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Submission to

Australian Competition and Consumer Commission

State Water Corporation

Pricing application to the Australian Competition and Consumer Commission for regulated charges to apply from 1 July 2014

130913

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 community 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 advice to all stakeholders and decision makers.

This submission represents the view of the Members of NSWIC in respect to State Water Corporation's (SWC) pricing application to the Australian Competition and Consumer Commission (ACCC) for regulated charges to apply from 1 July 2014. 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.

Contents

Compliance with Consultation Expectations

In March 2009, in response to the growing number and complexity of consultation processes, NSWIC adopted a policy outlining the expectations of industry in this respect. The policy is appended to this submission. All consultation processes in which NSWIC participates are evaluated against this policy.

We assess this consultation as *indirect* and encourage the Commission to ensure that individual irrigators, together with representative groups, have access to the process.

Our policy requires consultation to proceed through five stages.

I. *Identification of problem and necessity for change*

Unsatisfactory. NSWIC was entirely comfortable with the IPART model and, indeed, the Determination last made under it. No case has been made for change of regulator and, in particular, no case has been made for the fundamental shift in pricing structure.

II. *Identification of solutions and proposed method for implementation*

This process must occur subsequent to the close of submissions.

III. *Summary of submissions, identification of preferred approach*

This process must occur subsequent to the close of submissions.

IV. *Explanation of interim determination and final feedback*

This process must occur subsequent to the close of submissions.

V. *Publication of final determination*

This process must occur subsequent to the close of submissions.

General Comments

New South Wales Irrigators' Council (NSWIC) is pleased to finally be given the opportunity to respond to State Water Corporation's submission to the Australian Competition and Consumer Commission (ACCC) on bulk water pricing 2014 - 2018.

We had anticipated receiving SWC's submission shortly after the original 1 May 2013 deadline and were disappointed that the process was delayed by two months. NSWIC is a relatively small organisation that had arranged resources to deal with this process in the originally identified timeline. No notification was provided as to the length of the delay. The timeframe for submissions was not extended leaving our process squeezed. We note that this problem will exist for all stakeholders.

The importance of the original deadline is emphasized in this submission, as it was declared to be a key constraint for SWC to undertake further assessment, modeling and discussion based on constructive feedback presented by stakeholders prior to the finalisation of their submission. In particular, SWC continually refused to consider the analysis of a dual tariff structure model that would allow customers to choose one of two tariff structures which aligns with their underlying risk preferences. Instead, SWC - as a monopoly operator - simply rejected such a proposal on the grounds that insufficient time was available prior to submitting to the ACCC. In light of the significant delay in SWC's submission to the ACCC, such a response is clearly unjustified and seem to suggest that rather than a lack of time, there was a considerable lack of willingness by SWC to consider such an option.

NSWIC acknowledges that the Determination process for bulk water charges in NSW has fundamentally changed with the change in regulator from the Independent Pricing and Regulatory Tribunal (IPART) to the ACCC. However, NSWIC stresses that the underlying functions, services and operations of SWC have not changed as a result. This fact is of crucial importance for several aspects of SWC's submission to the ACCC.

In the first instance, SWC seeks a fundamental change in the manner in which bulk water charges are set in NSW. While such a proposal is not novel to NSWIC and its Members, we have found no corresponding evidence in SWC's submission that would demonstrate that such a change is necessary. The current fixed and variable tariff structure split is widely understood by SWC's customers and has provided SWC with a positive net profit over the current and previous Determination periods. This result suggests that, far from being broken, the current tariff structure is highly effective and should therefore be maintained. In addition, NSWIC is concerned that SWC has deliberately used the ACCC's Pricing Principle to advance their own interest and consequently proposed to shift the vast bulk of their business risk to customers, who are - by definition - most vulnerable.

On this point, NSWIC notes ACCC Chairman Rob Sims in his speech to the University of Wollongong (23 February 2012);

> *"...that we regulate for reasons for allocative efficiency, or to reduce dead weight loss. That is, the higher prices charged by the unregulated monopolist will see some customers who would have used the facility at efficient prices now choosing not to do so."*[1]

[1] http://www.accc.gov.au/system/files/Infrastructure%20-%20why%2C%20when%20and%20how%20to%20regulate.pdf

NSWIC submits that customers of SWC are not given a choice on whether to utilise SWC's facilities and pay SWC's charges as these charges are intrinsically linked to customer's Water Access Licenses. The only option available for SWC's customers is to sell their entitlements which would have a large scale impact on irrigated agricultural production in NSW. In short, we are bound to SWC as a monopoly operator. Their shift of risk to us is classic monopoly behavior which IPART has consistently rejected. We submit that the ACCC must do the same.

Gary Banks, former Chairman of the Productivity Commission said;

> *"The Commission sees a continuing role for pro-competition regulation of monopoly infrastructure to curtail abuses of market power and enhance economic welfare."*[2]

NSWIC believes that this comment clearly justifies the need for adequate regulation of a monopoly operator and that scope exists for a monopoly operator to exercise market power. We hold the opinion that SWC has exercised its market power, as a monopoly operator, with its proposal to amend the current tariff structure and shift its business risk to customers.

Further, SWC seeks a considerable increase in its required revenue for the next Determination period. NSWIC considers such increases excessive and claims that no substantive explanation is being provided by SWC that would justify such a significant change in revenue requirement. To the contrary, SWC itself suggests that *"(...) this submission is dominated by maintaining assets and services to deliver business as usual.*[3]" In addition, NSWIC submits that over the current Determination period SWC has so far, significantly under-spent ($67 million) on its allowed capital expenditure. We hold significant doubts over SWC's ability to fulfill its forecast CAPEX in the last year of the Determination which is projected to be 40 per cent higher than in the 2012-13 financial year.

SWC seeks to dispose of the current price cap approach which has provided transparency and certainty to SWC's customers. Instead, SWC proposes to implement a revenue cap approach with an annual price adjustment of 15 per cent. Furthermore, SWC seeks to instigate a carryover methodology that would allow any deficit or surplus from the Determination period to be carried forward into the next Determination. NSWIC opposes this move, making several submissions herein to counter this argument. We will note that the current approach has served both customers and SWC well in previous Determinations, underscoring our submission that no fundamental necessity for change has been identified.

SWC seeks an increase in the weighted average cost of capital (WACC) based on their interpretation of the ACCC Pricing Principles. NSWIC opposes such an increase and will propose the alternative approach contained in our submission that we submit will better reflects the ACCC Pricing Principles.

SWC seeks a significant increase in the metering service charges in the absence of complete and accurate actual operating and maintenance costs. In addition, NSWIC highlights that the current metering program is far from being determined and does not have universal support among customers. We reject such a proposal based on a lack of evidence. We submit that further investigation must be made into the true costs of

[2] http://www.pc.gov.au/annual-reports/annualreport0001/mediarelease
[3] Page 9, SWC submission to ACCC

operation and maintenance of meters and telemetry networks before a change to the methodology and charges can possibly take place.

Irrespective of SWC's submission to the ACCC, NSWIC would like to emphasize that we have continuously supported SWC's corporatisation and that we recognize the need for SWC to be a commercially viable operation. We also continue to support SWC's focus on the improvement of customer services and information.

As the balance of this submission addresses the submission of SWC, we advise that it must be read in conjunction with the SWC submission. Page and chapter numbers referred to in this submission are derived from the SWC submission.

Summary of Submissions

Chapter One

NSWIC submits that SWC proposal would cause greater risk, more uncertainty and likely higher costs for customers over the next Determination period without adequate compensation.

NSWIC submits that SWC's submission lacks considerable detail and transparency with respect to future operational expenditure.

NSWIC welcomes the removal of MDBA and BRC charges from SWC's bulk water charges.

NSWIC submits that the ACCC reject the proposal to roll meters into RAB and request more detail on costs and progress of the metering program.

NSWIC submits that SWC's WACC is recalculated to incorporate more realistic financial variables.

NSWIC submits that the proposed charges for the coastal valleys should be removed from SWC's submission as they are irrelevant for the analysis.

NSWIC submits that the proposed tariff structure change will have a significant financial impact on customer in case of low water availability.

Chapter Two

NSWIC submits that SWC quotes the value of its regulated asset base as the value of its asset portfolio instead of alternative calculations that are not further explained in SWC's submission.

Chapter Three

NSWIC submits that SWC proposed cost increases are unjustified and that SWC should make its efficiency gains and potential cost savings (over the current Determination period) available in order to better assess the proposed future revenue requirements.

NSWIC submits that the ACCC examine the expense associated with servicing "non paying" customers and remove this from charges levied against "paying" customers.

Costs associated with new Water Resource Plans should be excluded either as they belong in the next Determination period or because they are not the responsibility of SWC.

Costs associated with the Murray-Darling Basin Plan are to be met by the Federal Government and must be removed from the submission of SWC.

The reduction in key performance indicators must lead to measurable efficiency gains that will translate into cost savings for both SWC and its customers.

Costs associated with the National Water Meter Standard should be postponed until such time as a product is developed that meets the current standard and an agreement has been reached on how to proceed with the current metering program.

Costs associated with ACCC compliance are outside customer control and should be funded by external sources.

NSWIC submits that insufficient information has been provided to assess the claimed efficiency and productivity gains. As such, NSWIC rejects the associated costs increases.

NSWIC submits that the ACCC request more detail on the key cost drivers that drive the overall cost increases incorporated in SWC's submission.

<u>*Chapter Four*</u>

NSWIC submits that SWC attempts to provide an indication of business performance in the current regulatory period that is significantly different from reality.

NSWIC submits that the current tariff structure has served both SWC and its customers well over the current and previous Determination period and has even lead to a $6.2 million addition revenue gain for SWC.

NSWIC submits that climate change is not a legitimate business risk over the next Determination period and should therefore be disregarded in the analysis.

NSWIC rejects SWC suggestion to amend the consumption forecast figures that they sought and were granted only four years ago.

NSWIC submits that SWC faces significantly less revenue risk than its customers, due to the current tariff structure.

<u>*Chapter Five*</u>

NSWIC submit that the OPEX from the current determination period are replicated with annual CPI adjustment minus an annual efficiency dividend.

NSWIC submits that a careful analysis on SWC's proposed OPEX must be undertaken before future increases are accepted.

NSWIC submits that the move toward international standards appears to have significantly increased costs for SWC and its customers without any corresponding benefits.

NSWIC submits that no adjustments are made to the current metering charges until such time as a product is being developed that meets the current metering standards.

NSWIC submits that any costs associated with the implementation of the Murray-Darling Basin Plan must be covered through Federal funding sources and not through bulk water charges levied on SWC's customers.

NSWIC submits that those projects within the environment planning and protection thematic expenditure budget that are as a result of state legislation ought be fully cost-attributed to the State Government.

Further, NSWIC submits that those projects within the environmental planning and protection thematic expenditure budget that relate to heritage matters must be considered a legacy cost where heritage assets were constructed prior to 1997.

NSWIC rejects environmental costs increases as a result of entitlement transfers to the Federal government. Should costs in this regard have eventuated, NSWIC submits that they are fully covered by the Federal Government.

NSWIC submits that the proposed OPEX for the development of CARM are postponed until such time as the benefits of such a model have been independently estimated.

NSWIC submits that OPEX for routine maintenance should be carried over from this determination with annual CPI adjustment minus an annual efficiency dividend as no evidence is provided that would warrant a 13 per cent cost increase.

