing river. I would
19 point out that we went 20 years on 100 per cent allocation.
20 Then, all of a sudden, it went to 8 per cent overnight. We
21 only survived because if there was a storm, we got an SMS
22 that came through and said, "Yes we are declaring off
23 allocation on the water and you can hop in and use it."
24 That is the only reason there is still an industry there.
25

26 We agreed that was worth having. We did delay it for
27 the first two years because we know that the amount of
28 water in the dam at the moment will guarantee us 100 per
29 cent for the next two years. Particular section of the
30 plan doesn't come into operation straight away, and, yes,
31 it is worth it to us because it saved us.
32

33 However, we also note that the salinity trading
34 scheme, which is about half a million dollars a year income
35 to State Water and which is nothing to do with IPART, does
36 provide a similar service. It is a bit hard to understand
37 how it is another \$50,000 if that service is already there,
38 we need it, so we agreed it. We certainly still want it so
39 we are happy to pay it.
40

41 In summary, we note the increase proposed by State
42 Water. We note the arguments for the increased WACC, the
43 90/10. The 90/10 would suit us but we realise that those
44 who don't get water would not want to be paying a great
45 deal. We would also point out that we didn't have losses
46 in allocated predicted sales of water. We actually had
47 increases. We feel very much that under the new system

1 that is being put up, we are paying for what happens
2 somewhere else. Is that a subsidy? I don't know.
3 Certainly if everyone had been lucky enough as we were, it
4 probably would not have come up at all.
5
6 I must finish and I am sure my colleagues will come up
7 to speak in a minute. If there is no cross-subsidy or CSO,
8 no government obligation, to those two dams and the
9 Paterson - take the Paterson out because it has to be
10 included - you would get to the stage where there may be
11 one irrigator left up there who is paying the full cost of
12 the dam.
13
14 As Andrew Gregson so rightly says there are customers
15 apart there are non-identifiable customers that needed the
16 authorisation. What would you do if you had no-one there?
17 If everyone hands in their allocation, do you put a stick
18 of gelignite in the dam and blow it up or do you still pay
19 the same costs that are there now to maintain it? I'll
20 leave it at that and I am happy to answer your questions.
21
22 MR COX: Thank you. Can I just clarify one thing: do you
23 support, for the support in general terms, State Water's
24 proposal to rebalance general security and high security
25 charges?
26
27 MR BURNS: Yes, I do. I note Andrew's comments about
28 being pretty - not very open. I really and truly believe
29 that the high security should be charged on the basis of
30 costs. If 1 megalitre of high security has got to be put
31 aside for three years in the dam, it's using three times as
32 much storage space that a general security is and it should
33 be three times as high. That is sort of the sense, yes;
34 very much support that.
35
36 MR COX: Thank you. Richard?
37
38 MR WARNER: Thanks very much for that, Arthur. One of
39 the things you did say in your submission was that the
40 Hunter Valley Water Users Association didn't support the
41 move towards the 15-year average approaching that I think
42 State Water was advocating for estimating water
43 availability and it was I think also Lisa Welsh, in her
44 presentation, pointed out that the move to the 15-year
45 average would have very little effect on the Hunter or
46 Hunter users and I am just trying to figure out why you
47 have this objection to that 15-year average.

1
2 MR BURNS: I guess when I put that in it was the very fact
3 that we had had pretty standard sales and it really
4 shouldn't have affected and we didn't want to be involved
5 in the carry-on effects. The overall effects of the
6 15 per cent, as I can read it, is one of the major cost
7 drivers between the whole fairly high increases that
8 State Water is looking for in income. However, I take
9 advice on that.
10
11 MR WARNER: I think you also said in your submission that
12 your valley should also be near cost recovery and I think
13 State Water confirmed that and they really said that the
14 cost increases that you face have been driven by increase
15 costs and new investments. Are you satisfied with the
16 explanation you heard from State Water about those
17 increases?
18
19 MR BURNS: I think the point I was trying to make was
20 emphasising this Paterson/Lostock issue. The Hunter is
21 above cost recovery, I am quite sure of that and I wouldn't
22 mind if Lisa was to agree with me. If you take out that
23 \$700,000 that I mentioned, that is the Barnard water and
24 the Paterson, you take that off, you'll find that the
25 Hunter should be getting reductions.
26
27 MR WARNER: You've also said in your submission that you
28 believe that the cost estimates in State Water's submission
29 do not fully reflect the probable savings over the next
30 period. Would you like to explain those and how they
31 come --
32
33 MR BURNS: Yes. Certainly there's been fairly severe
34 staff reductions right across the whole of the coast,
35 including what we've heard about from Toonumbar, which I
36 am sure you're going to hear about from Bega in a minute.
37 Most of those changes have only applied in the last
38 12 months and they are still happening and I don't know
39 whether it's been long enough for those savings to be
40 factored right through in the submissions that we've got.
41 That's all.
42
43 MR WARNER: One of the other things we heard from
44 NSW Irrigators is that they would support a 5 per cent real
45 increase per year. Are you in favour of that? Do you
46 endorse that, accept that?
47

1 MR BURNS: We discussed this this morning, actually.
2 My submissions I think placed our position pretty clearly.
3 We believe one fair way of working out to what extent the
4 CSO should be - and I'd say that I understand that
5 State Water hasn't put it in that - they still need to
6 receive the money and it's got to be recognised. It's a
7 transparent CSO we're talking about and probably one fair
8 way of determining what is a fair level, bearing in mind
9 the relative sizes, is the actual true costs for the
10 Hunter - full cost recovery - for the Hunter once the
11 Paterson has been removed and hopefully once the
12 Barnard River stuff has been moved and that be set as the
13 upper limit. If the Hunter goes up, so does the others.
14 To my mind that would be a fairly sound way to approach it.

15
16 MR SMITH: You've mentioned that the measure for
17 apportioning State Water's overheads between valleys needs
18 to be examined. Why do you believe that alternative
19 approach to the current might be more efficient?
20

21 MR BURNS: I don't know if I am capable of completely
22 answering that. One way obviously is to charge per
23 megalitre. Unless you sit down and try and take every
24 second that George spends on different things and what
25 eventually that was, I guess it's hard, but I just have a
26 very strong feeling, I'm sure most of my colleagues do,
27 that there's a lot more time spent on chasing around with
28 the feds and the Murray Darlings stuff and all this and
29 what happens. The coast is just there sitting along. Sure
30 we get reasonably good service, it's been reduced a fair
31 bit lately, but I just think we are paying a fairly high
32 cost. That's all.
33

34 MR SMITH: Thank you. In your submission, and also you've
35 discussed this today, you have suggested that consideration
36 should be given to charging Macquarie Generation for water
37 storage release and accounting of Barnard reserve water -
38 sorry, accounting for water in the Glenbawn Dam. How
39 would you see this being implemented?
40

41 MR BURNS: From discussions I have had with some
42 State Water operatives, they estimate - the figure that I
43 had in the submission was \$240,000 - that part of the dam
44 that's used up and the costs of doing the releases and
45 doing the accounting and so forth is about \$240,000. I
46 have to rely on State Water to come up with a fair cost and
47 negotiate that with Macquarie Generation.

