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Submission to

Australian Competition and Consumer Commission

ACCC Draft Decision on

State Water Pricing Application 2014-15 - 2016-17

140417

Contents

Introduction

NSW Irrigators' Council (NSWIC) represents more than 12,000 water access licence holders across NSW. These water licence holders access regulated, unregulated and groundwater systems. Our Members include valley water user associations, food and fibre groups, irrigation corporations and commodity groups from the rice, cotton, dairy and horticultural industries.

NSWIC engages in advocacy, policy development and media relation. As an apolitical entity, we are available for the provision of advise to all stakeholders and decision makers.

This submission represents the view of the Members of NSWIC in respect to the Australian Competition and Consumer Commission's (ACCC) *Draft Decision on State Water Pricing Application: 2014/15 - 2016/17*. However, each Member reserves the right to independent policy on issues that directly relate to their areas of operation, or expertise, or any other issue that they may deem relevant.

Background

This submission is drafted in response to the ACCC's *Draft Decision on State Water pricing application: 2014/15 - 2016/17*. We recommend that this submission be read in conjunction with the ACCC's Draft Decision and any supporting documents. We also advise that NSWIC has relied on the Independent Pricing and Regulatory Tribunal's (IPART) *Review of Bulk Water Charges for State Water Corporation (1 July 2010 - 30 June 2014) - Final Report*[1] for comparison between the ACCC's Draft Decision and the current determination. References in this submissions are directly based on these documents.

In addition, we would like to remind the ACCC that NSWIC has made a previous submission to the ACCC on State Water's pricing application. Any comments and recommendations made in our previous submission are continuously endorsed by Council and are hence not repeated in this submission. Where NSWIC felt it necessary to reiterate a particular argument or provide further clarification on specific matters, we have included these points in this submission. For any other references, we recommend the ACCC consult NSWIC's previous submission (dated: 13 September 2013).

[1] http://www.ipart.nsw.gov.au/Home/Industries/Water/Reviews/Rural_Water/Review_of_Bulk_Water_Prices_to_be_charged_by_State_Water_Corporation_from_1_July_2010/18_Jun_2010_-_Final_Report/Final_Report_-_Review_of_Bulk_Water_charges_for_State_Water_Corporation_-_From_1_July_2010_to_30_June_2014_-_June_2010

General Comments

NSWIC welcomes the opportunity to make a submission to the ACCC's *Draft Decision on State Water's (SWC) pricing application: 2014/15 - 2016/17* (Draft Decision). With the significant delay of SWC's submission to the ACCC, we were extremely concerned that the review process had to be shortened which would have left stakeholders with insufficient time to fully assess the ACCC's Draft Decision. We are pleased that the ACCC has accommodated stakeholder's resource constraints and released the draft decision close to the original due date (28th February).

Whilst NSWIC supports many of the ACCC's draft decisions, we are concerned that many important cost parameters remain in flux. In particular, we believe further revisions to operating expenditure (OPEX), capital expenditure (CAPEX) and additional government charges (MDBA and BRC) will likely materialise over the next few months. We are particularly concerned about the future level of MDBA charges as the NSW Government has indicated to us that it will not apportion any additional MDBA contributions between bulk water users and the NSW Government. NSWIC believes that this could lead to significant price shocks in the next determination. In addition, NSWIC is very concerned about the proposed cost recovery mechanism for MDBA charges. As far as NSWIC can assess, the ACCC proposes to recover the full revenue shortfall of MDBA charges in the subsequent year of the determination. Such an approach could lead to additional price shocks Finally, IPART has previous conducted a high level efficiency analysis of MDBA charges and concluded in its 2010 review that an annual efficiency dividend should be applied to MDBA charges. NSWIC strongly urges the ACCC to adopt such an approach to ensure ongoing efficiency dividends from the MDBA.

Given these and other possible amendments, NSWIC believes that the values of bulk water charges in the ACCC's Draft Decision can only be regarded as indicative. This uncertainty impacts water access licence holders (WAL holders) who are unable to make accurate forward planning decisions for the next water year.

In addition, NSWIC is concerned that several of the ACCC's draft decisions are based on incomplete and imperfect information. In particular, NSWIC would like to point to SWC's embedded labour and overhead costs as well as meter service charges (MSC) which should be reassessed before the ACCC's final decision. As NSWIC anticipates that SWC will provide further information on these two items during the review, we stress that it will be vital to maintain ongoing consultation with stakeholders and provide WAL holders and their representative organisation with sufficient time to assess any new data and information submitted by SWC to the ACCC. Should such an allowance not be made, we request that the ACCC not take such information into consideration for the next bulk water pricing determination.

Furthermore, NSWIC would like to highlight that the review of SWC's bulk water charges is conducted alongside significant structural and operational changes to SWC's business. It was announced in March 2014 that SWC will be amalgamated with the Sydney Catchment Authority (SCA) to form a new entity "Bulk Water NSW"[2] (BWN). According to a letter received by the newly appointed chair of BWN Terry Charlton[3], the timeframe for the amalgamation is 12-18 months. This timeframe raises a range of important questions in respect to the next determination of SWC's bulk water charges.

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[2] http://www.dpi.nsw.gov.au/__data/assets/pdf_file/0006/507840/media_release_140304_new_world_class_water_delivery_provider_new_south_wales.pdf
[3] http://gallery.mailchimp.com/c6e5c2d75b14461767c095feb/files/BulkWaterNSW_Stakeholder_letter_FINAL.pdf

To date, NSWIC has not received written confirmation on which entity will regulate BWN. SWC's bulk water charges are currently determined by two different regulators, IPART and the ACCC. In addition, it is our understanding that the next determination for SCA is scheduled to commence 1 July 2016 while SWC is in the midst of its next determination of bulk water charges for the Murray-Darling Basin valleys of NSW. IPART thereafter will commence its review of SWC's charges for the coastal valleys of NSW in mid-2014 with a new determination expected to commence 1 July 2015. Given the vastly different determination timeframes for SWC and SCA, NSWIC is unclear about the proposed methodology for setting future bulk water charges in NSW.

Should it be the case that the next determination has to be reopened, NSWIC seriously questions the rationale for undertaking a bulk water pricing review at this point in time. Should the current review however be carried out in full, NSWIC is concerned that the changes to SWC's business and the future efficiency savings will not be adequately accounted for in the next determination.

As Terry Charlton outlined in its letter;

> *I am committed to integrating the operations of State Water and the SCA in a way that will deliver a more <u>efficient</u> and customer-focused bulk water entity, which will be both commercially successful and remain accountable to stakeholders.* (underlining added)[4]

NSWIC strongly believes that any efficiencies and cost savings resulting from the amalgamation must be translated into lower bulk water charges. As such, NSWIC urges the ACCC to conduct an OPEX review as part of the annual price assessment process to ensure that any cost savings achieved through the merger are accurately accounted for.
In the alternative, the current bulk water pricing review must be postponed to allow for a comprehensive assessment of BWN's future efficiency savings so that WAL holders will only pay for the prudent and efficient cost of SWC's operation within their valleys.

Furthermore, NSWIC is concerned about the possible financial implications of the merger between SWC and SCA. As NSWIC is less familiar with the asset base of SCA, we are concerned that the merger could lead to additional financial liabilities for SWC.

Finally, NSWIC believes that the amalgamation will lead to a change in the risk profile of BWN. While the ACCC's Draft Decision states that SWC is subject to substantial volumetric risk as part of its business operation, NSWIC believes that the amalgamation is likely to lead to a decrease in overall risk. Should this be the case, NSWIC believes that further consideration must be given to a lower required rate of return for SWC.