NSWIC rejects the implementation of international standards for SWC's asset management as it causes a significant increase in costs without any evidence of any achieved benefits.

NSWIC submits that more detail is provided for the reason behind a proposed 10 per cent annual increase in SWC's OPEX for damn safety compliance.

NSWIC submits that the activities identified as 'corporate' are, in fact, standard operating procedures that are already represented within regulated OPEX. As such, we oppose increased OPEX for these programs.

NSWIC proposes that SWC must aim to maintain the previously achieved efficiency targets.

NSWIC submits that an external analysis of SWC's prudent and efficient operating and capital expenditure must be conducted prior to the next Determination.

<u>Chapter Six</u>

No submissions

Chapter Seven

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

NSWIC submits that the difference between allowed and actual CAPEX is deducted from the determined CAPEX in the next regulatory period.

NSWIC submits that SWC presents clarification whether the amendment to State Water's Operating Licence will financially impact State Water's investment projects under the CIP.

NSWIC submits that problems with the ICT program are outside customer's control and customers should not bear the costs of a failed program implemented by SWC.

NSWIC submits that future works in respect to the PRA project are covered through the difference between actual and allowed CAPEX in the current regulatory period.

NSWIC submits that no expenditure for environmental planning and protection be allowed without explicit directions from the Minister for Primary Industries.

NSWIC submits that any proposed expenditure for CARMS is postponed until uncertainties relating to external funding sources have been clarified.

NSWIC submits that any projects that are determined to lie outside the next regulatory period are postponed and that any associated costs are re-assessed in the following determination period.

Chapter Eight

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

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.

NSWIC submits that the proposed tripling of the RAB value in the last year of the current Determination must be regarded as a considerable price shock and cannot be accepted.

NSWIC submits that the approach to valuing RAB as proposed by IPART must be maintained.

In considering each of the WACC parameters - along with the overall consideration of whether to move the individual WACC parameter in this Determination - NSWIC submits that the ACCC must consider if a case for change has been made.

NSWIC submits that the current WACC of 7.4% must be maintained for SWC.

NSWIC submits that a post-tax WACC calculation will not disadvantage SWC as the business currently receives benefits through its tax deferral.

NSWIC submits that a WACC of 6.2 per cent is more appropriate for SWC.

<u>Chapter Nine</u>

NSWIC submits that the benefits of deferred taxes cannot be solely attributed to customers as SWC also benefits from deferring its tax expenses.

<u>Chapter Ten</u>

NSWIC submits that the proposed revenue requirements are compared with actual expenditures over the current Determination to highlight the significant increases that SWC is proposing.

NSWIC submits that SWC must provide a detailed outline of changes in revenue requirement in each valley based on the categories outlined in table 11.1

<u>Chapter Eleven</u>

No submissions.

<u>Chapter Twelve</u>

NSWIC rejects SWC's proposal to amend the current price control mechanism as it leads to greater uncertainty, less transparency, and likely greater price volatility.

<u>Chapter Thirteen</u>

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

NSWIC submits that 2013-14 consumption figures are included into the IQQM at the earliest possible date to provide customers with accurate and up-to-date information about their future bulk water charges.

<u>Chapter Fourteen</u>

NSWIC submits that the proposed regulated charges must be rejected given the underlying proposed price control mechanism and tariff structure design.

NSWIC submits that the proposed regulated charges can only be regarded as indicative as SWC's proposed price control mechanism could cause large fluctuations in these charges.

NSWIC submits that the current large customer rebates should be maintained as no evidence has been provided by SWC that a reduction to the economies of scale and system-wide benefits has occurred.

<u>*Chapter Fifteen*</u>

NSWIC submits that further investigations must be made into the true operational and maintenance costs of meters and telemetry networks before a change to the methodology and charges could possibly be considered.

NSWIC submits that no amendments to the current metering charges should be made until such time as meter standard compliant products are available.

NSWIC submits that SWC must remove any comments and proposed metering charges from its submission that are based on hypotheses.

Without any further information or a peer reviewed business case, NSWIC submits that the charges proposed in the 2010 determination should be maintained.

NSWIC submits that the objective of the metering program was to achieve efficiency gains and that the efficiencies must translate into lower costs for customers and/or improved service standards..

NSWIC submits that only factional costs can be considered in the pricing submission.

NSWIC submits that costs associated with Commonwealth-funded meters can outweigh the actual meter capital cost.

NSWIC vehemently reject SWC's suggestion to cross subsidise the telemetered metering solution costs.

NSWIC submits that no evidence has been provided that would justify an increase in staff based on the telemetered metering solution.

NSWIC rejects the proposed allowance for the telemetered metering solution cluster infrastructure given that these costs and the supposed benefits are far from certain.

NSWIC rejects the inclusion of an allowance for meter replacement costs. In addition we reject that any meter charges should enter the RAB.

<u>*Chapter Sixteen*</u>

NSWIC submits that that the temporary transfer charges under the current Determination are appropriate and should be continued.

<u>*Chapter Seventeen*</u>

No submissions.

Chapter One - SWC Summary of Application

While NSWIC will make a detailed submission to the points raised in Chapter One of SWC's submission, we considered there to be merit in providing a preliminary response to the following arguments;

Main Factors Influencing Charges

NSWIC does not concur with SWC's assessment on the proposed factors that influence charges over next Determination period. As we have highlighted at the beginning of this submission, we consider the proposed tariff structure change and the suggested amendments to the price control mechanism as being considerably more important than SWC's depreciation rate or the removal of Murray-Darling Basin (MDB) and Border Rivers' Commission (BRC) charges. Moreover, the two are simply not related.

The amendments to the manner in which charges are proposed to be set would cause significantly greater risk, more uncertainty and likely higher costs for customers over the next Determination period without any adequate compensation in the form of efficiency gains or greater service delivery. As such, NSWIC considers SWC's proposal as a blunt attempt to shift its business risk to customers and therefore rejects SWC's proposal on the grounds of customer protection.

> **NSWIC submits that SWC proposal would cause greater risk, more uncertainty and likely higher costs for customers over the next Determination period without adequate compensation.**

Increased Operational Expenditure

NSWIC submits that SWC has not provided sufficient evidence to justify the proposed 13 per cent average annual increase in operating expenditure across the Murray-Darling Basin valleys in NSW. Such an increase is particularly puzzling in light of SWC's comments that *"...this submission is dominated by maintaining assets and services to deliver business as usual*."[4]

There is a fundamental disconnect between SWC's assessment of 'business as usual' and the proposed expenditure figures.

In particular, the proposed operational expenses in certain valleys surpass greatly the overall expenditure increases of 13 per cent. The ACCC Information Paper clearly outlines that the proposed increases in operational expenses in the Macquarie valley are 19.1 per cent and arise from routine maintenance and water delivery operations[5]. In comparison, SWC outlines that the key 'Operating cost drivers' are metering and compliance costs, crop statistic data gathering as well as Murray-Darling Basin plan requirements[6]. NSWIC submits that there is a significant lack of detail provided by SWC to justify such a significant cost increase and that more transparency and explanation must be provided in order to assess the overall proposed cost increases.

[4] Page 9, SWC submission to ACCC
[5] Page 54: Information paper: State Water 2014-17 Pricing Application
[6] Page 46 and 47, SWC submission to ACCC.

NSWIC submits that SWC's submission lacks considerable detail and transparency with respect to future operational expenditure.

MDBA and Border River Commission Charges

NSWIC welcomes the removal of fees associated with the Murray-Darling Basin Authority (MDBA) and Border Rivers' Commission (BRC) from SWC's bulk water charges. As we have outlined in our submission to the Independent Pricing and Regulatory Tribunal (IPART) on SWC's last price determination in 2010[7], NSWIC has always considered the process of recovering MDBA and BRC charges through SWC's bulk water charges to be an ill-suited process, and hence are pleased to see these fees removed from SWC's overall revenue requirement.

NSWIC welcomes the removal of MDBA and BRC charges from SWC's bulk water charges.

Lower Depreciation Values

While NSWIC understands that SWC will face lower depreciation values under an ACCC regulation, we submit that SWC intends to offset those lower depreciation values with additional depreciation requests under the metering program[8]. In particular, SWC proposes that the;

> "*meter replacement capital be rolled into the regulatory asset base and an annual allowance for the return on capital and return of capital (depreciation) for these meters be included in the meter servicing charges (MSC), rather than upfront capital costs*"[9].

NSWIC does not consider such an approach efficient or cost effective and submits that it must be rejected by the ACCC. In addition, NSWIC would like to point out that the ACCC Pricing Principles explicitly state that "assets that have been funded upfront by customers cannot enter the operator's RAB"[10]. These meters have not been funded by the operator and do not belong in their RAB. As there remains the possibility that meters will be owned by customers in the future, NSWIC urges the ACCC to disregard SWC's proposal and request more details on costs and progress of the metering program.

NSWIC submits that the ACCC reject the proposal to roll meters into RAB and request more detail on costs and progress of the metering program.

WACC

SWC has claimed that it will experience a reduction in the weighted average cost of capital (WACC) as a result of the WCIR and the ACCC Pricing Principles; however SWC's proposed WACC of 8.96 per cent is significantly higher than its current WACC of 7.4 per cent.

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[7] http://www.nswic.org.au/pdf/Submissions%20Archive/091023.pdf
[8] Page 167 and p. 177, SWC submission to ACCC.
[9] Page 177, SWC submission to ACCC
[10] Page 24, ACCC Pricing Principles

NSWIC rejects SWC's proposed WACC figure and questions the parameter specification based on internal analysis[11]. In response, NSWIC will propose alternate parameters that we consider to be more reasonable and closer aligned with worldwide standards in the electricity and water segment. According to a recently published report by Deloitte[12], international comparison has shown that world figures for WACC in the electricity segment range between 5.6 per cent and 5.9 per cent. Equivalent figures in the water segment outline that WACC values range between 5 percent and 5.3 per cent. Our calculations, which are included in a later part of this submission, will highlight that SWC's proposed WACC is significantly overvalued. As such, NSWIC submits that SWC's proposed WACC is rejected and instead a more realistic approach be implemented.

NSWIC submits that SWC's WACC is recalculated to incorporate more realistic financial variables.

Non-Basin State Inclusion

NSWIC considers the inclusion of non-Basin valley costs and revenues within the pricing submission to be irrelevant for this Determination process. A review of these charges will not commence until mid 2014, when further information will be available on OPEX and CAPEX of SWC.

In addition, NSWIC submits that the inclusion of those charges is highly unrealistic as such price increases would be financially detrimental to any Water Access Licence holder in these valleys and therefore lead to a wide-scale collapse of irrigated agriculture in the area.

NSWIC submits that the proposed charges be removed from SWC's submission until such time as SWC makes a submission to IPART on the Determination of bulk water charges in coastal valleys.

NSWIC submits that the proposed charges for the coastal valleys should be removed from SWC's submission as they are irrelevant for the analysis.