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1
2 MR SMITH: Thank you.
3
4 MR COX: Thank you very much.
5

6 MR BURNS: Thank you.
7

8 MR COX: Next we have the Bega Valley Water Users
9 Association and also Bega Cheese. I would invite their
10 representatives to come forward and introduce themselves.
11

12 BEGA VALLEY WATER USERS ASSOCIATION AND BEGA
13 CHEESE

14 MR PARBERY: Thank you, Mr Chairman, and members of
15 the tribunal. My name is Geoff Parbery, I am deputy
16 chairman of Bega Cheese. I joined the board in 1968 and we
17 had 67 employees and now we employ over 600 locally, 300 in
18 Tatura and 300 in Strathburn. I am also the local accountant
19 in a medium-sized tax practice doing about 3,500 returns and
20 we do probably half the supply base of Bega Cheese, so we
21 have quite a good knowledge of the dairy industry. Besides
22 that I also am involved managing the family property. The
23 family farm has been in the family 100 years, so again we
24 have quite a good knowledge of the effects of irrigation in
25 the area. Ken Garner is the development officer at Bega
26 Cheese and Geoff Johnson is president of the Bega
27 Irrigators.
28

29 A lot of the things that we want to go through have
30 been discussed but I think it is reasonable to summarise
31 them again. First of all through George again, last time I
32 saw him he was on the other side of the table, he is an
33 articulate and intelligent person and one probably couldn't
34 have a better CEO for State Water, so congratulations,
35 George. I've just got to get you on the same page as me
36 now, mate.
37

38 First of all, we are all aware that IPART needs to
39 balance the diverse needs and interests of the
40 stakeholders, that's just a fact of life, such as customers
41 needs and services to be affordable and of reasonable
42 quality that the communities need for prices that encourage
43 State Water development. That's a fact of life. We also
44 recognise IPART needs to ensure the long-term viability of
45 the agencies, which obviously are State Water. Whilst we
46 recognise full cost recovery is an important tenant of the
47 COAG water reform, we are all aware that provisions are

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1 made for the community service obligations to those regions
2 where full cost recovery would result in unacceptable
3 community outcome, and this certainly applies to the Bega
4 Valley Shire.

5
6 We are all aware that sub-economic dams, such as Brogo
7 can never receive full cost recovery, without full
8 recognition of community service obligation. In fact, it's
9 got the nickname "Beale's Bug", it's a 9,000 hectare dam.
10 I think some of the guys out west have probably got a
11 licence that's bigger than our whole dam but it's a very
12 effective dam for the running of Bega Cheese and its
13 farmers.

14
15 Any further attempt for full cost recovery without
16 substantial CSO recognition would not only cause
17 devastation amongst the irrigators, but also to the whole
18 region in the Bega Valley Shire. Brogo irrigators have
19 incurred substantial fee increases over the last several
20 years, which is now creating serious financial burden in
21 the operating of their dairy farm enterprises.

22
23 Irrigation's critical contribution to farming Bega
24 Valley Shire: Bega irrigation farms are 41 per cent more
25 productive than dry land farms. Their main growth has
26 historically come from the irrigation farms. 70 per cent
27 of our factory supply is from irrigated dairy farms.

28
29 As stated previously, any substantial water price
30 increase will not only cause massive problems for the
31 irrigators but this can flow through the whole region's
32 economy. Also, global warming cannot be ignored, which
33 would increase the reliance on irrigation.

34
35 Irrigators' impact, and this is very serious in our
36 area: we are noticing already a reluctance to expand and to
37 invest due to no cap on fees. Inefficient travelling
38 irrigators, dangerous bike shift irrigation, obsolete pivot
39 irrigators can now be replaced with more water efficient
40 and labour-saving alternatives.

41
42 Further, significant price increases will force
43 farmers to look for alternative feed sources, resulting in
44 less water being utilised, making it harder for the cost
45 recovery at Brogo Dam and this is a very, very important
46 point. Alternative feed sources could result in lower
47 production for farm prices, which ultimately will flow

1 through the production facility at Bega Cheese.

2
3 I have taken a real case study on an actual farm, a
4 successful farm on the Brogo. Just to demonstrate, we use
5 percentages all the time to show the real cost of what
6 happens to a farm in the rain. This is a farm with
7 1,369 megalitres and we have taken a 65 per cent
8 allocation. In 2005/2006 financial year, that includes the
9 commencement of the new IPART period, the fees on that farm
10 were \$15,000. For the 2009/2010, the year that we are now
11 finalising, those fees will go to \$30,000. This is an
12 increase over the four years of 100 per cent and actually
13 works out at \$33.70 per megalitre.

14
15 If we go full cost recovery, as George has put up in
16 his submission but has graciously acknowledged shouldn't
17 apply to us, 2010/2011 financial year - that's next year
18 after 2010 - that fee will go to \$96,000. Cost per
19 megalitre, \$180 per megalitre. The increase from the
20 2009/2010 year just finishing will be an increase to the
21 farmer of \$66,000, that's an increase of 220 per cent. The
22 percentage increase for the commencement of the IPART
23 period 2005/2006 will be 540 per cent.

24
25 As suggested by Bega, which was discussed, we were
26 recommending a 5 per cent compound over four years, which
27 is 21.6 per cent. By 2013/2014 the fee at that particular
28 farm will have risen to \$37,000. The percentage increase
29 from 2005/2006 when we commenced the period, which was
30 originally \$15,000 will go to 30,000, which is a
31 147 per cent increase, a massive increase. Even a
32 5 per cent compounded rate, a megalitre rate of 41.62 is
33 fast becoming totally unsustainable.