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[4] Ibid.

Summary of Submissions

<u>Chapter 1</u>

- *NSWIC submits that the ACCC provides a comparison between the revenue allowance in the current determination (IPART) and the proposed revenue allowance in the next determination (ACCC).*

- *NSWIC submits that SWC's proposed rate of return remains too high given the proposed merger between SWC and the SCA.*

- *NSWIC submits that the ACCC reassess SWC's proposed step-change OPEX to ensure that WAL holders only pay for the prudent and efficient costs of SWC's operation.*

- *NSWIC submits that the ACCC must ensure that MDBA/BRC charges recovered through SWC do not lead to price shocks.*

<u>Chapter 2</u>

- *NSWIC rejects the ACCC's one year base OPEX benchmarking approach and submits that a more extensive dataset and timeframe must be considered for base OPEX.*

- *NSWIC submits that no cross-subsidisation must take place between valleys.*

- *NSWIC submits that any efficiency savings resulting from the merger between SWC and SCA must be factored into bulk water charges.*

- *Given the uncertainty surrounding the new regulatory obligations of BWN, NSWIC submits that no further OPEX is made available for the certification of the environmental management system.*

- *NSWIC rejects the proposed step increase for new hydrometric monitoring agreement until further factual evidence is available.*

- *NSWIC submits that any financial obligations of SWC that result from a federal legislation must have a one hundred percent government cost share.*

- *NSWIC submits that OPEX for routine maintenance should be carried over from this determination with annual CPI adjustments minus an annual efficiency dividend.*

- *NSWIC submits that further detail on the 10 year routine maintenance category is provided.*

- *NSWIC submits that OPEX for business transformation programs should be internalised in SWC's operations and paid for through SWC's efficiency savings.*

- *NSWIC submits that an efficiency dividend of 1 per cent is not sufficient given the proposed merger between SWC and the SCA.*

Chapter 3

- *NSWIC submits that the RAB value must be based on actual expenditure figures rather than forecasts given the intrinsic link to bulk water charges.*

- *NSWIC submits that the opening RAB value must be set at the end of the third quarter of 2013-14 based on updated information from SWC which includes actual CAPEX figures together with an update on forecast expenditure for the remaining quarter.*

- *Given the uncertainty surrounding the current NSW metering project, NSWIC urges caution to not unnecessarily inflate future RAB values.*

Chapter 4

- *Should SWC be unable to provide relevant and important information on embedded labour and overhead costs, NSWIC submits that the ACCC should not provide SWC with an allowance for these costs.*

- *NSWIC submits that the ACCC must not rely on embedded labour and overhead costs from fish passage and dam safety projects as it only constitute 32 per cent of SWC's CAPEX.*

- *NSWIC submits that strict scrutiny be applied to SWC's CAPEX program and an annual reevaluation takes place to ensure that SWC has delivered on its CAPEX.*

- *NSWIC submits that unless SWC is able to provide comprehensive asset management plans for certain proposed CAPEX items, these costs should not be approved.*

- *NSWIC submits that a thorough cost benefit analysis of environmental planning and protection projects be conducted and possible alternative methods be suggested that are more cost effective.*

- *NSWIC submits that 'Corporate Systems' must be classified as standard operating procedures and hence not receive any additional CAPEX allowance.*

Chapter 5

- *NSWIC submits that SWC's proposed beta should be lowered due to the proposed merger between SWC and SCA.*

- *NSWIC support the ACCC in implementing consistent pricing principles in other Basin states.*

Chapter 6

- *NSWIC submits that the current IPART methodology must be carried over into the new Determination as the proposed amendments create significant price shocks.*

- *NSWIC submits that the ACCC should explore options to implement an 'as-incurred' CAPEX approach.*

<u>Chapter 7</u>

- *NSWIC submits that should the ACCC decide to adopt such an approach, we urge the ACCC to include most recent consumption figures from 2013-14 to provide a more representative dataset on which bulk water charges are based.*

- *NSWIC submits that a consumption forecasting model that takes into consideration the full IQQM data is the most valid method available.*

<u>Chapter 8</u>

- *NSWIC submits that the 20 year moving average approach and the overs/unders mechanism will make it virtually impossible for customers to make informed planning decisions for future water years.*

- *NSWIC strongly objects to a MDBA/BRC charge pass through methodology and request that the ACCC considers utilising its powers to scrutinize the MDBA charges.*

- *NSWIC submits that the ACCC adopts IPART's efficiency dividend approach to MDBA and BRC charges.*

- *NSWIC submits that current large customer rebates ought to be maintained as no evidence has been provided by SWC that warrant such a significant reduction in rebates.*

<u>Chapter 9</u>

- *Without additional information and a comprehensive business case, NSWIC rejects the proposed meter service charges and the methodology in full.*

- *NSWIC submits that a thorough cost benefit analysis is undertaken to assess the viability of the proposed metering project and scrutinizes the proposed charges.*

- *NSWIC submits that telemetry is not part of the proposed metering standards and should not be considered for the review of SWC's bulk water charges.*

<u>Chapter 10</u>

- *NSWIC submits that the ACCC proposed 20 year rolling average approach create adverse pricing outcomes.*

- *NSWIC submits that the balance in the proposed overs/unders account could lead to significant price volatility.*

Chapter 11

- *NSWIC submits that the ACCC applies a cost share methodology to any additional MDBA and BRC charges to ensure no price shocks.*

- *We submit that the ACCC applies a weighting (WACC) to the balance in the 'overs' and 'unders' account for MDBA and BRC charges.*

Chapter 1 - Total Revenue

NSWIC concurs with the ACCC's assessment that SWC's proposed revenue requirement was too high. Nonetheless, NSWIC notes that the ACCC's Draft Decision allows for a similar (if not higher) overall revenue than what is available to SWC in the current regulatory period[5]. The total revenue requirement set by IPART in the 2010 determination was as follows;

	2010-11	2011-12	2012-13	2013-14
Total Revenue Requirement	94,096	102,589	110,689	112,485
MDBA / BRC Charges	12,219	13,536	14,747	13,207
Revenue volatility allowance	2,237	2,237	2,237	2,237

Deducting MDBA/BRC charges and the revenue volatility allowances, NSWIC has calculated that the total allowed revenue for SWC over the last three years of the current determination was $277,562 million. Compared to the ACCC's proposed total revenue allowance of $283,000 million, this constitutes a $5,438 million (nominal) overall increase in revenue requirement. Whilst NSWIC acknowledges that these calculations are not directly comparable, we believe our assessment of increased revenue allowance for SWC is supported by figure 1-3 of the ACCC's Draft Decision[6]. Figure 1-3 highlights the IPART approved revenue allowances (user share) and the ACCC's draft decision. The trajectory for SWC's total revenue allowance (user share) appears to be steadily increasing.

In addition, NSWIC points out that a comparison between the ACCC's Draft Decision and SWC's pricing proposal is not as relevant to stakeholders as a comparison between the allowed revenue in the current determination and the proposed revenue allowance in the next regulatory period. This comparison would highlight the real change in overall allowed revenue which directly impacts the level of bulk water charges. It would also assist stakeholders in identifying changes to SWC's operation.