Indicative Bill

NSWIC submits that the indicative bills on page 4 and 5 of SWC's submission do not adequately illustrative the proposed changes in total costs over the next Determination as the figures for the 2014 financial year are inclusive of MDBA and BRC charges whilst the values for the 2015 - 2017 financial year are not. NSWIC suggests that the removal of the MDBA and BRC charges have likely contributed significantly to the overall percentage changes outlined in the last column of table 1.1, 1.2 and 1.3.
In addition, NSWIC is extremely concerned that the indicative bills do not provide a comparison between current bulk water costs and proposed future costs in case of low water availability. In our submission, this lack of information is designed to be deliberately misleading.

A comparison of total costs in such a scenario is particularly important as it outlines the greatest risk that Water Access Licence holders in NSW will be subjected to under SWC's

[11] Page 97 , SWC Submission to ACCC
[12] http://www.deloitte.com/assets/Dcom-Italy/Local%20Assets/Documents/Pubblicazioni/survey%20panel%20energy_ENG_bassa.pdf

proposal. As SWC has itself claimed, there exists the possibility of prolonged drought periods[13] and hence NSWIC had expected that SWC provide an indicative customer bill that outlines the changes in costs if water availability is low.

To illustrate the financial risk that SWC is proposing to impose on its customers, NSWIC has prepared two representative customer bills. The first table compares the current total costs (2013-14) for a high security customer and a 500 ML entitlement and a 20 percent usage with the total costs under the same scenario in 2014-15 to 2016-17. As the table highlights, the total costs for a high security customer will significantly increase in most valley should water availability be low.

Example 1:

	13-14	14-15	15-16	16-17
Border	$ 6,668.00	$ 2,718.00	$ 2,687.00	$ 2,666.00
Gwydir	$ 8,572.00	$ 5,670.00	$ 7,045.00	$ 8,556.00
Namoi	$ 10,108.00	$ 9,278.00	$ 10,930.00	$ 12,599.00
Peel	$ 16,756.00	$ 26,249.00	$ 31,404.00	$ 37,073.00
Lachlan	$ 7,984.00	$ 8,105.00	$ 10,127.00	$ 12,409.00
Macquarie	$ 7,108.00	$ 6,678.00	$ 8,483.00	$ 10,561.00
Murray	$ 2,087.00	$ 1,166.00	$ 1,349.00	$ 1,526.00
Murrumbidgee	$ 1,868.00	$ 1,811.00	$ 2,167.00	$ 2,521.00

Example 1: High Security Entitlement Holder (500ML) and 20% usage

The second table compares the current total costs (2013-14) for a general security customer with a 500 ML entitlement and a 20 percent usage and the total costs under the same scenario. As the table highlights, the total costs for a general security customer will increase even more in most valleys should water availability be low.

Example 2:

	13-14	14-15	15-16	16-17
Border	$ 2,548.00	$ 2,572.00	$ 2,237.00	$ 2,211.00
Gwydir	$ 3,327.00	$ 4,267.50	$ 4,290.00	$ 4,966.00
Namoi	$ 6,543.00	$ 8,812.00	$ 9,020.00	$ 10,239.00
Peel	$ 5,546.00	$ 13,946.00	$ 9,359.00	$ 8,348.00
Lachlan	$ 4,014.00	$ 5,295.00	$ 4,947.00	$ 5,559.00
Macquarie	$ 3,518.00	$ 4,972.00	$ 5,033.00	$ 5,941.00
Murray	$ 1,662.00	$ 1,104.00	$ 1,109.00	$ 1,241.00
Murrumbidgee	$ 1,173.00	$ 1,389.00	$ 1,417.00	$ 1,596.00

Example 2: General Security Entitlement Holder (500 ML) and 20 usage

NSWIC submits that the proposed tariff structure change will have a significant financial impact on customer in case of low water availability.

[13] Page 136 and 137, SWC submission to ACCC

Chapter Two - Summary of Operations

NSWIC welcomes the intent of SWC to exhibit a sense of social responsibility by having regard to the interests of the community in which it operates. This however seems to be contradicting the fact that SWC intends to shift a significant business risk from SWC to its customers who form the basis of that community.

NSWIC rejects the SWC claim that its asset portfolio is worth $3.6 billion (based on the modern engineering replacement asset value) and instead requests that SWC quotes the value of its regulated asset base as the value of its portfolio.

> **NSWIC submits that SWC quotes the value of its regulated asset base as the value of its asset portfolio instead of alternative calculations that are not further explained in SWC's submission.**

Chapter Three - Obligations and service standards

NSWIC notes that SWC proposes three cost driver categories in Chapter 3 being "business as usual", "new regulatory service" and "continuous improvement". We comment below on each category in turn.

Business as usual

NSWIC remains confused how to reconcile SWC's claim of 'business as usual'[14] while at the same time proposing significant increases in operational and capital expenditures in certain valleys. As details on the reasons behind the cost increases is not available from the submission, NSWIC submits that such cost increases either suggests a significant change in SWC's operation, or are unjustified. As nothing in the SWC's submission suggests that the underlying functions, operations and services of SWC have changed[15], NSWIC must deduce that the cost increases are unjustified and should not be accepted.

In addition, NSWIC notes that SWC declares,

> *"Its challenge is to deliver these duties with greater effectiveness and efficiency."* [16]

If SWC had achieved significant efficiency gains, NSWIC believes that this should have been reflected in a lower overall revenue requirement and/or improved levels of services. At this point, NSWIC is unable to assess any achieved efficiency gains or cost savings.

> **NSWIC submits that SWC proposed cost increases are unjustified and that SWC should make its efficiency gains and potential cost savings (over the current Determination period) available in order to better assess the proposed future revenue requirements.**

NSWIC also notes that SWC makes a short reference to its 'non-paying' customers. We consider it appropriate to provide more detail on this 'type' of customer and stress that their importance must not be underestimated. In our understanding, these 'non-paying' customers comprise of environmental managers who administer the 'environmental contingency allowances' and basic landholder rights. The environmental contingency allowances often make up a significant proportion of the water held in SWC's storage facilities. Environmental contingency allowances are currently not subject to SWC's bulk water charges, even though they receive the same benefits and services as other 'paying' customers. We regard this situation as a significant regulatory gap and urge the ACCC to consider this matter with focus on 'paying' customer impacts. We note that the costs associated with storing and releasing these environmental contingency allowances are currently born by Water Access Licence holders who do not receive a benefit from this particular service delivered by SWC. The same principle applies to basic landholder rights who currently receive benefits from SWC's services but do not pay for them.

> **NSWIC submits that the ACCC examine the expense associated with servicing "non paying" customers and remove this from charges levied against "paying" customers.**

[14] Page 9, SWC submission to ACCC
[15] Page 9, SWC submission to ACCC
[16] Ibid.

<u>New regulatory service obligation</u>

NSWIC submits that the proposed items in this category should either have no impact or reduce SWC's overall cost requirement.

- **Water Resource Plans**

  SWC proposes an increase in required revenue due to the implementation of the Water Resource Plans in 2019. NSWIC submits that the implementation of these plans lies outside the next regulatory period and given the uncertainty surrounding any possible changes, an estimation of required costs is unlikely to be accurate. We therefore propose that costs related to the new water resource plans are postponed until the next regulatory period when more information on possible changes is available. Further, these Plans are the responsibility of the NSW Office of Water as a regulatory authority and do not sit within the remit of SWC as an operator.

  > **Costs associated with new Water Resource Plans should be excluded *either* as they belong in the next Determination period *or* because they are not the responsibility of SWC.**

- **Murray-Darling Basin Plan**

  NSWIC rejects SWC's proposal to impose costs on customers for the implementation and/or interpretation of the Murray-Darling Basin Plan[17]. These costs as well as any other costs associated with the Murray-Darling Basin Plan are to be covered solely by the Federal Government and not by customers of SWC.

  > **Costs associated with the Murray-Darling Basin Plan are to be met by the Federal Government and must be removed from the submission of SWC.**

- **Key Performance Indicator**

  NSWIC welcomes the amendments to SWC's Operating Licence which will decrease the number of key performance indicators against which SWC will have to report. We expect that this change will bring efficiency gains which will translate into cost savings for both SWC and its customer. We will monitor this development closely to ensure that those efficiency savings will occur.

  > **The reduction in key performance indicators must lead to measurable efficiency gains that will translate into cost savings for both SWC and its customers.**

[17] Page27, SWC submission to ACCC

- **National Water Meter Standards**

  NSWIC submits that SWC's proposal to acquire specialist staff to manage the metering and compliance data is significantly premature. Whilst metering standards have now been agreed upon, we would like to highlight that there is currently no pattern approval in existence. As such, meters that are currently being installed (and are proposed to be installed over the next regulatory period) are not guaranteed to be compliant. As the current metering program is far from being determined, NSWIC submits that no technical staff should be employed prior to having a product that meets the agreed standards.

  > **Costs associated with the *National Water Meter Standard* should be postponed until such time as a product is developed that meets the current standard and an agreement has been reached on how to proceed with the current metering program.**

- **ACCC compliance**

  NSWIC remains concerned about SWC's proposed costs associated with the change in regulator from IPART to the ACCC. As SWC outlines in section 3.2.1,

  "This also requires changes to State Water's business function and processes to comply with ACCC rules which differ to IPART." [18]

  In addition, SWC declares that;

  "Increased regulatory costs, driven by the ACCC acquiring powers to regulated State Water's bulk water charges in the Murray Darling Basin. This includes $250,000 in 2014-15 to develop a tax asset base."[19]

  NSWIC submits that the SWC's proposed revenue requirement for the development of a tax base is highly ambiguous and not supported by solid evidence. In particular, NSWIC questions the difference in compliance requirements under IPART and the ACCC. For that reason, we urge the ACCC to thoroughly assess the efficiency and cost effectiveness of the proposed charges.

  We further stress that the change of regulator was outside customer's control. Customers of SWC did not request such a change and will be disadvantaged if the ACCC accepts SWC's proposed cost increases.

  > **Costs associated with ACCC compliance are outside customer control and should be funded by external sources.**

Continuous improvement

The irony of demanding revenue increases to support continuous improvement is not lost of NSWIC. We submit that genuine continuous improvement is intrinsically linked to operational efficiency which ought result in required revenue *decreases*.

[18] Page 26, SWC submission to ACCC
[19] Page 45, SWC submission to ACCC

Whilst NSWIC supports SWC's commitment to continuous improvement, we remain doubtful as to how SWC's *"(...)business transformation program (BTP) and metering program will work together to enhance levels of service, increase reliability and promote productivity across NSW."*[20]

Without proof on how SWC intends to achieve the claimed productivity gains, NSWIC remains doubtful whether the benefits of the proposed projects outweigh the costs.

In particular, NSWIC would like to stress that the benefits of Computer Aided River Management (CARM) have not been agreed upon. NSWIC requests that a business case be developed that assesses the costs and benefits associated with CARM before further CAPEX and OPEX costs are dedicated to such a project.

> **NSWIC submits that insufficient information has been provided to assess the claimed efficiency and productivity gains. As such, NSWIC rejects the associated costs increases.**

While NSWIC does not underestimate the importance of the points mentioned above, we submit that the overall cost drivers for the next regulatory period are not present in this category. For that matter, we strongly urge the ACCC to demand further detail from SWC on the main cost drivers. In particular, we request that the ACCC questions why such large cost increases are necessary in light of record water releases this year.