34
35 One of the most important things, of course, is the
36 potential impact on the community. Bega Cheese is the
37 major employer in Bega Valley Shire. Our dairy industry
38 employs approximately 920 people locally. The factory is
39 620 people. 300 people are employed by our farms. In
40 addition, many contractors are employed by Bega Cheese and
41 the local farmers. Our cheese and whey plant require
42 certain minimum milk supplied to remain commercially
43 viable. Our cut and pack plant for Bega Cheese requires
44 certain minimum cheese production to ensure the economic
45 running of the plant. Obviously if milk drops off, the
46 plants become inefficient. When the plants become
47 inefficient, as we are all aware of fixed costs, the price

1 of the milk will drop to the farmer, the price of milk
2 drops to the farmer, he then does what becomes sustainable,
3 then he puts off staff and Bega Cheese puts off staff.
4
5 Our dairy industry underpins the local economy and has
6 been growing and this has increased employment in the
7 shire. The industry contributes in excess of \$100m
8 annually, that's through wages to the factory and payment
9 to suppliers, with a huge multiplier effect through the
10 shire.
11
12 There is no other significant agricultural industry in
13 this region to replace dairy if it becomes unviable. There
14 is no other industry that can absorb these displaced jobs
15 if the dairy industry collapses. Lagoon Street factory
16 site (where Bega Cheese is manufactured) is totally
17 dependent on milk supply for viability. Bega Cheese
18 actually is an icon brand in Australia. I would hope most
19 of you would have Bega Cheese and not buy other ones and
20 we
21 are still number 1 brand in Australia, of which we are very
22 proud.
23 Lagoon Street Cheese manufacturing plant provides the
24 basis of the milk farmer income.
25
26 To conclude, and that was mentioned by George or Lisa,
27 State Water's own consultants have recognised the serious
28 effect that full cost recovery would have on South Coast
29 water users. However, they were not privy to the
30 multiplier effect reduced milk production will have on
31 suppliers, Bega Cheese and the local employment in Bega
32 Valley Shire. Hence their comments were very conservative.
33
34 IPART, in its September 2006 report, recognised our
35 needs as to greater certainty in regards to future pricing
36 and suggested future determinations should not seek to
37 fully recover all costs from the users in the North Coast,
38 South Coast, and Peel Valley, however, recognising future
39 tribunals cannot be bound by the 2006 determinations. They
40 were in my draft recommendation, Mr Chairman.
41
42 The 2006 tribunal also noted the loss of revenue from State
43 Water is relatively small. Whilst we recognise the increase
44 is inevitable, we believe the massive increases over the
45 last few years are now unsustainable and, if continued,
46 will have serious consequences on our farmers and the
47 whole community generally. The compound 5 per cent

1 resulting in the 21.6 per cent increase over the next four
2 years was suggested with trepidation, as when the megalitre
3 cost reaches 41.62 per megalitre, many producers will be
4 weighing up the alternatives for the future.
5

6 Thank you for giving me the opportunity to present
7 today.
8

9 MR COX: Thank you very much. As I understand what
10 you're suggesting, is that, if you like, the right balance
11 between social effects and cost recovery is 5 per cent
12 increase a year over the next determination period. Can
13 you tell us a bit more what led you to the view that
14 5 per cent was about the right balance?
15

16 MR PARBERY: The reason we suggested the 5 per cent -
17 frankly, we would have preferred a CPI - we acknowledge
18 George has his difficulties in running the dams. With the
19 drought in Australia at the moment, certainly over
20 New South Wales, Bega Valley has never, ever been in this
21 position before. We have no water on Brogo, none at all.
22 So we got through that event. Notwithstanding that, we are
23 trying to be realistic that there has to be some additional
24 cost recovery. By suggesting 5 per cent it's 5 per cent
25 off a very high base and we thought we were being realistic
26 but not being ridiculous, knowing our farmers will still
27 have difficulty with that percentage increase.
28

29 MR COX: Thank you. Richard.
30

31 MR WARNER: You've answered most of my questions; there
32 is
33 just one. I think you said that if we used 5 per cent
34 per annum compounding, you'd end up with a price of about
35 \$41 per megalitre in the Bega Valley. You would see that
36 as about the upper limit that prices could go, is that what
37 you're saying, before dairy farming becomes unprofitable?
38

39 MR PARBERY: When we're talking about water pricing here,
40 and I can give examples of this same particular property:
41 Power, last year, this property was \$60,000 and Mr Chairman
42 obviously indicated there's another ruling coming out on
43 Power, so it's a considerable cost. Because of the
44 uncertainty of this full cost recovery, we're having
45 massive problems, as I stated in my submission. Worn out
46 travellers should be replaced with proper, more efficient
47 use irrigation and there are massive OH&S problems.

1 We are getting very, very run down infrastructure
2 which our farmers are prepared to reinvest in, and that
3 would result in a better usage of water. But you reach a
4 limit and we believe at this limit it is becoming
5 unsustainable.
6
7 The other difficulty is - and IPART previously did
8 make a comment - they cannot commit further IPARTs. The
9 difficult part is while you don't have full cost recovery
10 in some form or other, it is really hard to put the money
11 involved in the systems you need. To put a good system on
12 this particular farm, you are probably talking half
13 a million dollars. That farmer is prepared to do that, and
14 George is not suggesting that because he has his own
15 commitments. If full cost recovery were to be applied to
16 that farm after it had made that sort of outlay, that
17 particular farm would probably be bankrupt and it would be
18 similar to the others on Brogo.
19
20 MR SMITH: Thank you. You said that you supported the
21 continuation of a transparent CSO payment from the New
22 South Wales government to support the South Coast region.
23 Do you believe that there should be an attempt over time to
24 move away from that?
25
26 MR PARBERY: Only if they want to put the average cost of
27 water over the whole of New South Wales, and I am not
28 saying that. I believe unfortunately that Brogo Dam - and
29 it has been recognised by IPART in the past - can never
30 have full cost recovery. We have some great fellows who
31 work on the dam. Those same fellows who handle the dam, a
32 9,000 megalitre dam, can probably do - who knows? There's
33 no limit because there is such a fixed cost of running it.
34 As a result of that, we have to look more towards the
35 community benefit.
36
37 Bega Cheese underwrites the Bega Valley Shire; there
38 are no ifs and buts on that. It is not practical to bring
39 in milk from Victoria. It is too far away. We are very
40 isolated. Yet that underwriting of the shire has put a lot
41 of employment and a lot of benefits back out through the
42 community. I think, because of the size of the dam, there
43 will always be a CSO. I cannot see how you can get full
44 cost recovery and still have an existing farming base.
45
46 MR SMITH: Thank you. Also in your submission you have
47 disputed some of State Water's cost claims. You have