> **NSWIC submits that the ACCC provides a comparison between the revenue allowance in the current determination (IPART) and the proposed revenue allowance in the next determination.**

<u>Proposed revenue requirement</u>

As the ACCC outlined in its Draft Decision, the reasons for the downward adjustment in SWC's revenue requirements are due to amendments to the rate of return, forecast CAPEX and OPEX. Whilst NSWIC will address each of these components in detail later in this submission, we would like to provide the following preliminary comments;

[5] IPART's final report for the last determination and deducting MDBA and BRC charges.
file:///C:/Users/Stefanie/Downloads/Final_Report_-_Review_of_Bulk_Water_charges_for_State_Water_Corporation_-_June_2010_-_Website_Version%20(9).pdf
[6] ACCC Draft Decision, p.11

- Rate of Return

NSWIC does not concur with the ACCC's assessment that a rate of return of 7.44 per cent is adequate for SWC. While we acknowledge that this value is significantly lower than SWC's proposed value of 8.96 per cent, NSWIC considers it still too high given the recently announced merger between SWC and the SCA. NSWIC is of the opinion that the merger will reduce SWC's volumetric risk, which in turn should reduce the required rate of return.

NSWIC submits that SWC's proposed rate of return remains too high given the proposed merger between SWC and the SCA.

- CAPEX

NSWIC considers it difficult to thoroughly assess the ACCC's proposed CAPEX as a large part of SWC's CAPEX work is confidential. We would like to reiterate however that SWC has continuously under-spent on its allowed CAPEX. We believe it is important that this fact is considered and appropriate safeguards are put in place to ensure that SWC will fulfill its proposed CAPEX plan.

- OPEX

NSWIC notes that SWC's allowed operating expenditure has not be substantially amended to the current regulatory period despite stakeholder's concerns about specific thematic expenditure items (which are outlined further in Chapter 2). We note that IPART's determined OPEX value over the current regulatory period were as follows;

	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
IPART	38,622	38,195	38,058	37,100			
ACCC					38,860	38,650	38,070

($ '000, 2009/10, 2013/14)

NSWIC submits that the ACCC reassesses SWC's step-change OPEX to ensure that WAL holders only pay for the prudent and efficient costs of SWC's operation.

Changes to revenue requirement

NSWIC points out that significant amendments to SWC's allowed revenue are possible due to further changes in forecast CAPEX, meter service charges and MDBA/BRC charges. As the NSW Government has recently informed us, it will request MDBA/BRC charges to be recovered through SWC's bulk water charges. In addition, the NSW Government indicated that these charges are likely to increase and that current cost share arrangements are not necessarily guaranteed (beyond the current arrangements for the $8.9 million MDBA contribution). This last point is of significant concern to NSWIC as it could lead to serious price shocks for SWC's customers.

NSWIC submits that the ACCC must ensure that MDBA/BRC charges recovered through SWC do not lead to price shocks.

Revenue 'smoothing'

In concluding, NSWIC is concerned about the approach of 'smoothing' SWC's revenue requirement over the next regulatory period. This method provides less clarity and transparency for stakeholders. While we understand that the resulting values are NPV neutral, the adjustments of revenue requirements to maintain price stability will mean that WAL holders will (in some instances) have to pay more in the earlier years of the next determination without yet having received some of the benefits from SWC's services and operations. NSWIC rejects such an approach and submits that IPART's methodology be carried forward to this determination period.

In addition, NSWIC would like to seek clarification on table 1-14 and table 1-15 as the calculations are not adequately explained.

> **NSWIC rejects the approach of smoothing revenue requirement and submits that IPART's previous methodology is carried forward in this determination.**

Chapter 2 - OPEX

NSWIC supports the ACCC's proposed reduction in SWC's OPEX but remains concerned about the proposed overall level and trend of OPEX in the next regulatory period. In particular, SWC's OPEX continues to rise and is at a higher level than during the current regulatory period (figure 2-1).

NSWIC believes that one reason of this rise in SWC's allowed OPEX, is the ACCC's proposed 'base and step' approach. Without solid evidence that SWC's current OPEX is prudent and efficient, NSWIC believes that such an approach could simply lead to a continuous increase in SWC's OPEX. In addition, NSWIC questions how the ACCC can assess SWC's base OPEX if it only relies on information from the 2012-13 financial year. Without further information, NSWIC objects to such benchmarking and submits that the ACCC's assessment of 'base OPEX' must be based on a more extensive dataset and timeframe.

> **NSWIC rejects the ACCC's one year base OPEX benchmarking approach and submits that a more extensive dataset and timeframe be considered for base OPEX.**

Cross-subsidisation

NSWIC has outlined on multiple occasions that it does not support cross-subsidisation between valleys. As such, NSWIC would like to seek clarification from the ACCC on the following statement in the Draft Decision;

> *"The ACCC's forecast is that the level of total bulk water OPEX for each valley, the comparison and determination of OPEX was not undertaken for individual categories or types of OPEX."* (p.34)

Whilst NSWIC acknowledges that a disaggregation of OPEX between different categories and types is challenging in some instances, we urge the ACCC to take significant care when determining valley specific OPEX to avoid cross-subsidisation. As NSWIC was not provided with additional detail on the financial magnitude of these 'categories or types' of OPEX, we are unable to assess the impact on bulk water charges.

> **NSWIC submits that no cross-subsidisation must take place between valleys.**

In addition, NSWIC stresses that an assessment of SWC's valley specific OPEX will become increasingly more difficult through the merger between SWC and the SCA. However, whilst transparency of OPEX is a significant concern to NSWIC, we believe that the merger of the two entities should result in further OPEX savings and efficiency dividends that ought to be attributed to bulk water users. It is our understanding that many 'back office operations' will be amalgamated straight after the merger, hence the savings should be directly visible in the first year of the next determination. NSWIC urges the ACCC to conduct an OPEX review as part of its annual price assessment process to ensure that any efficiency savings are accurately accounted for.

> **NSWIC submits that any efficiency savings resulting from the merger between SWC and SCA must be factored into bulk water charges.**

Step-Changes

Independent of our concerns about SWC's efficient and prudent 'base OPEX' we furthermore reject several of the proposed step changes in the ACCC's Draft Decision.

Certification of environmental management system (EMS)

NSWIC acknowledges that State Water's Operating Licence for 2013-18 requires SWC to develop, implement and certify and EMS by 30 June 2018. We do however note that since the announced merger between SWC and SCA, a new operating licence will be applicable to BWN. It should be considered whether SWC's obligation in respect to the EMS could change as a result of the merger. Given the uncertainty about the new regulatory obligations of BWN, NSWIC submits that no further OPEX is made available for this thematic expenditure item.

> **Given the uncertainty about the new regulatory obligations of BWN, NSWIC submits that no further OPEX is made available for the certification of the environmental management system.**

New hydrometric monitoring agreement with NSW Office of Water (NOW)

NSWIC rejects the proposed step increase for new hydrometric monitoring agreements. As the current determination for NOW has been deferred until 2015, we believe that the allowance for the 2014-15 regulatory period should be removed.

In addition, we believe there is significant uncertainty over what costs will be imposed on SWC for obtaining river gauging and data management services. Without further detail on what charges NOW will levy on SWC, NSWIC rejects this proposed step increase by the ACCC until factual evidence is provided to the ACCC and stakeholders.

> **NSWIC rejects the proposed step increase for new hydrometric monitoring agreement until further factual evidence is available.**

Regulatory costs

As the burden of two regulators is a direct result of a Federal Act (*Water Act 2007* and the associated *Water Charge (Infrastructure) Rules)*, NSWIC objects to charging bulk water users for this thematic expenditure item. NSWIC submits that any financial obligation of SWC that is a direct result of a federal legislation must have a one hundred percent government (NSW) cost share.