> **NSWIC submits that the ACCC request more detail on the key cost drivers that driver the overall cost increases incorporate in SWC's submission.**

[20] Page 28, SWC submission to ACCC

Chapter Four - Financial Position

Past and current regulatory period outcomes

SWC suggests to the ACCC that they *"will fully recover their allowed revenue requirements for the first time since corporatization in (2012-13)"*[21] and that *"under-recovery of revenue amounted to $79.1milllion over the previous regulatory period"*[22]. SWC uses this argument as evidence that a change in tariff structure is warranted.

NSWIC notes that SWC used exactly the same argument at the last Determination before IPART to request that it dramatically alter its demand forecasting model. The request was allowed, the model was changed and the revenue forecast was met. SWC now wants to double dip by using the same (now solved) problem to shift risk to its customers.

NSWIC submits that the focus should not be on whether SWC has met its allowed revenue requirement but whether SWC was able to generate a net profit from its operation. We note that SWC has returned a positive net profit before tax over the current and previous Determination period based solely on actual revenue, despite the fact that the previous determination included the worst drought on records[23]. In 2012-13 alone, SWC was able to generate a $50 million net profit before tax and it is forecast that this situation will continue over the entire next Determination period, albeit at a slightly lower level[24].

In addition, NSWIC emphasizes that the last two years (2011 - 2013) have been marked by significant increases in water availability across NSW which has led to record water releases by SWC in 2012-13. This has generated revenue in excess of the IPART allowed revenue allowance - in the order of $6.2 million[25].

NSWIC is particularly disappointed that SWC attempts to claim a shortfall in revenue of $79.1 million when only a comparison between allowed and actual revenue is being presented. We submit that such an analysis is misleading and does not show the full picture of profitability of SWC. In order to assess the profitability of SWC, a full analysis between actual costs and revenues must be presented.

> **NSWIC submits that SWC attempts to provide an indication of business performance in the current regulatory period that is significantly different from reality.**

NSWIC also notes that SWC attempts to blame the current tariff structure as a reason for a shortfall in notional revenue, whilst failing to mention that the current tariff structure has led to a windfall gain of $6.2 million in 2012-13.

> **NSWIC submit that the current tariff structure has served both SWC and its customers well over the current and previous Determination period and has even led to $6.2 million additional revenue gain for SWC**.

[21] Page 33, SWC submission to ACCC
[22] Page 33 and 34, SWC submission to ACCC
[23] Page 120, SWC submission to ACCC
[24] Page 120, SWC submission to ACCC
[25] Page 34, SWC submission to ACCC

Business Risk

In this section, SWC provides an analysis of the underlying risks faced by the business presumably to support the request for a change in tariff structure. This section does not, however, provide advice on what has changed so dramatically from previous Determinations as to warrant a fundamental shift in how bulk water charges ought be set in this Determination. Nor does it address the fundamental change to demand forecasting allowed in the last Determination. To the contrary, over the current determination SWC has generated a positive net profit and even surpassed its notional revenue by $6.2 million in 2012-13.

SWC argues that it is *"exposed to significant revenue risk relating to water sales volume, uncertainty and volatility"*[26]. We do not disagree with such an assessment however, we submit that the form of regulation that is currently in place - the setting of an effective minimum revenue stream - overcomes the volumetric risk. Additionally, NSWIC submits that SWC's customers are exposed to the same risk without any compensated minimum revenue stream or geographical diversity to offset localised water shortages.

SWC claims that volumetric risk exists on both the supply and demand side. We concur with SWC on the point that water supply is variable and that SWC and its customers are exposed to supply side risk. However we do not agree that demand side risk is relevant in a price Determination as it is merely a cap on upper level profits. Moreover, the increased use of carry-over and the continuous accounting practices in the northern NSW valleys have in recent years provided protection to SWC against the variance in demand.

In addition, SWC further argues that demand side risk is caused by agricultural input costs and commodity prices although no evidence in support of this claim has been advanced by SWC. Whilst NSWIC acknowledges that volatility in commodity markets has indeed been a feature of the previous Determination, there is not sufficient evidence to suggest that markets will remain as volatile in the next regulatory period. Further, commodity price fluctuation merely determines *what* a farmer will grow, not *whether* they will grow. In our submission, commodity prices are not linked to demand for water unless moving in concert.

Long-term supply uncertainty

NSWIC does not agree with SWCs argument that a 'further volume risk' relates to long term supply uncertainty[27]. Without any further evidence, NSWIC rejects the suggestion that further risk is imposed on SWC over the next Determination on the ground of climate change. Whilst the fundamental of long term climate change or variability may exist, it most certainly does not in the next four years. As the last two years have shown, water supply in Australia is highly volatile and not correlated with water supply in previous periods. As such, NSWIC strongly rejects SWC's claim that SWC is exposed to risk arising from climate change and hence requires an amendment to its current tariff structure.

> **NSWIC submits that climate change is not a legitimate business risk over the next Determination period and should therefore be disregarded in the analysis.**

[26] Page 35, SWC submission to ACCC
[27] Page 36, SWC submission to ACCC

Furthermore, NSWIC notes that SWC attempts to use the argument of climate change to further lower the consumption forecast figures. The model that SWC presented and had endorse four years ago was designed to do exactly that. No evidence is provided that suggests the recently endorsed model was wrong. NSWIC submits that the problem has been addressed in the manner that SWC sought and does not need to be reconsidered.

NSWIC emphasizes that we have continuously supported the use of the full IQQM dataset for demand forecasting instead of a 20-year rolling average that was granted at the last Determination. As the last two years have shown in particular, water availability in NSW is highly variable and the full IQQM dataset captures this variability with much more accuracy than the 20-year rolling average approach.

> **NSWIC rejects SWC suggestion to amend the consumption forecast figures that they sought and were granted only four years ago.**

Revenue volatility risk

As outlined at the onset of this Chapter, NSWIC is disappointed that SWC attempts to blame the current tariff structure for current shortfalls in allowed revenue (emphasis added) over the current Determination period. Not only has SWC achieved a positive net profit but the current tariff structure has also enabled SWC to surpass their notional revenue requirement by $6.2million in 2012-13. In addition, the current tariff structure enables SWC to achieve a base revenue, irrespective of water availability, which is a feature that is not available to SWC's customers.

> **NSWIC submits that SWC faces significantly less revenue risk than its customers, due to the current tariff structure**.

In addition, NSWIC notes that SWC's key financial indicators in table 4.3. provides clear evidence that SWC was able to generate a positive return on its assets and its equity over the current determination in addition to a positive net profit overall. NSWIC submits that these indicators show more accurately the financial viability and profitability of SWC

Business risk and future regulatory outcomes

NSWIC considers SWC analysis of its credit rating as being skewed given SWC's assumption of a WACC value of 8.96%. As we will outline later in this submission, NSWIC considers such a WACC to be significantly inflated, in particular if any of SWC's price control proposals are being accepted.

Chapter Five - Operating Expenditure

NSWIC is concerned at the significant increases in proposed operational expenditure (OPEX) over the next determination period. As outlined in Table 5.1, SWC suggests a near $5 million dollar increases in OPEX between 2013-14 and 2014-15 alone and proposes to maintain such elevated levels over the entire next regulatory period, albeit at slightly lower absolute totals. As the ACCC Information Paper outlines, SWC's proposal constitutes a proposed average annual increase of 13% in real terms whereby the actual increases within particular valleys are significantly higher[28].

NSWIC is unaware from the submission of SWC how or why its operations have changed that significantly - if at all - to warrant such large price increases. SWC has itself outlined on multiple occasions (page 9 and 100) that its operation and risk have not fundamentally changed and hence there are no reasons to suggest that a significant change in OPEX is justified.

> **NSWIC submit that the OPEX from the current determination period are replicated with annual CPI adjustment minus an annual efficiency dividend.**

In addition, NSWIC requests more detail on the proposed cost increases for all thematic expenditure items, in particular "water delivery and other operational" (proposed average annual increase of around 20%) and "routine maintenance" (proposed average annual increase of around 24%). We reiterate that the submission of SWC does not identify what would drive such large cost increases if the business operations, services and objectives of SWC have not altered.

Furthermore, we note that the more recent water year has led to significant water releases by SWC which have generated considerable revenue gains for the business. We request an explanation as to how SWC's considers its operation to differ to the current year.

As such, NSWIC is content to endorse continuing of the baseline OPEX pursuant to the current Determination, but is not convinced that an increase of 13% average annual increase is justified.

<u>Key drivers of change</u>

NSWIC questions the proposed tripling of wage growth over the next Determination which are exactly offset by additional efficiency savings related to business systems[29]. We note that SWC has not advanced an explanation on this point and we therefore urge the ACCC to carefully consider SWC's proposal.

> **NSWIC submits that a careful analysis on SWC's proposed OPEX must be undertaken before future increases are accepted.**

In addition, NSWIC has continuously warned about the additional costs of moving towards international standards. Table 5.2 clearly confirms our concerns in that significant cost increases are being proposed in respect to environmental planning and protection, asset

[28] Page 26, Information paper: State Water 2014-17 Pricing Application
[29] Page 45, SWC submission to ACCC

management planning and corporate systems. NSWIC has stressed in its submission to IPART[30] that a cost benefit analysis should precede any further consideration about implementing international standards for SWC. We have so far not been able to assess the benefits of moving to the proposed international standards, while we see evidence that the associated costs are significant.

NSWIC submits that the move towards international standards appears to have significantly increased costs for SWC and its customers without any apparent corresponding benefits.

As NSWIC has outlined previously in this submission, we hold considerable doubt over the proposed operational costs in relation to moving regulation to the ACCC. We consider the ACCC to be the most appropriate body to assess whether the $250,000 costs is justified for the development of a tax asset base and again emphasize that such a move was not requested by customers who appear to pay as a consequence.

Operating cost drivers

NSWIC submits that the lack of detailed information relating to operational cost drivers prevent stakeholder's commenting in detail on the proposed cost increases. Nevertheless, NSWIC makes the following points in response to SWC's submission;

- Metering and compliance

  NSWIC submits that the current metering program is neither determined nor has universal support. With standards been agreed upon in the absence of a product being designed that meets those standards, we object to the significant cost increases in this 'thematic' expenditure item.

  We consider it appropriate that any proposal that aims at changing the metering charges and methodology for how those charges are being set, be put on hold until such time as a meter standard compliant product can be developed, tested and assessed. Without such a product, costing of the program can only be regarded as indicative and possibly significantly biased.

  In addition, NSWIC notes that SWC has itself stated that the NSW Metering Project is still in "its infancy, (and hence) complete and accurate actual operating and maintenance costs were not available"[31].

  NSWIC is not content to fund the operating expenditure for a product that is not yet developed, nor tested and hence, cannot be priced. We urge the ACCC to apply strict scrutiny to SWC's proposed costs in respect to metering. In the interim, we submit that no adjustment be made to the current metering charges.

  NSWIC submits that no adjustments be made to the current metering charges until such time as a product is being developed that meets the current metering standards.

30

31 Page 166, SWC submission to ACCC

- Crop Statistics

  While NSWIC disputes this proposed cost item, we consider it appropriate that the ACCC consult with NSWIC Members in the Lachlan and Border River[32] valleys on this proposed cost item.

- Murray Darling Basin Plan

  NSWIC rejects any proposed cost increases that relate to the implementation of the Murray-Darling Basin Plan. Given it is a Federal commitment that any costs associated with the Murray-Darling Basin plan are funded through federal sources, we are not content to accept a cost burden being imposed on SWC's customers in this respect.