1 requested that a review of these claims take place. Is
2 there any particular area that you would like to draw our
3 attention to or is it just a general observation?
4
5 MR PARBERY: No, it is a general observation. We have not
6 had the opportunity, and I am not sure if we are entitled
7 to; George will tell me. I would like to see the costings
8 and the budget costings on Brogo Dam and let our cost
9 accountants go through those - I am not sure if we are
10 allowed to do that, George - particularly fixed cost
11 allocation and depreciation claims.
12
13 I think that dam was built in the 1950s or something.
14 It has probably depreciated five times over. It has been
15 revalued again to the old debit and credit and you are
16 taking the depreciation off the bottom line again. It
17 would be a very interesting exercise. We are not
18 necessarily disputing it but it would be very interesting
19 to do that exercise.
20
21 MR SMITH: Thank you.
22
23 MS KRIEGER: Can I just ask a follow-up question to your
24 comment on the need for security farmers to invest in
25 better infrastructure. We are looking at a four-year price
26 determination. What is the investment horizon for the
27 farmers? What sort of length of security are you looking
28 at there in terms of pricing?
29
30 MR PARBERY: That is a very good question. For example,
31 in 2006, because of the uncertainty most people did
32 nothing. Probably an eight or 10-year security would let
33 you get a payback. We would all get the benefits of the
34 better efficiencies. You would get the better usage of the
35 water. We know what a valuable resource water is. At the
36 moment there is nothing worse than seeing a big travelling
37 irrigator in the corner of the paddock going round and
38 round because no-one has taken the time to turn off. There
39 are very good computerised systems that would utilise that
40 water much better. To do that and to avoid going bankrupt,
41 they need a payback over a 10-year period.
42
43 THE ACTING CHAIRMAN: I think you raise a very
44 interesting
45 point about the lack of certainty created by the absence of
46 full cost recovery. I think it is a good reason to strike
47 for full cost recovery wherever we can. That is a very
important point. Certainly we at the tribunal can do what

1 we think is reasonable for the next few years, but it is
2 very difficult for us to bind a future tribunal. That is
3 problem for everyone. Thank you very much. The next
4 presentation will be the Toonumbar Dam Water Users
5 Association. Could I ask their representatives to come
6 forward.
7

8 TOONUMBAR DAM WATER USERS ASSOCIATION

9
10 MS TONGE: Mr Chairman, ladies and gentlemen, My name
11 is Fleur Tonge. I am here representing the Toonumbar Dam
12 Water Users Association. The Toonumbar Dam Water Users
13 Association represents licensed water users supplied by
14 Toonumbar Dam on the regulated sections of Iron Pot and
15 Eden Creek. Our group was also represented by the Coastal
16 Valleys Customer Service Committee and we would like to
17 support their submission to IPART. Also with regard to
18 those submissions I have heard this afternoon from the
19 Irrigators Council, we certainly agree with where those
20 people are coming from.
21

22 We have reviewed the State Water submission and the
23 IPART water issues paper relating to this determination and
24 we are very grateful for this opportunity to put something
25 in person.
26

27 If the PowerPoint decides to work, I will put it on
28 later because there are some things that are easier to look
29 at rather than just hear about, but I am going to go
30 through our major issues. They are the forecast operating
31 cost for Toonumbar Dam; the allocation of cost between
32 irrigation users and the community; the balance of costs
33 between fixed and usage charges; the economic and social
34 impact of the proposed prices; and the current and future
35 usage.
36

37 Firstly, the forecast operating costs for Toonumbar Dam: very
38 similar to those other speakers, we really do not follow
39 just where all the costs have come from. Toonumbar Dam
40 is a very small dam with very low functional
41 cost requirements. State Water has in fact done a very
42 good job at making a very efficient dam. The outlet works
43 are very small, therefore not very costly to maintain and
44 repair. The dam has free-flow spillway so there are no
45 floodgates to maintain and, as we all realise, floodgates
46 are an important part of the big dams, and capital costs,
47 as Lisa showed us over the next period of the

1 determination, are very small.

2
3 But according to the State Water figures provided in
4 the submission State Water is aiming to recoup from the
5 users \$842,000 in the year 2010/2011. We assume this
6 figure includes those fixed costs or the indirect costs and
7 also the higher WACC, the weighted average cost to capital.
8 We actually believe this is a gross overstatement of the
9 cost of running and maintaining Toonumbar Dam, so we
10 certainly have some issues in the way the fixed costs are
11 allocated to Toonumbar. Even the operating costs we feel
12 do not represent truly what Toonumbar Dam costs.
13

14 In 2008 State Water undertook a restructure to reduce
15 costs and, as I said, they did a good job. They reduced
16 staff from five down to one, or it will be one from June.
17 They leased out the conference centre and the golf and
18 sporting facilities. Yet, according to the operational
19 expenditure amounts listed by State Water, they have only
20 decreased the actual cost by \$230,000 from \$784,000 in
21 2006/2007 down to \$555,000 in 2009/2010.
22

23 I note that Lisa put some figures up beyond 2009/2010
24 and those figures very quickly go on the upward slide again
25 back up to over \$600,000. So we are not confident that
26 these really reflect what is happening at Toonumbar. The
27 remainder of the costs, the \$290,000-odd, we believe would
28 be the indirect cost and cost of capital. We see this as
29 an extremely high figure especially when there is such a
30 small number of users. We are certainly not taking much
31 time of the office staff down at head office for Toonumbar
32 problems. I don't think we have any answer to these costs
33 except to ask IPART to look into how these costings are
34 done.
35

36 My next point is the allocation of costs between users
37 and government. Since the submission was sent, our draft
38 water sharing plan for Toonumbar has been received. There
39 were several points to note in this draft, and if we can
40 get the PowerPoint up I'll go through them on the
41 PowerPoint, and we need slide 4.
42

43 The report card for Toonumbar Dam has only just been
44 released in the last couple of weeks so not many people
45 would have seen this. The dam capacity, as we know, is
46 11,000 megalitres. Entitlements of 10,330 megalitres are
47 held between 68 licence holders. Losses from the system

1 are 4,000 to 5,000 megalitres per year. These losses are
2 to groundwater and to riparian uses. To ensure the dam
3 meets the basic landholder right the regulated system is
4 regulated in such a way that there is a visible flow at the
5 most downstream licence holder. This is also close to the
6 downstream limit of the regulated system. The annual usage
7 by licence holders is 1,000 to 2,000 megalitres, and the
8 environmental contingency allowance is 1,000 megalitres to
9 be set aside at the beginning of each year. There is no
10 access to uncontrolled flows, and there is a proposal at
11 present to extend the downstream boundary of the regulated
12 system.