> **NSWIC submits that any financial obligations of SWC that result from a federal legislation must have a one hundred percent government (NSW) cost share.**

Periodic routine maintenance

As outlined in our previous submission, we reject any increases in this thematic expenditure item. As the name for this thematic expenditure item suggests, a routine maintenance should be part of the base OPEX and should not attract any additional OPEX requirements for SWC.

> **NSWIC submits that OPEX for routine maintenance should be carried over from this determination with annual CPI adjustments minus an annual efficiency dividend.**

Whilst we acknowledge that the ACCC has addressed NSWIC concerns in respect to this thematic expenditure item, we are not convinced that sufficient explanation has been given on the elevated number of routine maintenance in the 10 year category. We urge the ACCC to provide further detail on this particular expenditure item.

> **NSWIC submits that further detail on the 10 year routine maintenance category is provided.**

Cold water pollution investigations

NSWIC rejects the proposed step increase for this thematic expenditure item. As the ACCC's Draft Decision outlines, cold water pollution investigation is currently an obligation under SWC's operating licence and water supply works approvals. As such, NSWIC considers this evidence that SWC should have factored these costs into its base OPEX. No further allowance should be made for this thematic expenditure item.

> **NSWIC submits that OPEX for cold water pollution investigation is already accounted for in SWC's base OPEX and hence no further step increase OPEX should be made available.**

In addition, NSWIC considers it questionable that the ACCC allowed a step change in OPEX of $70,000 whilst SWC has currently incurred costs of about $66,000 for investigation of Burrendong. NSWIC submits that if the ACCC decides to allow for further step increases in OPEX for this thematic expenditure item, then the maximum allowance should be no greater than the current revealed costs plus CPI.

Business Transformation Program

NSWIC strongly rejects the OPEX allowance for the business transformation program. As we have outlined in our previous submission to the ACCC, an allowance has already been made in the current determination for a number of IT upgrades. NSWIC therefore submits that the funds for previous IT upgrades have not been utilised efficiently and hence no further allowance should be provided to SWC to undertake such works. To the contrary, should further IT upgrades be necessary, NSWIC submits that they are internalised in SWC's operation and paid for through SWC's efficiency savings.

> **NSWIC submits that OPEX for business transformation programs should be internalised in SWC's Operations and paid for through SWC's efficiency savings.**

Efficiency Dividend

NSWIC welcomes the ACCC's assessment that SWC should be able to achieve an ongoing efficiency gain after accounting for forecast wage growth. However we question whether 1 percent (after wage growth) is sufficient especially given the merger between SWC and SCA.

> **NSWIC submits that an efficiency dividend of 1 per cent is not sufficient given the proposed merger between SWC and the SCA.**

Chapter 3 - RAB

As the RAB is a crucial input in determining SWC's total revenue requirement, we consider it vital that the opening RAB at 2010 and the methodology to determine the 2014 RAB is correct and transparent.

NSWIC notes that the ACCC is required to assess SWC's proposed RAB for each year of the 2010-14 and 2014-17 regulatory periods. According to the ACCC's Draft Decision, uncertainty exists about the opening RAB as at 1 July 2010 due to a discrepancy between actual and forecast CAPEX for 2009-10 and 2010-11. NSWIC strongly urges the ACCC to investigate these matters as any subsequent consideration of RAB would be flawed should the opening RAB for 2010 not be accurate.

Roll Forward Methodology

NSWIC reiterates that we consider the practice of rolling forward the RAB in order to create an opening value for the next Determination as flawed given that the process is based on forecasts in the last year of the current regulatory period.

As SWC has significantly under-spent on its CAPEX in the first three years of the current regulatory period, we are highly doubtful that SWC can deliver on its CAPEX forecast in 2013-14. As table 3-1 outlines, the ACCC's draft decision expected net CAPEX in 2013-14 to be $83.2 million while net CAPEX in all other years of the current regulatory period were significantly lower. This means that a significant proportion of the opening RAB on 1 July 2014 will be based on forecast CAPEX instead of actual verified expenditures. As such, NSWIC would like to reiterate its previous submission at this point;

> **NSWIC submits that the RAB value must be based on actual expenditure figures rather than forecasts given the intrinsic link to bulk water charges.**
>
> **NSWIC submits that the opening RAB value must be set at the end of the third quarter of 2013-14 based on updated information from SWC which includes actual CAPEX figures together with an update on forecast expenditure for the remaining quarter.**

In this way, the ACCC will have a better understanding on the actual capital expenditures made by SWC over the last year of the current regulatory period and should be better placed to determine an appropriate opening RAB value.

NSWIC stresses again that such a proposal is not only appropriate but also supported by the ACCC Pricing Principles;

> *"The RAB should represent the value of all assets that have been funded directly by the operator and which are required for the provision of infrastructure services for which regulated charges are payable."*

We consider this comment to clearly outline that the RAB value should represent the value of the assets that have actually been funded, and not the value of the assets that might be funded.

In addition, NSWIC notes that the ACCC Pricing Principles state;

> *"If the initial value of the RAB was to result in prices changing significantly from prior levels - that is, if it resulted in price shocks - this would be a perverse and generally unintended outcome. Hence, the regulator should ensure that the initial RAB value does not result in price shocks."*

NSWIC considers this statement is of considerable importance due to the proposed changes to SWC's depreciation methodology. As will be outlined at another point in this submission, NSWIC believes that the ACCC's proposed approach to calculate asset lives and depreciation will lead to a significant price shock that contradicts the ACCC's pricing principles.

Opening RAB

NSWIC would like to seek clarification as to why the ACCC has accepted a significant higher opening RAB even though IPART's previous determination fixed a lower value. As this is a significant difference in opening RAB (i.e. by $57.8 million) we consider it warranted that stakeholders are provided with more detailed information on the reason behind this increase.

In addition, NSWIC does not concur with the ACCC's assessment that;

> *The impact of this error is an increase to the RAB as at 1 July 2010 due to the inclusion of the higher estimated CAPEX for 2009-10. However, this impact is more than offset by the revised reduction in the true up that occurs in the 2013-14 to reflect that State Water's actual CAPEX of $70.4 million (nominal) for 2009-10 was much closer to the corrected estimated CAPEX allowance for that year than the amount originally proposed.*

NSWIC considers that only values that IPART has allowed should enter into the RAB.

Metering

NSWIC is also concerned about the proposed growth in SWC's metering program. Whilst we will address this issue in chapter 9, we would like to point out that SWC's assets in respect to metering is forecast to grow which will lead to an increase in RAB and ultimately to an increase in bulk water charges. Given the uncertainty surrounding the current NSW metering project, NSWIC urges caution to not unnecessarily inflate future RAB values whilst uncertainty remains about the metering project.

> **Given the uncertainty surrounding the current NSW metering project, NSWIC urges caution to not unnecessarily inflate future RAB values whilst uncertainty remains about the metering project.**

Chapter 4 - CAPEX

NSWIC considers it difficult to comment on the proposed CAPEX allowance as much of the information relevant for this chapter is confidential. We do however congratulate the ACCC on its assessment of the embedded labour and overhead costs which we note were significantly reduced (i.e. by $10.7 million). The resulting decreases in SWC's CAPEX allowance is welcomed by stakeholders who have been very concerned about SWC's capital expenditure plans over the next regulatory period.