  NSWIC submits that any costs associated with the implementation of the Murray-Darling Basin Plan must be covered through Federal funding sources and not through bulk water charges levied on SWC's customers.

Environmental planning and protection

NSWIC notes that SWC proposes an average annual increase of 3 to 4 per cent for this thematic expenditure item without providing sufficient information on detailed programs that SWC plans to implement. Nevertheless, NSWIC makes the following submissions:

> **NSWIC submits that those projects within the environment planning and protection thematic expenditure budget that are as a result of state legislation ought be fully cost-attributed to the State Government.**
>
> **Further, NSWIC submits that those projects within the environmental planning and protection thematic expenditure budget that relate to heritage matters must be considered a legacy cost where heritage assets were constructed prior to 1997.**

Water delivery and other operations

NSWIC notes that the average extraction value of 4300GL will likely increase with the inclusion of the last water year. NSWIC submits that these figures should be included in the current estimates to provide a more accurate representation of actual average water extraction.

NSWIC also emphasizes that the proposed cost increases for this thematic expenditure item lies in the magnitude of nearly 20%. Whilst insufficient information is provided in the SWC submission, we are concerned that the proposed cost increases are associated with the Murray-Darling Basin Plan and the Commonwealth Environmental Water Holder.

[32] Lachlan Valley Water Users Association and Border Rivers Food and Fibre respectively.

As SWC outlines,

> *"(...) with the implementation of the Murray Darling Basin plan the environment as a water customer has become far more prominent. This has resulted in greater stress on the operators in the valley due to the new requirements of this user. "* [33]

Whilst NSWIC acknowledge that the environment has been a major customer in the NSW Murray-Darling Basin, we object to the claim that this user holds different 'requirements' to other Water Access Licence holders. The entitlements that were transferred to the Federal Government maintain their original characteristics and it is for the environmental water holders to ensure that water that is used for the purposes of the environment reaches the environmental assets. As such, NSWIC rejects the claim that SWC's operating costs should increase as a result of water-entitlements being transferred to environmental water holders. In addition, we submit that should such cost increases eventuate, they should be paid exclusively by the Federal Government and not by SWC's other customers according to the beneficiary pay principle.

Further, the aggregation of entitlements to one user from multiple users ought result in cost efficiencies and savings that should be passed on to all customers.

> **NSWIC rejects environmental costs increases as a result of entitlement transfers to the Federal government. Should costs in this regard have eventuated, NSWIC submits that they are fully covered by the Federal Government.**

In addition, NSWIC cannot see the connection between the emerging challenges of environmental water releases and the necessity to develop the Computer Aided River Management river model (CARM). The significant OPEX and CAPEX costs proposed for CARM are not justified in NSWIC's opinion, especially given the absence of a rigorous business case being provided by SWC. Such an analysis would assess the accuracy and net benefits of such a model and also provide more detail on the proposed efficiency savings that are being proposed by SWC.

> **NSWIC submits that the proposed OPEX for the development of CARM are postponed until such time as the benefits of such a model have been independently estimated.**

<u>Routine maintenance</u>

SWC outlined that routine maintenance represents over 25 per cent of annual operating expenditure and is therefore the single biggest contributor to SWC's total operating costs. While NSWIC acknowledges the importance of routine maintenance, we consider it puzzling that SWC suggests a near 13% annual average increase in this thematic expenditure item, while at the same time declaring that "State Water's asset maintenance costs have been approximately $10 to $12 million per annum in recent years and remain approximately within this band over the next regulatory period."[34]

[33] Page 51 , SWC submission to ACCC
[34] Page 54, SWC submission to ACCC

Based on the comment above and other statements made by SWC within its submission, we assume that the underlying business operation of SWC have not significantly changed and hence operating cost changes in this magnitude are not justified.

> **NSWIC submits that OPEX for routine maintenance should be carried over from this determination with annual CPI adjustment minus an annual efficiency dividend as no evidence is provided that would warrant a 13 per cent cost increase.**

Asset management planning

NSWIC reiterates that we have continuously objected to the implementation of international standards for SWC's asset management. We continue to object to such a change and point to the significant cost increases that will be imposed on SWC's customers.

> **NSWIC rejects the implementation of international standards for SWC's asset management as it causes a significant increase in costs without any evidence of any achieved benefits.**

Dam safety compliance

As SWC proposes an annual increase of around 10 per cent in its OPEX for this thematic expenditure item, NSWIC request more detail on the proposed works. In particular, further information must to be provided on what costs are attributed to 'expert advice', 'surveying and mapping' and 'risk management drivers'.

> **NSWIC submits that more detail is required to justify a proposed 10 per cent annual increase in SWC's OPEX for dam safety compliance.**

Corporate systems

NSWIC recognises the need for the proposed projects, but we are unable to support additional OPEX for activities that must be categorised as standard operating procedure. The OPEX requirements that have previously been identified by IPART must have a discretionary component built in that allows funding of such projects.

> **NSWIC submits that the activities identified as 'corporate' are, in fact, standard operating procedures that are already represented within regulated OPEX. As such, we oppose increased OPEX for these programs.**

Operating efficiency targets

We congratulate SWC on achieving cost efficiency of 20.4% throughout the 2006 - 2010 regulatory period; however we question why SWC is only including a 1% efficiency target equivalent for the next regulatory period.

NSWIC proposes that SWC must aim to maintain the previously achieved efficiency targets.

In addition, NSWIC notes that IPART commissioned an external consultant report for the 2006 and 2010 Determinations to review SWC's prudent and efficient operating and capital expenditure[35]. NSWIC submits that a similar external analysis must be conducted for the next Determination.

NSWIC submits that an external analysis of SWC's prudent and efficient operating and capital expenditure must be conducted prior to the next Determination.

Major variances in operating expenditure for 2012-13

NSWIC further notes that SWC has not met its regulated OPEX over the last regulatory period. A further increase of 13% OPEX over the next regulatory period must be rejected and measures should be put in place to ensure that SWC continues to increase its efficiencies. For that reason, NSWIC proposes that the current regulated OPEX is maintained to ensure that SWC is indeed operating efficiently. As far as NSWIC can assess there have been no items outlined in SWC's submission that would indicate a significant change in SWC's business operation and hence no change to the current OPEX is warranted in NSWIC's opinion.

[35] Available under:
http://www.ipart.nsw.gov.au/Home/Industries/Water/Reviews_All/Bulk_Pricing/Review_of_Bulk_Water_Prices_to_be_charged_by_State_Water_Corporation_from_1_July_2010/23_Feb_2010_-_Release_of_Atkins_Cardno_Final_Consultant_Report/Final_Consultant_Report_-_Atkins-Cardno_-_Strategic_Management_Overview_and_Review_of_Operating_and_Capital_Expenditure_-_State_Water_Corporation

Chapter Six - Approach to cost allocation

NSWIC appreciates an overview of the methodology that SWC will utilize to distribute general business and corporate overheads as well as transfer to predefined assets/activities. We would however like to raise our concerns about the lack of detailed provided in Chapter 5 and 7 regarding the key drivers of OPEX and CAPEX.

We also note that SWC suggests that the basis for proposed CAPEX is payroll costs - i.e. indirect and direct salary component. Should this be the case, NSWIC had expected to see in greater detail how these payroll costs are proposed to develop over the next regulatory period. Such an overview would greatly assist in providing transparency for stakeholders and provide perhaps a better indication for the significant cost increases as they proposed by SWC.

Chapter Seven - Capital expenditure

NSWIC submits that the information provided by SWC lacks sufficient detail to allow for a comprehensive assessment of SWC's proposed capital expenditure. In the absence of this, NSWIC submits that the ACCC direct SWC to provide such information to an acceptable standard.

In addition, NSWIC holds considerable doubt over SWC's ability to deliver against its forecast capital expenditures in 2013-14 given that SWC has significantly under-spent over the first three years of the current Determination. NSWIC notes that similar forecasts were made during the last Determination, where major capital expenditures were proposed for the last year of the Determination and not met.

As the forecast capital expenditure in 2013-14 will influence the commencing RAB value in the next Determination, we submit that the opening RAB value be set at the end of the third quarter in 2013-14 based on updated information from SWC that includes actual CAPEX together with an update on forecast expenditure for the remaining quarter.

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

In addition, should actual expenditure be below forecast in 2013-14, NSWIC submits that the difference is deducted from the determined CAPEX for the next regulatory period.

> **NSWIC submits that the difference between allowed and actual CAPEX is deducted from the determined CAPEX in the next regulatory period.**

Asset management and planning approach

NSWIC notes that SWC's previous asset management and planning approach was set to comply with the NSW Government's Strategic Management Framework and the NSW Government's Total Asset Management Policy and Guidelines (TAM). Furthermore, the Capital Investment Plan (CIP) provided a pathway for State Water's capital investments over the previous Determination.

While previous investments are not relevant in this instance, NSWIC is concerned that the CIP has potentially dictated capital investments whose impact will carry over to the next Determination period while State Water has since been subjected to amendments in its operating license. In particular, SWC's operating license was amended in 2013 and will require SWC to be compliant with the International Standards ISO 55001: 2013 Asset Management Systems - Requirements. Based on this new requirement, we request further detail on SWC's comment that;

> *"The CIP is the prioritized list of projects that will proceed to construction in current and future years aligning with the (Total Asset Management Plan 2009) planning horizon."*[36]

[36] Page 71, SWC submission to ACCC

In particular, we are concerned that there could be a conflict between the previous compliance requirement and the newly imposed requirement. We urge the ACCC to assess this point carefully to ensure no investments are being commenced over the next regulatory period unless those investments are assured of being compliant with the new requirements.

NSWIC submits that SWC presents clarification whether the amendment to State Water's Operating Licence will financially impact State Water's investment projects under the CIP.

Historical capital expenditure

NSWIC notes that SWC's actual capital expenditure in the current Determination remains significantly below IPART's allowed CAPEX. We urge the ACCC to carefully consider any proposed future CAPEX to ensure that customers will not be asked to pay for works which are never undertaken.

Furthermore, SWC states that significant problems arose in respect to the ICT program during the current Determination period, and that additional expenditure in the magnitude of $3 to $4 million annually will be required in the next Determination. We submit that these problems must be treated as an external event and not be added as an additional expense to customers who have already paid for such programs.

NSWIC submits that problems with the ICT program are outside customer's control and customers should not bear the costs of a failed program implemented by SWC.

Proposed capital expenditure and major works

NSWIC notes the significant capital expenditure proposals in the 2014-15 period. Based on forecast figures from 2013-14, SWC proposes to increase its CAPEX by around 25%. However if 2012-13 actual CAPEX figures are compared with proposed CAPEX figures in 2014-15 then the increase would be 78%. NSWIC considers that such a large CAPEX proposal warrant detailed explanation by SWC and such explanation is not provided in SWC's submission.

State Water's dam safety upgrade program

Given the significant under-spending in this thematic expenditure item over the current Determination period, NSWIC proposes that any difference between actual and allowed revenue is deducted from the determined CAPEX in the next determination period.