13
14 We believe this water-sharing plan includes
15 significant community interests. The basic landholder
16 rights account for an unknown but large quantity of water
17 each year. During this November alone, there have been
18 very few licensed irrigators, because at the beginning of
19 November we had some good rain events. So there have been
20 very few licensed irrigators using the water and yet to
21 meet the requirements of water at the last licence holder,
22 they have been letting 22 megalitres out of the dam each
23 day.

24
25 Our farm is close to the last holder. At that farm we
26 see an enormous variation in the flow, especially after the
27 weekend. Our assumption is that the riparian users are
28 more likely to operate on weekends. Now, they have every
29 right to do that, so there is nothing we can do.

30
31 This is a photo taken at our farm just near where we
32 pump. Ten kilometres upstream from that point there is a
33 metering point and they were metering 30 megalitres of
34 water, just 10 kilometres upstream. As you can see, there
35 is nothing like 30 megalitres of water going past at that
36 point. At that stage we were actually flat strapped. That
37 water wouldn't even go over your boot. We were flat
38 strapped to find enough water to keep the pumps going, so
39 we were finding that many an evening the irrigators would
40 be stopped by morning because the pumps had run dry.

41
42 If the community interests are taken to be the losses
43 from the system, because we know that water ends up
44 somewhere or is used by them, and the 1,000 megalitres of
45 the environmental contingency allowance, it is reasonable
46 that the government should be allocated the costs of this
47 water on behalf of the community. Given that this is more

1 than half of the dam's capacity, it raises the issue of how
2 many users the dam can actually support especially in a dry
3 year unless it has very good inflows. The security of the
4 water is in fact dependent on there being a large number of
5 sleeper licences or very high inflows. If the irrigation
6 users are expected to cover the costs of the losses and the
7 environmental allowance, we believe there would be
8 considerable cross-subsidisation to the community.

9
10 My next point is the appropriate balance between fixed
11 and usage charges. There has already been some discussion
12 on this afternoon and I support the discussion we have had
13 already. Toonumbar Dam was constructed for the purpose of
14 providing regulated supply of water for irrigation.
15 Currently however the prime use of the dam is to provide
16 drought security. Of the 68 licence holders more than
17 80 per cent are inactive and hence are only earning the
18 general security entitlement charge. These properties are
19 considered valuable due to their access to an assured water
20 source; yet they are contributing minimally to the
21 maintenance of the dam.

22
23 Just out of interest, Eden Creek would have always had
24 a dry period prior to the dam's existence. There would
25 have been several months probably where it would have
26 actually run dry; whereas, of course, that does not happen
27 now.

28
29 In a dry year the number of active licence is likely
30 to double with some also participating in temporary
31 transfers of allocation. A well-established IPART
32 deliberation was to bias the charges to the usage in the
33 belief that this would create greater water use efficiency.
34 In our particular case where the issue is lack of return on
35 investments rather than water use efficiency, we question
36 whether this charging regime is actually appropriate for
37 our stream.

38
39 The issue is confounded further by information in that
40 report card which, as I showed you, indicates that the
41 security of Toonumbar water is dependent upon a large
42 number of sleepers remaining in existence.

43
44 Another issue regarding the usage charge is the lack
45 of effective metering of water used. Not only does State
46 Water have no understanding of the amount taken by riparian
47 users but licence holders are charged according to a wide

1 range of devices such as electricity meter readings, diesel
2 hour readings and diary entries of hours pumped. The
3 accuracy of some of these systems is open to question and
4 one wonders whether the lack of water extraction may
5 account for some of these inaccuracies.

6
7 The social impact is the next point I would like to
8 touch on. State Water has proposed that our current price
9 be increased by more than 1,000 per cent. When I saw these
10 figures, I was really wondering whether I was one of those
11 customers who they wanted to keep in a viable situation.
12 If this price is accepted, we believe there would be
13 significant economic and social impacts to the whole of our
14 region, in a similar fashion to the Bega story. In dollar
15 terms we believe the loss would be in excess of \$20m when
16 the multiplier effects are considered to our local
17 community.

18
19 There are a wide range of industries associated with
20 our valley, including dairies, piggeries, beef and cropping
21 enterprises. Many of these enterprises are dependent on
22 their access to Toonumbar water, whether it is for drought
23 security, as in the case of dairy farmers and the piggery
24 operators where the irrigation water is an essential part
25 of their operations, or the beef and cropping farms which
26 they tend to use it mainly as a drought-proofing part of
27 their farm.

28
29 The Toonumbar area is now recognised as one of the few
30 areas of reliable water supply within reasonable distance
31 of Brisbane. Two dairy farming families recently purchased
32 dairy farms on the water system drawn by the security of
33 the water. There has also been some interest from small
34 crop growers who have been limited by the severe water
35 restrictions in south-east Queensland over the last decade.
36 However if the prices were to be raised by over 1,000 per
37 cent, farmers simply couldn't afford the water and we
38 believe farmers would hand in their entitlements. Selling
39 them probably would not be an option given that there would
40 be no buyers.

41
42 Dairy farmers would be most seriously affected and
43 would most likely leave the area. These alone, we believe,
44 add in the vicinity of \$8m to the local community. The
45 return for piggeries would be seriously affected making
46 their future also questionable. Beef farmers we believe
47 would be forced to stock more conservatively without the

1 option of an irrigation strategy for their dry times.

2
3 To highlight these effects, similar to Bega I would
4 like to give you two case studies. The first one is the
5 farm that my husband Sam and I operate. It is an
6 irrigation farm, 158 hectares. We have a dry land area of
7 40 hectares. We currently produce about 1.8 million
8 litres. The estimated value of farm and stock is about
9 \$4m. It is a well-located farm, fully developed with good
10 quality plant and infrastructure and allows us to be
11 efficient in our use of water, labour and machinery. We
12 have won a number of awards based on efficiency including
13 last when we won the Parmalat farm of the year.

14
15 We consider that a return of capital of 4 per cent per
16 annum is appropriate for Australian agribusiness. We have
17 no borrowings and do not require significant capital
18 expenditure, so we believe that we are one of the stronger
19 farm businesses in terms of coping with these increased
20 prices.

21
22 Our farm underwent an IDMP - an irrigation and draining
23 management plan - some years ago, so our equipment
24 is regarded as appropriately efficient, and in a dry year
25 we use about 400 megalitres of water. That keeps us
26 operating a good pasture system. Our entitlement is about
27 720 megalitres but sometimes our allocation in the very dry
28 years has been as low as 50 per cent, but that sounds good
29 compared with some other dams.