In addition, NSWIC continues to hold considerable doubt over SWC's ability to deliver on its forecast CAPEX in 2013-14 (and beyond) given that SWC has considerably under-spent on CAPEX over the first three years of the current regulatory period (Figure 4-1). We reiterate that a similar picture emerged during the previous determination.

The CAPEX value for 2013-14 is of particular importance as it has a direct influence on SWC's open RAB for the 2014-17 regulatory period. As such, we reiterate our strong support for setting the opening RAB value at the end of the third quarter in 2013-14 as it can be based on updated information from SWC's actual CAPEX.

Capitalised labour and overheads

NSWIC supports the ACCC's assessment of SWC's excessive capitalised labour and overhead forecasts but we remain concerned that SWC will provide further information to justify its previous proposal. As NSWIC and its members do not have access to any information on the capitalised labour and overheads forecast, we strongly urge the ACCC to make any further information by SWC available to stakeholders. As the ACCC has outlined;

> *"The ACCC requested that State Water provide data on all internal labour costs included in the cost forecasts for each project and State Water advised that it was unable to do so."* (p.97)

Should SWC be unable to provide relevant and important information to the ACCC, NSWIC submits that the ACCC should not provide SWC with an allowance for these items. Only prudent and efficient costs should be reflected in future bulk water charges and if the regulator is not able to assess the efficiency of these costs, then they should not be passed on to customers. As such, we object to the ACCC's methodology of extrapolating existing labour and overhead costs;

> *"Despite the ACCC only being able to identify the labour and overheads in projects accounting for 32 per cent of State Water's CAPEX, the ACCC identified labour and overheads of $11.4 million."* (p.98)

In addition, the ACCC Draft Decision states that;

> *"Given the lack of detailed information, the ACCC considers that the fish passage and dam safety costings (where labour and overheads were identifiable) are the best information available to indicate State Water's approach to forecasting labour and overhead costs."* (p.99)

NSWIC considers this process flawed as not all projects would attract the same labour and overhead costs. In addition, since fish passage and dam safety only make up 32 per cent of SWC's CAPEX we strongly reject the ACCC's extrapolation approach and insist on transparency of SWC costs. Otherwise, NSWIC submit that the ACCC should follow the ACCC's consultant's recommendation and remove labour and overheads from SWC's cost forecasts.

Should SWC be unable to provide relevant and important information on embedded labour and overhead costs, NSWIC submits that the ACCC should not provide SWC with an allowance for these items.

NSWIC submits that the ACCC not rely on embedded labour and overhead costs from fish passage and dam safety project as it only makes up 32 per cent of SWC's CAPEX.

Deliverability of overall capital expenditure

As NSWIC has outlined in its previous submission to the ACCC, we share the ACCC's concern about the deliverability of the overall CAPEX program. However, we disagree that this problem only exists in the first year of the next determination. We submit that deliverability issues have been systemic with SWC as the last two determinations periods have shown.

As such, NSWIC submits that strict scrutiny be applied to SWC's CAPEX program and an annual reevaluation takes place to ensure that SWC has delivered on its CAPEX. Should significant discrepancies emerge, NSWIC believe that adjustments to overall CAPEX allowance should be considered by the ACCC (subject to maintaining price stability). NSWIC reiterates that it considers it crucial that bulk water users are only charged for those CAPEX which has been commissioned and is operational, rather than CAPEX that has been planned.

As such, NSWIC submits that strict scrutiny be applied to SWC's CAPEX program and an annual reevaluation takes place to ensure that SWC has delivered on its CAPEX.

Assessment methodology

NSWIC understand that the assessment of forecast CAPEX is difficult as different projects are at different stages of readiness. We do however submit that the uncertainty surrounding some thematic expenditure items is a concern to stakeholders who are forced to pay for projects whose costs are not yet agreed upon. NSWIC urges the ACCC to thoroughly consider the underlying costs of each project and should SWC not be able to provide comprehensive asset management plans, then we submit that these costs should not be approved.

Should SWC not be able to provide comprehensive asset management plans for certain proposed CAPEX, NSWIC submits that these costs be not approved.

Environmental planning and protection

NSWIC stresses that the ACCC's Draft Decision for environmental planning and protection is a significant cost driver of SWC's bulk water charges in some valleys. As this thematic expenditure item is 50 per cent user funded, any significant increases will have a direct impact on customers.

While we note that the ACCC has reduced the CAPEX allowance for this thematic expenditure item by $11.9 million, we believe that not sufficient scrutiny has been applied to assess the need for all of SWC's proposed projects. Neither has a comprehensive cost benefit analysis been conducted that would assess whether the proposed projects are cost effective. Stakeholders have continuously raised concerns that the works proposed by SWC are very expensive without a corresponding assessment for their need or their benefit.

In addition, NSWIC reiterates that SWC has based the CAPEX proposal in this thematic expenditure item on assumptions about directions from the Minister of Primary Industry. Without clear direction from the Minister, NSWIC does not accept State Water's proposal of $57.3 million or the ACCC's draft allowance of $45.4 million.

NSWIC submits that a thorough investigation of possible alternative works be done that might be more cost effective. NSWIC recognises that the ACCC's consultant supported fishway offset program as a more cost-effective way of meeting environmental objectives rather than fishways at the main dam walls. However, NSWIC submits that there are possibly other ways to enable fishways that are even more cost effective.

NSWIC would also like to point out that the NSW Government has informed us that the *Fisheries Management Act 1994* is being considered by the NSW Government for amendment. This could therefore lead to a significant change in SWC's obligation in relation to environmental planning and protection.

> **NSWIC submits that a thorough cost benefit analysis of environmental planning and protection projects are being conducted and possible alternative methods are being suggested that are more cost effective.**

Water Delivery and other operations

NSWIC welcomes the ACCC's assessment of SWC' proposed water delivery and other operations proposal.

Corporate Systems

We remain concerned about the cost allowance for this thematic expenditure item. We believe that corporate system must be classified as standard operating procedures and hence not receive any additional CAPEX allowance.

> **NSWIC submits that Corporate Systems must be classified as standard operating procedures and hence not receive any additional CAPEX allowance.**

NSWIC continues to urge the ACCC to thoroughly consider the proposed expenditure and only allow funding if the updates will lead to benefits for SWC's customers.

As the ACCC outlines in its draft submission;

> *"There is a justified need to replace ageing systems and avoid risk of failure of business and operating systems."* (p.127)

However, NSWIC notes that an allowance for CAPEX was made in the current regulatory period for such upgrades. Customers are yet to see the benefits of such expenditure.

Additionally, we are concerned that SWC has provided additional information to the ACCC on its Corporate System expenditure proposal that was not available to stakeholders. As the ACCC's draft determination outlines;

> *"Subsequent to providing its pricing application, State Water provided the ACCC with new information, which indicates that State Water considers it has under-estimated its funding needs for the BTP."* (p.130)

NSWIC rejects such an approach and requests that any cost proposals outlined by SWC are made available to stakeholders. Without complete information, customers will be unable to fully assess SWC's pricing proposal. In addition, NSWIC does not share the ACCC's assessment that;

> *"The ACCC considers that its decision does not preclude State Water from proceeding with an increased level of CAPEX above its approved allowance in the next period if it is confident that the internal benefits justify the expenditure. Given the large role that efficiency plays in State Water's justifications for the BTP, further works under the BTP may be effectively self-financing."* (p.130-131)

NSWIC does not believe the ACCC has provided sufficient clarity that additional expenditure must be offset by additional savings elsewhere. Should this not be the intention of the above statement, NSWIC is very concerned that the ACCC's assessment could mean additional costs for stakeholders that are not thoroughly assessed or approved by the ACCC.