In addition, NSWIC has considerable concerns about SWC's comment that;

"The learnings from the PRA project have implications for State Water's dam safety upgrade program. There remains a substantial body of work to be undertaken to investigate upgrade options for many non-compliant dams which is work required in order to assess the viability of such upgrades"[37]*.*

[37] Page 79, SWC submission to ACCC

NSWIC interprets "a substantial body of work" as a request by SWC to impose significant additional costs on customers. Given the significant under-spending in respect to dam safety upgrades, NSWIC submits that any proposed future costs in this respect are covered through the difference between actual and allowed CAPEX in this regulatory period.

> **NSWIC submits that future works in respect to the PRA project are covered through the difference between actual and allowed CAPEX in the current regulatory period.**

Environmental planning and protection

NSWIC notes that SWC has based its CAPEX proposal in this thematic expenditure item on assumptions about directions from the Minister for Primary Industries. Without clear direction from the Minister, NSWIC does not accept the proposed $57million capital expenditure.

> **NSWIC submits that no expenditure for environmental planning and protection be allowed without explicit directions from the Minister for Primary Industries.**

In addition, NSWIC notes that SWC seeks $3 million for urgent work on the Lake Brewster project. It is our understanding that the remedial work is an enhancement to a project funded through the Water Smart Australia program. As such, the project provided both water quality and water efficiency outcomes, and returned water savings to the Commonwealth Government. The Lachlan Customer Service Committee has endorsed the requirement for repair work at Lake Brewster as a high priority but has not been provided with a detailed project outline or costing. As the Lake Brewster project provides water quality as well as water efficiency outcomes, and therefore a benefit for the whole community, NSWIC submits that State Water should source external funding for this project. To gain a detailed understanding of the issue, we strongly urge the ACCC to liaise with our member organisations on this issue.

Water delivery and other options

NSWIC reiterates its concern in respect to the proposed works in this thematic expenditure item.

Without a detailed business case that assesses the net benefits and proposed efficiency gains of the Computer Aided River Management System (CARMS), NSWIC rejects the proposed expenditures of $5 million per annum over each year of the next determination period. In particular, NSWIC is concerns that SWC is proposing to recover $5 million per annum from customers, whilst at the same time sourcing ' third party funding' for the project[38].

As significant ambiguity exists over the net benefit of CARMS together with uncertainty of external funding sources, NSWIC submits that the proposed expenditures must be rejected until such time as these issues are clarified.

[38] Page 84, SWC submission to ACCC

NSWIC submits that any proposed expenditure for CARMS are postponed until uncertainties relating to external funding sources have been clarified.

We urge the ACCC to take particular note of NSWIC valley-based organisations that will provide further background on this proposed item and the discretionary capital projects.

Corporate Systems

As outlined in our response to Chapter 5, NSWIC recognizes the need for corporate systems but we are unable to support additional CAPEX that must be categorized as standard operating procedures.

NSWIC urges the ACCC to thoroughly consider the proposed expenditure in this regard and only allow funding if the upgrades will lead to net benefits for SWC and customers.

Information management and the business transformation project

NSWIC notes that customers have previously funded an upgrade of the ICT system without obtaining any commensurate benefits. We are concerned that the proposed costs in this thematic expenditure item continue to fund projects that are not completed.

Investment

NSWIC notes that an internal review conducted by SWC could impact the expenditure forecasts AND the timing of when the predicted expenditure will occur. Aside from significant transparency issues, NSWIC submits that such a review constitutes a significant obstacle in assessing the necessity of the proposed expenditure items. For that purpose, NSWIC requests that any projects which the review determines to lie outside the next determination period be postponed and that any costs associated are reassessed in the following Determination period.

NSWIC submits that any projects that are determined to lie outside the next regulatory period are postponed and that any associated costs are re-assessed in the following determination period.

Capital expenditure as incurred vs. as commissioned

NSWIC seeks clarification on section 7.6 Capital expenditure as incurred versus as commissioned. In particular, NSWIC seeks to understand the following;

Under the IPART framework, the value of the assets used during the preceding period was calculated using a capital as incurred approach. Consequently, it is incorrect to present previous regulatory capital expenditure on an as commissioned basis and the subsequent regulated asset base role forward.

Chapter Eight - Revenue required for capital expenditure

NSWIC considers chapter 8 to be the foundation that underpins SWC's submission to the ACCC. The calculations and proposal put forward in this chapter not only influence SWC's assessment of its financial viability they also directly impact on customers' bulk water charges. Given this crucial link, NSWIC will comment on each of SWC's proposals in turn.

Regulated asset base (RAB)

NSWIC considers the practice of rolling forward the RAB in order to create an opening value in the next Determination period as flawed given that the process is based on forecasts in the last year of the current Determination. NSWIC notes that SWC has significantly under-spent on its CAPEX in the first three years of the current Determination - by a magnitude of $67 million. In contrast, SWC forecasts to increase its CAPEX to $97 million in the last year of the current Determination which is $15 million more than each year of the current regulatory period.

This heavy weighting of CAPEX in the last year of the current Determination is questionable at best, in particular given SWC's track record over the last three years. Without proof that these capital expenditures will necessarily eventuate, NSWIC submits that SWC is proposing a future RAB value that is based by 30 per cent on forecasts[39]. As a matter for comparison, NSWIC emphasises that a similar situation occurred in the previous Determination, where some 56 per cent of RAB (of five year CAPEX) was attributed to 'forecast' rather than 'actual' capital expenditure.

> **NSWIC submits that the RAB value must be based on actual expenditure figures rather than forecasts given the intrinsic link to bulk water prices.**
>
> **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 Determination and should be better placed to determine an appropriate RAB value.

NSWIC believes 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."*[40] (emphasis added)

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

[39] Based on CAPEX only.
[40] Page 23, ACCC Pricing Principles

In addition, NSWIC notes the ACCC Pricing Principle which states;

> *"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."*[41]

Based on the closing figures included in table 8.1 of SWC's submission, NSWIC emphasises that SWC's application proposes a closing RAB value that is $157 million greater than the closing value in 2012-13. In comparison, the difference between 2009-10 and 2010-11 was $85 million between 2010-11 and 2011-12 it was $64 million and between 2011-12 and 2012-13 it was $54 million. NSWIC submits that the proposed tripling of a RAB value in the last year of the current Determination is a considerable price shock and cannot be accepted.

> **NSWIC submits that the proposed tripling of the RAB value in the last year of the current Determination must be regarded as a considerable price shock and cannot be accepted.**

Furthermore, NSWIC notes that SWC intends to index its RAB value whilst also requesting the use of a nominal WACC. NSWIC questions the need to adjust both these values for inflation and requests that the ACCC assesses whether such a practice would constitute double counting and hence lead to higher charges than necessary.

In addition, NSWIC notes that SWC also suggests an alternative approach to valuing its asset base, based on the Modern Engineering Equivalent Replacement Asset value[42]. NSWIC considers such a proposal irrelevant given that the WCIR are clear on this matter;

> *"Scheme 2 of the WCIR provides that where a Part 6 operator has already had its RAB value set by an agency of a state under a law of the state, this is the value that must be used for the initial starting value under the Part 6 approval or determination process."*[43]

In addition, NSWIC notes that ACCC Pricing Principles further outline that;

> *"Once a RAB value is set it must not be subject to revaluation. Revaluation creates uncertainty for the regulated business and its customers and can result in price shocks and windfall gains (...) to the business."*[44]

NSWIC submits that the 'revaluation' based on the Modern Engineering Equivalent Replacement Asset value approach would lead to a significant windfall gain for SWC. The resulting price shock and the fact that no further evidence has been provided by SWC that such an approach is more accurate or efficient leads to NSWIC to reject such a revaluation. We submit that the methodology implemented by IPART must be maintained for the next Determination.

> **NSWIC submits that the approach to valuing RAB as proposed by IPART must be maintained.**

[41] Page 24, of ACCC Pricing Principles
[42] Page 96, SWC submission to ACCC
[43] Page 24, ACCC Pricing Principles
[44] Page 23 of ACCC Pricing Principles

Finally, Table 8.1 also outlines that asset disposals over the five years from 2009-10 to 2013-14 are zero. NSWIC submits that further information in this respect must be provided. We are unconvinced that this information is accurate.

Rate of return (WACC)

In assessing SWC's proposed WACC, NSWIC references SWC's comment in Chapter 4;

> *"(...) an allowance is provided to appropriately compensate State Water's investors (NSW Government) for the opportunity costs of investing scarce capital resources in State Water and the risks attached to that investment".*[45]

NSWIC notes that SWC is not only proposing to provide 8.96% in compensation to its investors - the NSW Government - but that the proposed WACC suggests that the risk attached to that investment has increased. NSWIC does not concur with either of these assessments and emphasises that SWC has provided no evidence that a 1.56% increase in the current WACC is in any way justified.

> **In considering each of the WACC parameters - along with the overall consideration of whether to move the individual WACC parameter in this Determination - NSWIC submits that the ACCC must consider if a case for change has been made.**
>
> **NSWIC submits that the current WACC of 7.4% must be maintained for SWC.**

SWC seem to further advance a case based on business risk in order to increase the current WACC value. NSWIC rejects such a proposal as we cannot see any evidence how SWC's underlying risk could have changed over the current Determination. If anything, financial markets seem to suggest that the significant volatility and risk that was inherent over the current and previous Determination has significantly diminished and hence a lower compensation should be sufficient to compensate investors.

In addition, NSWIC notes SWC's comment in section 8.2.4;

> *"Unless the business's underlying risk has changed substantially since IPART's determination - which it has not since State Water is essentially engaged in the same regulated activities today as it was in 2010 (...)"*[46]

As SWC has itself outlined that its business risk has not changed, NSWIC considers 'risk' as an invalid argument to suggest an increase in the current WACC value.

Post-tax vanilla WACC

SWC suggests that due to the ACCC approach, SWC will experience a lower WACC and hence be significantly disadvantaged, despite the fact that SWC proposes to increase the WACC by 1.56 per cent. Irrespective of this inconsistence, NSWIC emphasises that the two approaches (pre and post tax WACC calculation) will not make a difference once SWC is actually paying taxes. As detailed in Chapter 9 of this submission, NSWIC considers

[45] Page 34, SWC submission to ACCC
[46] Page 100, SWC submission to ACCC

SWC's tax deferral is a benefit to SWC. We believe that this benefit is 'compensation' enough for SWC. Should SWC pay taxes in future regulatory years, then it is NSWIC's understanding that this tax expense will be included in the future WACC. NSWIC therefore see absolutely no reason why the current WACC should be artificially inflated to 'compensate' SWC for a 'lower' WACC given that SWC currently benefits from its tax deferral.

> **NSWIC submits that a post-tax WACC calculation will not disadvantage SWC as the business currently receives benefits through its tax deferral.**

WACC methodology and summary of estimates

NSWIC does not concur with SWC's assessment in respect of the WACC methodology;

> *"State Water considers that it is appropriate to adopt a different approach from that proposed in the Pricing Principles. In addition, there are some areas, where the Pricing Principle paper is ambiguous on the precise approach that the ACCC intends to use. In those areas, State Water has developed its approach based on an assessment of established finance principles and good regulatory practice in Australia and elsewhere."*[47]

NSWIC considers there to be absolutely no reason why such a deviation is justified and submits that SWC simply tries to artificially increase its WACC. In particular, NSWIC notes the ACCC Pricing Principles in this regard;

> *"In determining the WACC, it will be necessary to ensure the rate of return is commensurate with the commercial risk associated with the business' regulated activities such that the business recovers its efficient costs."*[48]

As SWC's underlying business risk has not changed, NSWIC submits that no change in the WACC is necessary. In addition, the above quote makes a specific reference to the 'efficient' costs of the business. As NSWIC has outlined on multiple occasions, SWC's argument is centred on the difference between allowed and actual revenue in contrast to actual revenue and costs. Given the $50 million net profit that SWC achieved in 2012-13, we consider there to be even less evidence for a change in the WACC.