30
31 The costs of this water in 2010/2011 will be \$185,000.
32 Don't worry too much about all the figures on this slide,
33 and I would just say that the figures are private figures.
34 I am happy for people at IPART to understand them and the
35 effect of the price hikes, but it is probably not useful to
36 go public with all the figures.

37
38 The farm income we have estimated through 2008 and
39 2009 are actuals; the year to June 2011 is estimated. We
40 supply Parmalat and our price has been contracted, so our
41 price is reasonably secure for the moment. If you look at
42 the cost of production, go down to the pasture water costs,
43 and look across that line, you will see that in 2008 our
44 cost was \$XX,XXX. This is only for the water. This is not
45 for electricity. In 2009, it was up to \$XX,XXX, and in
46 June 2011, it will be \$XXX,XXX. You can see what that does
47 to the gross profit. Gross profit there goes from \$XXX,XXX

1 in 2008 down to \$XXX,XXX in June 2011. Of course, that
2 drops right down to the farm profitability where we have
3 ended up with a loss.
4
5 Return on investment was where we felt we needed it in
6 June 2009 and then there would be a negative in June 2011.
7 I think you can see from this that we could no longer
8 afford to irrigate. We would have to move to a totally
9 different system of silage and bought-in feed. The next
10 issue for us would be that an intensive feeding regime in a
11 high rainfall area is not for the faint-hearted so
12 relocation would be most likely our best option. We have
13 spoken to the other dairy farmers on the system and they
14 feel the same way.
15
16 So our farm would probably be split into at least
17 three farms. Most of the farms in our area have been very
18 small farms that have been joined together and so can be
19 split up again. The future of our farm would be probably
20 to be split into three hobby farms at least where the
21 owners would enjoy the benefits and the security of the
22 free riparian water for their stock and domestic use.
23
24 The second case study is a very large piggery that is
25 also on the system. Their total production is 1.3 million
26 kilos of pork. Its general security entitlement is
27 480 megalitres, high security is 93 megalitres and their
28 annual usage is about 180 megalitres. The estimated value
29 of land, plant and stock is about \$8.8m. That is a very
30 significant business employing 16 people. The pigs
31 supplied from this enterprise make up one half day's kill
32 at the local Booyong abattoir and are essential to that
33 abattoir's future survival.
34
35 The large size of the piggery means it has
36 significant economies of scale and a low per unit cost of
37 production. In other words, some of the other piggeries on
38 the system will not cope as well with an increase in the
39 fixed water cost as this business would. It would be
40 impossible to operate this business on a seasonal or
41 part-time basis and the proposed water sharing plans means
42 that no access to high flows will be allowed, so there was
43 no option to do a water harvest and store system in an
44 effort to prepare oneself in that manner.
45
46 The following figures are just for 2009 and then
47 showing what happens when the increased water prices are

1 included. So the piggery business in 2009 was quite
2 buoyant. As I think you are aware, the piggery business
3 has the ability to drop disastrously at various times.
4 These figures do not reflect any other increases in prices.
5 What they basically show is that with that increase in
6 water charge, the profitability drops about \$100,000, the
7 return on investment by about 1 per cent, and it adds about
8 6.5 cents to their cost per kilo of pork. Given that their
9 margin is not that high, it wouldn't be very hard for the
10 whole system to suddenly become negative. Their idea was
11 that it might not mean that they are out in the first year
12 but it does make the businesses much more questionable in
13 the future.
14
15 The two cases presented are mature businesses. They
16 are most likely to be able to survive the price hike that
17 is being suggested. I think you will agree that there is
18 no way that the current users on the Toonumbar system could
19 continue to operate with these proposed prices. The
20 inability to harvest high flows and the very limited demand
21 for water trading in these areas would create a situation
22 where entitlements would just simply be handed in. Not
23 only would this destroy many people's livelihood and the
24 productivity of their farms but the only remaining
25 customers would be the riparian users who would receive the
26 water free of charge. The flow on-effect to the community
27 would include job losses, the likely closure of Booyong
28 abattoir and the loss of many supporting businesses that
29 provide goods and services to these farms.
30
31 Finally, I wish to refer to the current and future
32 usage. Our group believes that the usage of Toonumbar
33 water could increase significantly in the future if the
34 following issues are addressed appropriately, and they are:
35 water prices that are comparable to other irrigation areas;
36 a water sharing plan that does not dilute the current water
37 available; and trading of water entitlements.
38
39 As discussed earlier, Toonumbar is currently
40 recognised as reliable water supply and several farming
41 families have moved into the area. It is of interest that
42 the local council is currently carrying out survey works on
43 the Richmond River to the confluence of the regulated
44 system. It would be extremely disappointing if State Water
45 had the view of forcing farmers to give up their
46 entitlements with the aim of supplying an urban authority.
47

1 In conclusion I reiterate our lack of confidence in the
2 costing figures when we know Toonumbar is very efficiently
3 run and it is a very low cost small dam. We would like to
4 see a more appropriate split between fixed and usage
5 charges, a recognition that more than 50 per cent of the
6 water is for community purposes. We would also like to see
7 an understanding of the extreme economic and social impact
8 that price increases of 1,000 per cent would have; and
9 finally the suitability of the area to further be developed
10 for irrigation farming enterprises. Thank you.

11
12 MR COX: Thank you very much for your presentation. We
13 certainly ensure the details you wish to remain
14 confidential won't go any wider than this group here today.

15
16 MS TONGE: Thank you.

17
18 MR COX: I just wanted to ask you: I think Bega Valley
19 suggested there should be some sort of limit, say
20 5 per cent a year on price increases to their valley. How
21 would that work for your group; would that be an acceptable
22 compromise?

23
24 MS TONGE: Yes, we would see that as a reasonable
25 compromise. It gives some surety to us where we're
26 heading. We accept that we've got to see some increases,
27 we understand why that's got to happen, so I think we would
28 see that the 5 per cent would be acceptable to us. I think
29 probably more important, or as important as that, would be
30 some sort of change in ensuring that some of the sleepers
31 at leasts are actually being motivated to sell entitlement
32 or change, so that seems to be a big problem in our area,
33 that there's not enough users within the system.

34
35 MR COX: Thank you. Richard.

36
37 MR WARNER: Thank you. That was most useful. State
38 Water often meets with its customer committees and briefs
39 them on costs and their pricing submission, proposals and all
40 those sorts of things. Did they brief you on their proposals for
41 the Toonumbar at all prior to this?