Allocation of State Water wide costs to each valley

NSWIC is concerned about the ACCC statement that;

> *"State Water is undertaking several CAPEX projects where the project benefits State Water as a whole and the cost of these projects cannot be explicitly allocated to one of the valleys. Where this is the case, State Water has allocated a portion of the cost to each valley."* (p.137-138)

While NSWIC acknowledges that allocating certain costs might be difficult, we would like to reiterate at this point that we strongly oppose cross-subsidisation. In addition, we consider that the allocation of a portion of the cost to each valley does not allow for a transparent assessment of overall CAPEX costs in each valley.

Chapter 5 - Rate of Return

NSWIC welcomes the proposed reduction in SWC's WACC, however we believe that further revisions to the rate of return will be necessary due to the recently announced merger between SWC and the SCA. The merger should decrease the volumetric risk of SWC and hence should directly influence SWC's beta value which the ACCC is proposing to set at 0.7. In light of the merger, NSWIC submits that the ACCC should consider lowering the beta value to accurately reflect SWC's underlying systematic risk.

NSWIC believes that this request is supported by the ACCC's draft decision in that it notes;

> *"..that 0.7 was consistent with the upper range of the empirical equity beta estimates of 0.44 - 0.68 in the AER's 2009 WACC review."* (p.150)

With the merger of SWC with SCA, NSWIC believes that the overall beta is likely to be lower.

> **NSWIC submits that SWC's beta should be lower due to the proposed merger between SWC and SCA.**

Basin wide consistency

NSWIC would like to comment on the ACCC's Draft Decision;

> *"The rationale for publishing the pricing principles was to achieve consistent implementation of pricing approvals and determinations throughout the Murray Darling Basin."* (p.143)

NSWIC would like to stress that inconsistency remains between Basin states as bulk water charges are handled very differently in the Basin. NSW has for years been at the forefront of water management and bulk water charges.

> **NSWIC support the ACCC implementing consistent principles in other Basin states.**

Chapter 6 - Regulatory Depreciation

NSWIC is extremely concerned that the ACCC proposes to significantly deviate from previous calculations on SWC's remaining economic asset lives. As the ACCC Draft Decision states;

> *"The ACCC considers that applying different remaining economic lives to each valley is more transparent and better reflects the principles of user pays than adopting a single remaining asset life for all valleys and better represents the mix of assets used in each valley."* (p.174)

As the ACCC has proposed significantly lower values for SWC's remaining economic asset lives, we believe that this amendment leads to a significant price shock. This concern is furthermore supported by the following statement;

> *"To the extent that changes to remaining economic lives impact on State Water's regulated charges, the ACCC considers that price shocks can adversely affect the efficient development of a market and its related markets and have a perverse or unintended pricing outcome."* (p.175)

In addition, the ACCC states that its own analysis shows that;

> *"..total revenues to be recovered from users over the entire 2014-17 regulatory period would decrease by between 1 per cent and 2.5 per cent across most valleys compared to State Water's application."* (p.175)

NSWIC believes that such an amendment is significant, in particular since some valleys are proposed to experience only a 1-3 per cent adjustment to their overall bulk water charges (i.e. NSW Murray and Murrumbidgee). In addition, NSWIC would like to point out that the ACCC is proposing a 1 per cent efficiency dividend from SWC in the next determination. Given the significant adjustments to SWC's asset calculations, these efficiency savings have been dwarfed by a proposed amendment in the asset life methodology.

Finally, NSWIC does not consider it valid to claim that;

> *"The revenue impact of this draft decision on the remaining asset lives is over the 2014-17 regulatory period and is more than offset by the reductions to other building block costs."* (p.175)

NSWIC believes that an offset in another category is not a valid excuse to propose a significant price shock in another. We submit that the ACCC's proposal to amend SWC's asset lives constitute a price shock based on the ACCC's pricing principles.

> **NSWIC submits that the current IPART methodology must be carried over into the new Determination as the proposed amendments create significant price shocks.**

As-incurred CAPEX

In addition, NSWIC is disappointed that the ACCC accepts SWC's proposal to use a 'as-incurred' CAPEX, instead of the ACCC's preferred approach of using a 'partially as-incurred method'.

As the ACCC has outlined;

> *"Under a partially as-incurred approach the regulated business earns a return on capital on CAPEX as the cost is incurred. However, the business is only able to earn a return of capital (depreciation) on assets that are commissioned and providing services - that is, assets that are providing infrastructure services, as required by Schedule 2 of the WCIR."* (p.178)

NSWIC believes that the WCIR are clear in that depreciation should only be applicable to infrastructure that provides infrastructure services. As such, NSWIC does not accept SWC's view that a significant financial reporting amendment is required to provide this data at present. Whilst NSWIC recognises that such an approach does not impact on the amount of depreciation, we still highlight that the timing of the depreciation is important for stakeholders who do not want to pay for infrastructure that is not yet providing infrastructure services.

> **NSWIC submits that the ACCC should explore options to implement an 'as-incurred' CAPEX approach.**

Chapter 7 - Forecast water extractions and entitlement volumes

NSWIC notes that creating a forecast for consumption has been - and must continue to be - a task for the regulator. Basic climate variability and unpredictable rainfall patterns make this task difficult. In order to assess and determine consumption forecast values, NSWIC reiterates that IPART has relied on the Long Run Average (LRA) from the IQQM model for previous Determinations (or similar in valleys where IQQM is not used).

Whilst NSWIC acknowledges that IPART has deviated from this approach in the most recent Determination, we continue to support the use of the full IQQM (or equivalent) dataset and submit that the last two years of this Determination have clearly shown that a 20 year averaging approach is not necessarily superior to the full IQQM model.

In particular, the full IQQM model provides a long run average consumption forecast of 5450 GL, which closely aligns with actual extraction figures in 2012-13 (5986 GL). In comparison, the 20 year rolling average approach returned (4283 GL) as proposed by the ACCC in its draft decision (p.182). According to the ACCC's Draft Decision,

> *"The forecast water extractions approved in this draft decision represents a decrease of four per cent relative to 2010 IPART approved forecasts."* (p.181)

This value significantly deviate from the most recent consumption figures and create additional upwards pressure on bulk water charges.

Timeframe

NSWIC rejects the ACCC's approach of using the values of actual extractions in 1993-94 to 2012-13 for the forecast consumption in the first year of the next determination. The ACCC must recognise that this sample is significantly biased due to the very low extractions during the millennium drought and are not in any way representative of water extractions in the most recent years. Basing water extractions on such a timeframe will create significant downward bias which will directly impact bulk water charges. The decrease in consumption forecast will cause upwards pressure in prices, which has shown to have created significant profits for State Water this financial year.

> **NSWIC submits that should the ACCC decide to adopt such an approach, we urge the ACCC to include most recent consumption figures from 2013-14 to provide a more representative dataset on which bulk water charges are based**.

Volatility

NSWIC strongly disagrees with the ACCC's assessment that some methods relative to others may minimise the magnitude of price fluctuations, mainly;

> ...*proposed 20 year moving average in that it shortens the forecast horizon.*

Whilst the forecast horizon is certainly shorter than under the IQQM model, the ACCC has disregarded the fact that a 20 year moving average that is based in large part on the millennium drought cannot be considered a 'representative sample'.