Furthermore, NSWIC draws the ACCC's attention to a further point raised in its Pricing Principles;

> *"Several of the parameters used to calculate the WACC are influenced by market conditions which can change over time. In these instances the pricing principles will be updated accordingly."*[49]

NSWIC will make a compelling argument that several of SWC's values are significantly overstating current market conditions and as such, NSWIC will propose alternatives.

Risk free rate

[47] Page 97 and 98, SWC submission to ACCC
[48] Page 26, ACCC Pricing Principles
[49] Page 27, ACCC Pricing Principles

NSWIC rejects SWC's submission in respect to the risk free rate (RFR) as we consider the proposed value to significantly overstate current conditions. SWC's suggests a value of 5.26% which is significantly higher than the mean annualised Commonwealth Government nominal bond yields which are often used as benchmarks for the RFR. As a matter of comparison, the following table is provided based on a discussion paper published by the Queensland Competition Authority;

Financial Year	5 year Nominal CGS	10 year Nominal CGS
2007-08	6.44%	6.27%
2008-09	4.64%	5.06%
2009-10	5.31%	5.57%
2010-11	5.15%	5.38%
2011-12	3.59%	4.05%
2012-13	2.66%	3.07%

In particular, with the onset of the global financial crisis in 2007, yields on Australian Commonwealth Government Securities (CGS) decreased significantly and have continued a downward trend since (as the table highlights). These present yields reflect a greater than 300 basis point decline relative to the yields prevailing in 2007-08.

Whilst NSWIC considers it appropriate that a figure closer to 3.07% must be used for the SWC's WACC analysis, we also considered the average 10 year nominal CSG over (most) of the current Determination (2009/10 - 2012/13). The value would equate to 4.52% which is still significantly lower than SWC's proposed value of 5.26%. However, given the continuous decline in risk free rate[50], NSWIC submits that the 2012-13 figure more accurately reflects the current conditions within Australia, and hence submits that a risk free rate of 3.07% is used for the analysis.

In addition, an international comparison of Government bond[51] yields support's our assessment that SWC's proposed risk free rate is significantly overstated.

	10 year maturity	15 year maturity
Australian Bond	3.85%	4.33%
UK Gilts	2.63%	3.69%
German Bund	1.82%	2.61%
Japan JGB	0.74%	1.77%

Finally, SWC's suggestion to use the long term risk free rate coupled with the long term market risk premium is not valid in NSWIC's opinion, as the ACCC Pricing Principles clearly outline that the market risk premium should be set at 6 per cent.

[50] Please refer to appendix B

[51] Bloomberg http://www.bloomberg.com/markets/rates-bonds/government-bonds/australia/, accessed 15 August 2013

Beta

NSWIC rejects SWC's proposal for a 0.9 beta based on a consulting report by Strategic Finance Group (SFG). As SWC is not a listed company, there exists no methodology that would allow for a direct estimation of beta .To suggest that UK and US water networks should be used as an approximation is flawed given the significantly different market conditions and regulatory environments.

NSWIC notes that the ACCC Pricing Principles clearly state that under the WCIR the equity beta should be 0.7[52]. In addition, the ACCC Pricing Principles state that the ESC determination of regional and rural water prices determined a beta of 0.65. NSWIC considers these values to more closely align with SWC's true beta and submits that a value of 0.65 and 0.7 is used for the next Determination.

Based on these alternative figures, NSWIC proposes an WACC value of 6.2 per cent based on;

Parameter	**Values**
RFR	3.07 %
MRP	6 %
Beta	0.65 - 0.7
DRP	2.55 %
Gearing	0.6
Cost of Equity	7.12%
Cost of Debt	5.62%

NSWIC submits that a WACC of 6.2 per cent is more appropriate for SWC.

[52] Page 28, ACCC Pricing Principles

Chapter Nine - Tax expenses

NSWIC does not concur with SWC's claim that;

> *"Given the ACCC's use of a post-tax WACC, this effectively means that the tax benefit of accumulated losses has been transferred to customers."*[53]

Whilst SWC is unable to incorporate its tax expenditure into the ACCC's building block, it must be noted that SWC also does not currently pay taxes. We consider such a tax deferral as a benefit to SWC and raise the point again that SWC was able to generate a net profit before tax of $50 million and anticipates generating a positive net profit in each year of the next Determination.

As such, NSWIC believes that SWC tries to claim victim whilst the figures in table 9.1 suggest otherwise. The deferral of taxes and the generated net profit before tax of $50 million could be used by SWC to generate an additional return - another argument why the 'benefit' cannot (and should not) only be attributed to customers.

Additionally, despite SWC's claim that the weighted average cost of capital (WACC) over the next Determination period will be lower due to the WCIR and the ACCC Pricing Principles, State Water proposes a higher WACC than it currently has. This fact seems to completely contradict SWC's own argument.

Finally, NSWIC notes that should SWC pay taxes in future Determination periods, then this tax expense will be added to the WACC. Hence, any artificial inflation of the WACC due to a non-payment of taxes at this current stage is not justified.

> **NSWIC submits that the benefits of deferred taxes cannot be solely attributed to customers as SWC also benefits from deferring its tax expenses.**

[53] Page 120, SWC submission to ACCC

Chapter Ten - Total Revenue Requirement

NSWIC notes that SWC's proposed average annual increase in required revenue is misleading as estimates are used from the last year of the current Determination. As such, NSWIC submits that the actual increase proposed by SWC for its total revenue requirements might be significantly higher than suggested in SWC's submission.

As NSWIC sees no merit in comparing forecasts with forecasts, we submit that an updated annual average increase figure must be provided by SWC in the third quarter of this water year.

In addition to our comments made to Chapter 5 and 7, we also submit that the proposed revenue requirements are compared with actual expenditures over the current Determination to highlight the significant increases that SWC is proposing in this regard.

> **NSWIC submits that the proposed revenue requirements are compared with actual expenditures over the current Determination to highlight the significant increases that SWC is proposing.**

NSWIC considers this approach to have particular merit as SWC has indicated in its own submission,

> *"Unless the business's underlying risk has changed substantially since IPART's determination - which it has not since State Water is essentially engaged in the same regulated activities today as it was in 2010 (...)."*

Should proposed revenue requirements deviate significantly from current expenditures (which NSWIC suspects will be the case), we believe there is considerable scope for further investigation into SWC's proposed CAPEX and OPEX.

Finally, NSWIC notes that the total net return on assets as outlined in table 10.1 is heavily dependent on the underlying WACC calculations, plus the Determination of the regulated asset base. Our concerns with both figures have been outlined in detailed in Chapter 6.

<u>Government share revenue requirement</u>

NSWIC notes that the dollar value of the NSW Government contributions increase by a significantly lower amount than the contributions recovered by customers even though overall cost share proportions are maintained. This does not only highlight that SWC's customers are disproportionally burdened in the next Determination period but it also illustrates a significant lack of transparency on how SWC proposes to change the revenue requirements for customers vs. the NSW Government. In particular, a detailed outline of changes to total costs based on the proposed cost shares (table 11.1) would significantly aid stakeholder's understanding of the proposed adjustments.

> **NSWIC submits that SWC must provide a detailed outline of changes in revenue requirement in each valley based on the categories outlined in table 11.1**

Chapter Eleven - Cost sharing between users and government

NSWIC welcomes the NSW Government commitment to maintain current cost share ratios over the next regulatory period.

NSWIC makes no further submissions on Chapter 11.

Chapter Twelve - Form of Price Control

NSWIC notes that SWC seeks a fundamental change to the current price control mechanism and tries to acquire four separate risk insurance tools to "mitigate the risk of revenue volatility whilst minimising price shocks and other impacts on customers where possible"[54]. We vehemently object to such a proposal and submit that such a suggestion provides clear evidence that SWC is exercising its monopoly power. In the following paragraphs we will comment on each of SWC's proposal in turn.

> **NSWIC rejects SWC's proposal to amend the current price control mechanism as it leads to greater uncertainty, less transparency, and likely greater price volatility.**

Revenue Cap

SWC proposes to move from a price cap approach to a revenue cap approach. A revenue cap will cause considerably greater uncertainty and risk for customers since bulk water prices will not be known aside from the first year of the next Determination. The reason for this outcome stems from the proposed mechanism. Bulk water prices will have to align each year with the overall allowed revenue requirement and hence will have to be amended should a deviation between actual and allowed revenue occur. Given that water availability in NSW is variable, this could mean significant price shocks each year for irrigators who will have to base their operation and investment decisions on even more uncertainty. In addition, this mechanism ensures that SWC will always achieve its allowed revenue (emphasis added), whilst the same protection is, by no means, available to irrigators.

NSWIC submits that this approach is a clear deviation from the National Water Initiative, the principal aim of which was to allow water to move to its highest value use. In the event that costs to Water Access License holders cannot be accurately foreseen, highest value use cannot be effectively determined. SWC, in shifting risk away from itself and onto customers, effectively attempts to undermine the market approach to water management adopted in Australia.

NSWIC notes that a revenue cap is usually imposed to ensure that underlying costs for a business are not artificially inflated. Hence a revenue cap places an upper boundary on possible revenue acquired. This subsequently incentivises the business to run as efficiently as possible and keep costs at a minimum. NSWIC notes that SWC's reasoning for implementing a revenue requirement is completely different and runs contrary to the general understanding for implementing such a cap. In the present case, SWC is seeking a revenue cap as a risk protection mechanism for its business, instead of being a regulation imposed on the monopoly provider to minimise costs.

Finally, NSWIC is concerned that such a revenue cap is unlikely to drive further efficiency savings within SWC as actual revenue is not compared with costs but rather the 'allowed revenue'. Given our concerns in respect to SWC's previous CAPEX expenditure, we emphasise that such an approach will not only provide an insurance mechanism for SWC, it will remove the imperative for it to optimise the use of its acquired funds.

[54] Page 129, SWC Submission to ACCC

Carry-over mechanism

SWC proposes to further impose a carry-over mechanism between Determinations should any revenue shortfalls (or windfalls) in revenue occur over the next regulatory period. NSWIC considers this the second insurance mechanism that SWC tries to impose to protect itself from lower than (possibly) expected revenue. We believe that such a mechanism does have the capacity to cause significant price shocks between Determinations which could have substantial impact on the medium and long term planning and investment decisions for irrigators.

Fixed capital investment in irrigation generally represents 'sunk costs' and are made based on irrigators best available knowledge at the time about future input costs. Should bulk water charges change dramatically between Determinations, then this could have a detrimental effect on the viability of invested capital by irrigators. The mechanism is therefore likely to serve as a disincentive for State Water's irrigation customers to further modernise their operations.

Finally, NSWIC stresses that the carry-over mechanism is proposed for the 'allowed' revenue requirement rather than the actual revenue that was required for the period. As we have outlined in the previous section, NSWIC notes that SWC has significantly under-spent on its CAPEX against its allowed revenue. If the ACCC accepts such a carry-over mechanism, then the amount that might be carried over to items/projects that are never commenced. We ask the ACCC to recognise this shortfall and reject such an approach.