42
43 MS TONGE: No, we weren't aware of the size. We have had
44 the opportunity to be involved in a subsequent committee,
45 though, so that's our fault for not being involved there
46 but we do have, I suppose, such a small number of us and
47 the time commitment, we have chosen not to actually to go

1 in person to those committees but we do have up in our area
2 Chris Magner on the unregulated part of the river who comes
3 to the customer service meetings and he lets us know what's
4 happening, so we have been getting some information but
5 certainly not directly from State Water and we were fairly
6 shocked when we saw the size of these figures.

7
8 MR WARNER: You indicated that you would like to see, or
9 you consider that current prices have a bias in favour of
10 usage charging and that you would favour a higher fixed
11 charge proportion and a lower usage charge proportion in
12 revenue. Do you have any idea what that relative balance
13 should move to?

14
15 MS TONGE: I have been reluctant to try to answer that.
16 Representing the users on the stream there's probably
17 80 per cent who are sleepers, so if you go on a numbers
18 thing, they're going to say "Well, you know, we really
19 don't - maybe 50: 50 something like that" but thinking of
20 the actual users, I know they're going to say something
21 slightly different. So we really haven't had a meeting
22 where we've got hands up to say what is the best and I know
23 it would really depend upon which entitlement holder you
24 spoke to as to how it would affect their pocket.

25
26 MR WARNER: If you were being selfish what would you
27 propose?

28
29 MS TONGE: Possibly about 60 to 70 per cent fixed.

30
31 MR WARNER: That's fine, that's good; thank you. One of
32 the other things that's come up is that State Water has
33 struggled to recover its costs because of water shortages
34 and drought over the last period and in fact it's only sold
35 about 29 per cent of its water sales forecast and recovered
36 about 68 per cent of its revenue requirement. Do you have
37 a view on how we should stitch up State Water's revenue, so
38 that we can overcome these shortfalls and prevent this
39 volatility?

40
41 MS TONGE: I feel in our area there's been very little
42 effort put into increasing usage and we believe that
43 there's a lot of potential in our area for increasing usage
44 and I suppose that's one of the reasons what we realised
45 the very high level of fixed charges we believe have been
46 put to our dam and yet we feel that we're really getting no
47 corporate service, as such, to assist our area, in terms of

1 the increasing usage. In the real world as a business, if
2 things start going wrong and you haven't got as much to
3 sell as usual, the first things you have to do is reduce
4 your fixed costs and while I know they've done a very good
5 job up in our area of reducing their variable costs within
6 the Toonumbar system - they're reducing the number of
7 employees from the five to one and on the operating costs
8 they've done an excellent job - but I really wonder at the
9 corporate level have they in fact reduced fixed costs?
10

11 As farms when we've had hard times we've had to look
12 to ways that - some fixed costs you can't touch but some
13 you can. So I really wonder have they done everything they
14 can in terms of their fixed costs, given that their
15 saleable item has decreased so much? The other thing is:
16 have they looked at all their other opportunities with this
17 water? They're really only selling for irrigation. Maybe
18 there's other things they can do, looking outside the box.
19

20 MR SMITH: In your submission you've talked about the
21 water sharing plan that has been developed for the dam and
22 you've said that there's a fear that there'll be reductions
23 in the allocations. Do you have any idea of what level of
24 reductions could be expected?
25

26 MS TONGE: The question is whether the reach of the
27 regulator system will be extended. That is one of the
28 proposals. Now, if that is extended, it means, firstly,
29 there would be more losses in the system because the creek
30 bed is a sandy creek bed continuing beyond the Eden Creek
31 into the Richmond River, that's all sandy creek bed. There
32 are many more hobby farmers and riparian farmers that
33 would be going past so you would have many, many more
34 losses coming out of the system.
35

36 I am not sure that the farmers would be going down
37 to - whether they would be wanting a regulated system in
38 their area but it's hard to say what sort of allocation
39 reduction it would receive because if that doesn't happen,
40 it won't be as significant but if it does happen it could
41 be, you know, half again or if all the sleepers suddenly
42 became active, if they sold their entitlements to an urban
43 user, for instance, who actually used the water, you can
44 see that those losses are going to continue and so suddenly
45 only half the dam is available for use, unless there's good
46 inflow during the year. Sometimes that happens.
47

1 MR SMITH: Thank you. In the North Coast your valley is
2 one of the furthest away from achieving full cost recovery.
3 What kind of approach do you think should be taken to cost
4 recovery to look at - it's probably not possible, as you
5 put, to get to that full cost recovery level but what kind
6 of approach would you see fit the purpose?
7

8 MS TONGE: Yes, I believe they've got to do things to
9 increase usage, whereas I currently believe the things that
10 have been on offer will decrease usage. So I believe that
11 anything that will increase usage will actually improve the
12 cost recovery. We don't accept the figures that we've
13 seen. We don't believe the dam costs anything like that
14 amount to run.
15

16 Many of us feel that if we were allowed to harvest
17 high flows into an off-stream storage, that you can
18 probably store 100 megalitres yourself, you know, without
19 any sort of the costs that we would pay for 100 megalitres
20 from the dam. So those sort of scenarios just don't add up
21 to the dam costing that amount. It is a good dam. It was
22 only built in the 1970s. It doesn't need a lot of repair.
23 It is working well. Those costs just do not add up to be
24 reasonable.
25

26 MS KRIEGER: Just one follow-on question. You told us in
27 the figures that you showed us that you thought a
28 4 per cent return was reasonable for a business. Is that
29 referring to your area or is that a more widespread return
30 that you think applies?
31

32 MS TONGE: We're thinking a widespread return, but there's
33 many agriculture businesses that we know that won't achieve
34 that but we believe long-term it is reasonable to expect if
35 you're putting money into something you would want at least
36 4 per cent. People putting money into something else can
37 often get more. We know that there are the vagaries of any
38 market, we've all seen that in shares in recent times. So
39 for us, my husband and I, we have tried to diversify our
40 interests but we believe if we can't achieve, you know,
41 3 to 4 per cent, why would you be doing it? It does make
42 me question the WACC that State Water is expecting because
43 they are operating in a largely agricultural setting.
44

45 MR COX: Thank you very much. That was most interesting.
46 We now have the opportunity for statements and questions
47 by people sitting in the audience and once that's been

1 completed we will invite State Water to respond to what's
2 been said at the end of the day. Are there any statements
3 or questions? I think we covered it all, so I invite
4 George and Lisa to come and respond.

5
6 RESPONSE BY STATE WATER

7
8 MR WARNE: George Warne from State Water. I'd just like
9 to commend the quality of the presentations and how it
10 really has helped our understanding. I travel a bit
11 through this wide brown land and I have been to Toonumbar
12 and I encourage anyone to go there. It is one of the most
13 beautiful places in the world and I was heartened to see
14 there are at least two farm businesses there that seem, on
15 the face of it anyway, to have enormous potential and I
16 think there might be more.