NSWIC also vehemently disagrees with the ACCC's and IPART's assessment that there is evidence of a 'structural break' in water extractions in most valleys. This assessment was made by IPART during the millennium drought, however most recent years have shown that basic climate and rainfall patterns are unpredictable. As such, NSWIC does not consider there to be any evidence to suggest that a structural break has taken place in water extractions in NSW Murray Darling Basin valleys.

As we have outlined in our previous submission, the full IQQM dataset highlights that there have been previous periods of very low water availability (including droughts) and these factors are incorporated into the calculation of average consumption. In comparison, the use of a 20 year rolling average model means that consumption figures are continuously updated in each year of the regulatory period. Whilst NSWIC acknowledges that year-on-year fluctuations would be small, the additional uncertainty that a rolling average methodology creates will not assist individual WAL holders to predict future price movements. This is particular relevant given the ACCC's proposed 'unders/overs' mechanism that might be introduced to also adjust bulk water charges year on year. As such, NSWIC reiterates its strong support for the use of the full IQQM model;

> **NSWIC submits that a consumption forecasting model that takes into consideration the full IQQM data is the most valid method available.**

Chapter 8 - Bulk Water Charges

NSWIC strongly supports the ACCC's decision to maintain the current 40:60 (fixed: variable) tariff structure. As we have outlined extensively in our last submission, we considered SWC's proposal to constitute a significant shift in risk from SWC to customers. We note that SWC has proposed this amendment on multiple occasions in the past, but IPART has continuously and comprehensively rejected such an approach on the basis of equity and risk sharing between SWC and its customers.

However we note that two submissions to the ACCC supported the transitioning towards higher fixed charges, one of which was SCA. As SWC will soon be amalgamated with SCA, we are concerned there will be further push from the BWN for a higher fixed tariff structure. Whilst we acknowledge that the ACCC has made it clear to maintain the 40:60 (fixed : variable) tariff structure, we would like to highlight this issue as a matter of great importance to our members.

<u>Bulk Water Charges</u>

NSWIC has previously outlined its concerns to the proposed overall revenue requirement and made submissions to support these arguments in chapter 2,3 and 5.

NSWIC believes that the ACCC's proposed charges are far from certain due to possible significant adjustments to CAPEX, meter service charges and MDBA/BRC charges. As such, we do not currently share the ACCC's views (table 8-7) of bulk water price comparison (based on 2013-14 values).

In addition, NSWIC considers the charges presented in table 8-1, 8-2 and 8.3 as 'indicative' because many important input cost factors are yet to be determined. Furthermore, bulk water charges in 2015-16 and 2015-17 are even more uncertain due to the proposed 20 year rolling average approach and the 'overs/unders' mechanism. These two mechanisms will lead to even greater price volatility and make it virtually impossible for customers to make informed planning decisions for future water years.

> **NSWIC submits that the 20 year moving average approach and the overs/unders mechanism will make it virtually impossible for customers to make informed planning decisions for future water years.**

<u>MDBA/BRC charges</u>

NSWIC would like to stress that bulk water charges will considerably change with the inclusion of MDBA and BRC charges. As the ACCC states,

> *"The NSW Government informed the ACCC in February 2014 that its contribution to MDBA and BRC costs would be recovered from users through State Water charges in the 2014-17 period and that State Water will be required by the NSW Government to recover these costs."*

This recovery process has been heavily criticised by NSWIC as the efficiency of the MDBA could not be comprehensively assessed. As IPART did not have a mandate to thoroughly assess the efficiency of MDBA and BRC charges, these charges were passed on to customers.

NSWIC strongly object to a MDBA/BRC charge pass through and request that the ACCC considers utilising its powers to scrutinize the MDBA charges.

However, we note that IPART applied an efficiency dividend to MDBA charges, which we urge the ACCC to adopt.

NSWIC submits that the ACCC adopts IPART's efficiency dividend approach to MDBA and BRC charges.

High Security Premium

NSWIC believes that the ACCC Draft Decision provides insufficient information on the methodology for calculating high security premiums in NSW (8-12). Based on the last IPART determination, NSWIC is of the understanding that the high security premium is based on an 'access' premium and a 'scarcity' premium. We have submitted to IPART in 2010, that we do not agree with the 'scarcity' premium as the concept of 'scarcity' does not relate to delivery infrastructure but to the good which is being delivered through it - water. The scarcity value of water is priced in the market for that commodity and hence there is no requirement for shadow pricing derived from that market for delivery infrastructure pricing.

NSWIC submits that scarcity is priced in the market for water and should not be further priced via delivery infrastructure.

In addition, NSWIC would like to point out that it is SWC's responsibility to release water, however it must be recognised that in some valleys there is no difference in delivering water against high or general security entitlement holders. Given these valley specific differences, NSWIC strongly urges the ACCC to consult with our members on this issue as the rationale for this premium is not necessarily justified in all of NSW.

Large customer rebates

NSWIC welcomes the continuation of large customer rebates. However, we question the significant reduction in proposed rebates for several ICDs. In particular, the reduction for Murrumbidgee Irrigation and Coleambally are significant (57 and 58 per cent respectively). Whilst little information is provided in the ACCC's draft decision as to why the cost parameters were changed significantly from the 2010 Determination, we are unable to fully assess and comments on the significant changes.

NSWIC submits that current large customer rebates ought to be maintained as no evidence has been provided by SWC that warrant such a significant reduction in rebates.

NSWIC continues to urge the ACCC to consult closely with the irrigation corporations on this issue as their knowledge and expertise on this matter is invaluable.

Chapter 9 - Metering and Miscellaneous Charges

NSWIC believes that insufficient information is provided in the ACCC Draft Decision on meter service charges.

As we outlined in our previous submission, NSWIC does not believe enough evidence has been provided that would warrant a fundamental change in the way meter service charges are being set. We furthermore note that the ACCC's Draft Decision also lacks a solid explanation as to why such a change in methodology is necessary.

> **Without additional information and a comprehensive business case, NSWIC rejects the proposed charges and the methodology in full.**

We reiterate that the NSW metering scheme is far from being determined and does not currently have universal support. Whilst metering standards have now been agreed upon, no product exists that complies with these standards. As such, a proposal to amend the current meter service charges and other charges associated with the scheme (i.e. telemetry) are significantly premature and should not proceed.

In relation to the metering standards, NSWIC vehemently disagrees with the ACCC's assessment that;

> *"The ACCC is satisfied that the interim metering standards provide sufficient certainty that meters installed will not need to be replaced before the end of their useful lives solely to comply with the national framework."* (p.240)

While NSWIC acknowledges that this is a possibility, this assessment is far from certain, given the duration and issues surrounding the NSW metering projects. NSWIC urges the ACCC to closely consult with our members on specific valley issues. Given the differences between valleys, NSWIC stresses that care must be taken not to impose a system on users that is neither efficient nor cost effective.

In addition to the uncertainty surrounding the current metering scheme, NSWIC questions the details in the ACCC's draft determination. In particular, we would like to seek clarification on the following;

- What are the meter service charges (if any) for customer who own their own meter? In addition, should no specific meter service charge be applicable to these customers, NSWIC requests that further information is provided what the embedded meter reading and maintenance charges are in the current proposed bulk water charges. Furthermore, NSWIC submits that the ACCC must provide detail on what services SWC will provide for customer owned meters and how those services have been factored into the Draft Decision.

- Are the metering service charges applicable for each meter or per site. As insufficient information is available in the ACCC draft decision, NSWIC would like to emphasise that certain properties will have a range of meters and hence should the charges be applicable on a 'per meter' basis, this could lead to significant cost increases for individual WAL holders and hence considerable price shocks.

Furthermore, NSWIC would like to seek clarification to the following;

> *On the basis of information available, the ACCC considers that State Water should be able to operate and maintain meters at a similar level of cost to that experienced in 2012-13 and 2013-4. The ACCC notes that State Water's current charges are still sufficient to recover operating and maintenance costs at an average cost per meter of $296*.

Whilst NSWIC agrees with the ACCC principle to maintain current cost allowance for operating and maintaining meters, NSWIC cannot find sufficient evidence what the ACCC's proposed charges will be for the next regulatory period. In addition, we would like to point out that the proposed charges on p.238 are in some instances significantly less than $296. We request that this possible inconsistency is investigated further.

<u>CBA of metering project</u>

NSWIC would like to voice its considerable frustration that (to date) no comprehensive cost benefit analysis has been undertaken that would assess the efficiency and effectiveness of the NSW metering project. While costs for the projects remain to be based on a small sample in the NSW Murray and NSW Murrumbidgee, NSWIC has not yet seen any evidence of SWC's proposed savings and benefits of the scheme. As a matter of urgency,

> **NSWIC submits that a thorough cost benefit analysis is undertaken that assesses the viability of the proposed metering project and scrutinizes the proposed charges.**

<u>Telemetry</u>

NSWIC has previously voiced its concern about the proposed telemetry charges proposed by SWC and accepted by the ACCC. In addition to the comments raised in our previous submission, we would like to point out that telemetry is not a component of the current metering standards and hence not a requirement. As such, NSWIC questions telemetry consideration in its entirety and urges the ACCC to reconsider its draft decision on the proposed charges.

In addition, NSWIC will stress that telemetry <u>should</u> lead to cost savings, however the currently proposed charges are completely contradicting this assumption as charges with telemetry are significantly higher than charges without telemetry. No evidence has been provided as to why such additional costs are necessary and why customers have to pay for telemetry whilst it is not a requirement under the standards.

> **NSWIC submits that telemetry is not part of the current metering standards and should not be considered under the review of SWC's bulk water charges.**

<u>RAB</u>

As NSWIC has outlined on multiple occasions, we hold significant reservations about the entire metering project, however we are particularly concerned that if no solid cost benefit analysis on the NSW metering project is conducted, SWC's asset base could be artificially inflated. Based on SWC's estimate, the NSW metering project will significantly grow over the next determination which will considerably add to SWC's asset base. Without consideration of the prudent and efficient cost of such a project, NSWIC is extremely concerned that customers will not only be asked to pay higher meters service charges but also continuously pay a return on and depreciation of SWC's meter who might or might not constitute a prudent and efficient investment.

Chapter 10 - Form of Price Control

NSWIC welcomes the ACCC's Draft Decision to maintain the current price cap approach. As we have outlined in our previous submission, we rejected SWC's proposed revenue cap approach on the basis that it would lead to considerably greater uncertainty and risk for customers.

We do not however agree that SWC bears the full volume related revenue risks as suggested on p.254. As we have outlined in our previous submission to the ACCC, the volumetric risk is already mitigated through the current (and proposed future) tariff structure. As 40 per cent of SWC's future revenue will be recovered through fixed charges (which are independent on future water availability), we consider it unjustified that the ACCC suggests that volumetric risk lies with SWC alone under a price cap approach. NSWIC would like to remind the ACCC that SWC's customers do NOT have access to a similar risk protection mechanism.

However, NSWIC notes that the ACCC proposes two alternative approaches to account for any variations in SWC's actual revenue (compared to its allowed revenue). The proposed 'overs/unders' mechanism and the 20 year rolling average approach will increase price volatility and hence transfer additional risk to customers. The two mechanisms will also reinforce each other with the result that prices will increases at times when WAL holders can least afford it. Also, the two mechanisms will make it virtually impossible for WAL holders to predict future prices and hence plan accordingly. We consider this to be of great importance since the ACCC's pricing principles state;

> *"..the decision in applying a form of price control will largely reflect a decision about achieving revenue stability for the operator and price stability for the customers."*

NSWIC cannot see how the ACCC's proposed price control mechanism is able to fulfil the ACCC's pricing principle of 'price stability' for customers. In addition, the proposed price control mechanism will operate contrary to customer's cash flows which the ACCC acknowledged on p.255;

> *"Many of State Water's customers are likely to have cash-flows which are positively correlated with water availability."*

The proposed new price control mechanism will cause prices to increases when cash flows of customers decrease. This could create additional financial hardship and is, in the opinion of NSWIC, a perverse and unintended pricing outcome. As such, we strongly disagree with the ACCC on its comment on p.257;

> *"We expect that the effect of the form of control will be that fewer changes to regulated charges will be necessary over a regulatory period."*

NSWIC believes that contrary to the ACCC's assessment, there will be more fluctuations in bulk water charges as a result of the ACCC's proposed price control mechanism.

> **NSWIC submits that the ACCC proposed 20 year rolling average approach create adverse pricing outcomes.**

Overs/Unders Account

NSWIC would like to point out that the balance in the 'overs/unders' account will be carried across to the next determination. As such, there are significant risks that the balance in the account will significantly grow should we experience another prolonged dry period. This build-up could lead to significant price fluctuations in later years.

For equitable reasons, NSWIC would like to also point out that the significant OVER-recovery in 2013-14 is not being accounted for in the next determination. NSWIC considers this inequitable and proposes an adjustment of future revenue requirement based on the over-recovery achieved by SWC in this last year of the current regulatory period.

> **NSWIC submits that the balance in the proposed overs/unders account could lead to significant price volatility.**

Chapter 11 - Cost Share Approach

As outlined in our previous submission to the ACCC, we welcome the NSW Government commitment to maintain current cost share ratios over the next regulatory period.

However, NSWIC is concerned that the current cost shares proportion applicable to the MDBA and BRC charges will not be carried over into the next determination, as the NSW Government has indicated to stakeholders that NSW's MDBA and BRC charges will likely increase. Whilst the NSW Government indicated that the current $8.9 million in MDBA contribution will continue to be split between the NSW Government and bulk water users, we have not received a guarantee that any additional contributions by NSW will also be subject to the cost share arrangements. This is a significant concern to bulk water users in NSW and could create significant cost increases for SWC's customers. NSWIC urges the ACCC to address this issue and ensure that bulk water users will not experience a significant price shock as part of the next determination.

Aside from NSWIC continuous request for an efficiency assessment of MDBA and BRC charges, we note that IPART has previously imposed an efficiency divided on SWC's MDBA and BRC charges.

> **We submit that the ACCC applies a similar cost share methodology to any additional MDBA and BRC charges to ensure no price shocks.**

In addition, we are deeply concerned about the recovery mechanism for MDBA and BRC charges. As the ACCC Draft Determination states,

> *"The full revenue shortfall is recovered in the subsequent year."*[7] (emphasis added)

This means that in addition to the disproportional cost burden that SWC's customers will bear for MDBA charges, the 'unders' and 'overs' mechanism could lead to significant price shocks. NSWIC rejects such an approach and submits that the balance in the 'overs' and 'unders' account for MDBA and BRC charges has to be weighted by the WACC. Such an approach aligns with the cost recovery approach of bulk water charges in general.

> **We submit that the ACCC applies a weighting (WACC) to the balance in the 'overs' and 'unders' account for MDBA and BRC charges.**

[7] P. 266 of ACCC Draft Determination