17
18 For the record there is an issue at the heart of this
19 community service obligation that we are all missing and I
20 think farm groups have done themselves no favours by
21 getting behind New South Wales farmers and opposing
22 riparian costs. They have done themselves no favours by
23 letting their neighbours take as much water as they feel
24 like taking without a licence while supporting these
25 ridiculous 16th century notions of riparian rights. I
26 think that it is time for a revolution in that area and
27 maybe within that are the seeds of a solution to this very
28 issue of what it really costs to run a river in an area
29 that has population that is growing, subdivisions occurring
30 at a rapid rate and people that really highly value a
31 regulated water source but are not paying one bean for it.

32
33 I would encourage irrigators collectively and as
34 individuals to give their farmers' association an absolute
35 wake-up call and say, "Guys, it's time we recognise the
36 cost of this service that's been provided". It's
37 particularly disheartening for State Water in some of our
38 very dry inland areas to be spending thousands of dollars
39 and driving hundreds of thousands of kilometres to appease
40 communities, many of which have got no commercial
41 relationship with us whatsoever but they enjoy the full
42 benefit of our efforts to run a regulated river system.

43
44 Just listening to the presentations today and hearing
45 the hints about this issue that is community service
46 obligation, rather than it being some generic big bucket
47 the state government has to find, I think we could do more

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1 and I would ask you to look at the work being done by
2 Coleambally Irrigation in particular, where they've made a
3 conscious effort to meter every water use that is taken
4 from their channel system and they said the savings made
5 and the improvements in their operational systems have been
6 nothing short of spectacular.

7
8 There are a number of other issues that came through
9 today, I wish they were as iconic as Bega Cheese

10
11 MR BURNS: Just different.

12
13 MR WARNE: I guess I would point out to you that it's not
14 two years ago that the rice industry was also iconic in the
15 Riverina; we were paying farmers to buy water. If you have
16 such a viable, fantastic industry that hangs off our dams
17 maybe you could consider a CSO distributing towards the
18 operation of our business to encourage your production to
19 increase; just keep it in the Bega Valley.

20
21 I was just interested to see that it is such an iconic
22 and important part, it is very difficult to transport that
23 whole industry. It hangs off highly productive farms in
24 quite a concentrated area and maybe we've all got to look
25 collectively at the ways of keeping that together.

26
27 We had a look at our overheads in the right measure
28 for assigning them, we think we've got it right. We're using
29 fully absorbed costing. We don't ask irrigators to pay
30 through their regulator charges for the administration and
31 operation of our unregulated business. We are quite proud
32 of our new financial system and how it is able to isolate
33 those costs. We encourage scrutiny of that sort of thing
34 but if there are suggestions about a fairer or a smarter
35 way to distribute our non-direct costs, we are very happy
36 to discuss that with you, provided we don't run out of
37 money.

38
39 I think that likewise my comments on the CSOs and
40 these areas that have growing populations, I don't think we
41 ought to be scared of industrial, commercial or domestic
42 uses, we will embrace them because vitally they are a
43 source of very significant income and I think in the case
44 of Toonumbar, maybe that's the beginning of the answer not
45 the problem, that we start to look at some of the other
46 people that live in very close proximity, their reluctance
47 to look at building new dams but maybe an enhancement of

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1 that storage, because as was pointed out: with one dam
2 today, you can run storage of 9,000 or 90,000 or maybe
3 900,000 megalitres and maybe that is part of the answer in
4 that area that is not as constrained to rainfall as some
5 people are. I don't want to add more but Lisa you may.
6
7 MS WELSH: I had just two points I wanted to make. One
8 was to touch on a comment that was made by Arthur about
9 some implied double dipping in terms of the costing for
10 seven-day-a-week operations, as compared to services that
11 we provide to the Hunter for the new training scheme.
12 There is some commonality in the work required because both
13 of them are triggered by additional flows. However, even
14 though there is some commonality, there is also some
15 additional specific work required to be undertaken and that
16 does take some time to calculate additional flows and
17 translate that into an off-allocation event and they are
18 the costs that State Water has included, so there is no
19 double dipping to that extent.
20
21 I was very interested to see Fleur's presentation but
22 at the same time I was a little bit concerned with some of
23 the questions raised about State Water's financial
24 information. Look, I understand that the coastal CSC does
25 meet in Sydney and that's actually a representative body,
26 that is the North Coast, the South Coast and the Hunter
27 which recognises that, yes, we need to be efficient in
28 providing our customer service to those valleys. That does
29 necessarily make it difficult for some of our customers to
30 meet. However, there are also some business papers that
31 are provided to those committees that do provide things
32 like financial information and I think probably you would
33 find valuable and I think that is a compromise we can
34 certainly make, that even if you can't attend the meetings
35 there may be some use in your also seeing those business
36 papers, so that's something that we can I guess decide
37 outside this forum. That's all I wanted to say.
38
39 Sorry, one thing that we didn't touch on is that the
40 current pricing regime for the North Coast and the Hunter
41 is slightly different to the rest of State Water.
42 State Water's other valleys have a 40/60 fixed
43 variable charge; that proportion is reversed in the Hunter
44 and the North Coast in recognition of those sleeper
45 licences and that's something that State Water is seeking
46 to maintain as well.
47

1 MR COX: Thank you very much.
2
3 MS TONGE: Can I ask a question: where do we see that come
4 through on our statements or our bills, that 60/40?
5
6 MS WELSH: I understand it is in place already as per the
7 current IPART determination.
8
9 MS TONGE: I'll have to see you later about that.
10
11 MS WELSH: Yes.
12
13 CLOSING REMARKS
14
15 MR COX: In closing I would like to say I think we have had
16 a very good discussion this afternoon about some of the
17 important issues affecting the coastal valleys and I think
18 it has been extremely valuable in focussing our attention
19 on what are the more significant issues we will need to
20 decide. So thank you very much for the effort you put into
21 it and for attending and I think for the constructive
22 discussion we had.
23
24 Our next stage obviously is to prepare a draft which
25 we will start to do over the Christmas/new year period and
26 endeavour to be in a position to have a draft approved
27 available for people to comment on in March and then you
28 will be able to say just exactly what it is we've got wrong
29 and we look forward to that, but thank you very much to you
30 for your attendance today and for the very constructive
31 discussion we have had. So thank you.
32
33 AT 4.20PM THE TRIBUNAL ADJOURNED ACCORDINGLY
34
35
36
37
38
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