15 per cent annual adjustments

SWC proposes a 15 per cent annual adjustment mechanism in conjunction with its submission of a revenue cap approach. Whilst NSWIC agrees that such a constraint will put an upper (lower) boundary on the yearly price adjustment, we emphasise that this mechanism still causes significantly greater price volatility which will consequently mean greater uncertainty for irrigators. To the contrary, the current price control mechanism sets bulk water prices for the entire Determination and only allows those prices to adjust by CPI. Hence a comparison between the current and the newly proposed mechanism means a comparison between possible 2-3 per cent price adjustments and up to 15% price adjustments each year. Finally, NSWIC believes that the 15 per cent annual price adjustment could create perverse outcomes e.g. bulk water users might opt to use more water in years of lower water availability that they otherwise would for fear that prices in the next year will rise significantly. NSWIC does not consider such perverse outcomes as consistent with sensible water management in NSW.

Tariff Structure

NSWIC considers SWC's proposal for a shift in the current tariff structure as the most offensive risk protection mechanism that SWC is seeking. We note that SWC has proposed this amendment on multiple occasions in the past, but that IPART has continuously and comprehensively rejected such an approach on the basis of equity and risk sharing between SWC and its customers.

NSWIC reiterates that we consider SWC's proposed tariff structure as clear evidence that SWC is exercising its monopoly market power to shift its business risk to customers. In particular, this tariff structure will protect SWC from all possible water availability scenarios. In case of very low water availability, SWC is effectively seeking to recover its full allowed revenue while the business is not able to provide its full services to customers. On the other hand, irrigators, under such a scenario, would be asked to pay for a service that they cannot access. As irrigators have no choice but to pay SWC's fixed charge component due to the intrinsic link with irrigator's Water Access Licences, we consider SWC's proposal as highly inequitable and reject it as a matter of principle.

NSWIC rejects SWC's proposed price control amendments on the grounds that SWC - as a monopoly operator - is simply aiming to acquire four separate risk protection mechanisms without any equivalent compensation for customers. We further note that these demands come atop the fundamental shift in demand forecasting allowed at the last Determination by IPART which had the effect of dramatically reducing volatility risk for SWC through shifting risk to its customers. We submit that the creeping approach to risk shifting must be rejected by the ACCC.

NSWIC furthermore submits that SWC's proposed price control mechanism runs contrary to standard economic theory in that lower demand (in case of low water availability) should cause a decrease in prices. In SWC's case a lower demand would cause an increase in prices. Such an approach can only be regarded as counter-intuitive.

NSWIC rejects SWC's comment that this form of price control will "minimise price shocks and other impacts on customers (...)"[55]. As we have outlined in the previous section we believe that SWC's proposal is likely to cause significant price shocks and will have a multitude of other undesirable effects on customers.

NSWIC also notes that SWC is using the WCIR, the *Water Act 2007* and the *ACCC Pricing Principles* to advance its own objectives to acquire more risk protection tools whilst the same protection is not available to SWC's customers. We urge the ACCC to address this issue as a matter of priority to ensure that the protection of customer from a monopoly operator is ensured.

<u>Reason for change</u>

SWC claims that a change in the price control mechanism is necessary and inevitable in order to ensure the commercial viability of SWC and to guard against SWC's business risk that arises due to a mismatch between variability in SWC's revenue and costs[56]. NSWIC notes that the same mismatch between revenue and costs is also present for any of SWC's customers with the additional constraint that the latter do not have access to the insurance that is afforded to SWC by its base level revenue mechanism. In addition, NSWIC notes that SWC's submission on price control is based on actual versus allowed revenue, rather than actual revenue and costs. We will not accept a change in price control mechanism that is based on revenues alone without consideration of actual expenditure figures.

In addition, SWC states that "commercial viability is the recovery of efficient costs to ensure State Water can undertake its core activities to capture, store and release of bulk

[55] Page 129, SWC submission to ACCC
[56] Page 129, SWC submission to ACCC

water (...)[57]". Whilst NSWIC has never argued with the need for SWC to remain financially viable, we note that the proposed price control mechanism does not constitute a recovery of efficient costs but a recovery of allowed costs without detail on the actual underlying expenditure. In addition, NSWIC notes that SWC is seeking a near 13 per cent increase in its operating expenditure which is a significant increase for the purpose of undertaking 'core' activities.

Alternative forms of price control to mitigate revenue volatility risk

NSWIC submits that SWC has not thoroughly considered alternative options advanced by stakeholders. In particular, the possibility of using a dual tariff structure was continuously rejected by SWC as it was claimed that neither sufficient time nor sufficient resources were available to allow for such an analysis. The claim of timing was thoroughly undermined by SWC itself when it delayed provision of its submission to the ACCC by two months.

Whilst NSWIC does not necessarily endorse such a dual tariff structure approach, we believe that further consideration of the proposition is warranted. We remain deeply disappointed at the failure of SWC to consider this approach on the advice of its customers.

Revenue Volatility allowance

NSWIC notes that SWC admits in its pricing submission to the ACCC that the ACCC's governing legislation does not explicitly prevent the inclusion of a revenue volatility allowance. However, SWC notes further that;

> *"There is a lack of precedent for this approach amongst Australian regulators and no established methodology for calculating such an allowance."*

NSWIC rejects this claim vehemently and refers to discussion at its March meeting which was attended by members from both the ACCC and SWC. During the related proceedings, a question was raised whether the ACCC would be able to allow such a volatility allowance. NSWIC emphasises that the ACCC did not reject such an allowance and stated that there is nothing in the current rules that would prevent the ACCC from providing such an allowance.

Managing the impact on customers

Whilst NSWIC acknowledges that a fixed charge deferral scheme is not relevant for the ACCC approval process, we would like to comment on this point nonetheless.

A deferral scheme with an interest charge will not alleviate the underlying financial difficulties of irrigators across NSW but rather shift an even greater burden to a later point in time. In times of low water availability irrigators are not able to access water and their income is severally affected. As such, these individuals will already be under significant financial stress which will not be eliminated by the prospect of paying an 80% fixed charge component with interest at a future point in time[58]. NSWIC considers it necessary to

[57] Ibid.
[58] Page 141, SWC submission to ACCC

mention that the NSW Government promised prior to the last election to waive fixed charges in case of two years of zero allocations.

Finally, NSWIC would like to respond to SWC's comment on pricing of bulk water in other jurisdictions[59]. It must be recognised that the reliability of water in NSW is considerably different to other jurisdictions and hence a direct comparison is neither feasible nor advisable. NSWIC urges the ACCC to take into consideration that the reliability in NSW in many cases is significantly lower and hence there is already an inbuilt risk by holding entitlements in NSW. Such entitlement holders will be significantly disadvantaged if the current price control mechanism is adjusted as proposed by SWC's.

[59] Page 142, SWC submission to ACCC

Chapter Thirteen - Forecast demand and consumption

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, IPART relied upon 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 weighted average approach is not necessarily superior to the full IQQM model. In particular, the full IQQM model provides a long run average consumption forecast of 5450GL which closely aligns with actual extraction figures in 2012-13 (5986GL). In comparison, the 20 year rolling average approach returned a value of 4627GL for this Determination period.

Furthermore, 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 Determination. Whilst NSWIC acknowledges that year-on-year fluctuations would be small, the additional uncertainty that a rolling average methodology creates will not assist individual Water Access Licence holders to predict future price adjustments.

In addition, as the last two years have clearly highlighted, there is no correlation between weather conditions from one year to another, and hence the move towards a 20-year moving average does not add any significant benefits to the analysis but rather decreases the transparency for customers.

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

Finally, NSWIC would like to emphasise that Murray-Darling Basin Authority has discharged the 20 year average demand forecasting model in favour of the full IQQM dataset for the Murray-Darling Basin Plan.

Either way, should the ACCC however accept SWC's proposal to maintain the 20 year rolling average approach, NSWIC submits that the 2013-14 consumption figures must be included into the analysis at the earliest opportunity so that customers are able to obtain a more accurate picture on future bulk water charges.

> **NSWIC submits that 2013-14 consumption figures are included into the IQQM at the earliest possible data to provide customers with accurate and up-to-date information about their future bulk water charges.**

Chapter Fourteen - Regulated tariffs

NSWIC contests SWC's claim that the structure of bulk water charges remains largely unchanged[60], especially in light of SWC's proposal to amend the current tariff structure. The claim is clearly nonsense when SWC's submission seeks a fundamental change to pricing structures.

Proposed regulated charges

We have previously outlined our concerns to SWC's proposed revenue requirements and have made submissions to support our comments on Chapter 5,7 and 8. In particular, NSWIC consider SWC's proposed revenue requirement as significantly inflated and demands an external prudent and efficiency analysis of all of SWC's proposed charges. Without such an analysis, NSWIC is unable to endorse the proposed regulated charges for high security entitlements, general security entitlements and usage.

Furthermore, we have outlined the efficiency and equity issues with the proposed price control mechanism and tariff structure design which underpins these charges. NSWIC continues to stress that no justifiable explanation has been provided by SWC that warrants such a fundamental change in the way bulk water prices are currently being set.

> **NSWIC submits that the proposed regulated charges must be rejected given the underlying proposed price control mechanism and tariff structure design.**

In addition, NSWIC rejects the inclusion of the proposed charges for NSW's coastal valleys as these charges are not relevant to the ACCC Determination; these charges will be reviewed by NSW regulator IPART next year when further information is available on SWC's operating expenditures, capital expenditures and any community service obligations.

Finally, NSWIC points out that the charges presented in table 14.1, 14.2 and 14.3 can only be regarded as 'indicative' as SWC's proposed price control mechanism could cause these charges to fluctuate considerably. In particular, SWC proposes a 15 per cent annual adjustment in comparison to IPART's CPI adjustments. This means price fluctuations will be significantly larger under SWC's proposal than has been the case under IPART.

Such uncertainty is neither desirable nor useful for irrigators in NSW.

> **NSWIC submits that the proposed regulated charges can only be regarded as indicative as SWC's proposed price control mechanism could cause large fluctuations in these charges.**

Large customer rebates

NSWIC welcomes the continuation of large customer rebates. However, we cannot see any evidence that a reduction in rebates is justified. NSWIC submits that the benefits of economies of scale and system-wide benefits persist and that in many cases, the transformation of an entitlement is not complete, i.e. an individual irrigator only transforms part of his licence. As such, these irrigators remain customers of the ICD and the overall benefits to SWC would be maintained.

[60] Page 149, SWC submission to ACCC

> **NSWIC submits that the current large customer rebates are maintained as no evidence has been provided by SWC that a reduction to the economies of scale and system-wide benefits has occurred.**

NSWIC urges the ACCC to consult closely with the irrigation corporation on this issue as their knowledge and expertise on this matter are invaluable.

Chapter Fifteen - Metering charges

NSWIC notes that SWC seeks a fundamental change in the way meter service charges are being set in NSW and in addition requests a significant increase in these charges. This request is made by SWC despite the complete lack of accurate actual operating and maintenance costs. NSWIC cannot - and will not - agree with such an approach.

> **NSWIC submits that further investigations must be made into the true operational and maintenance costs of meters and telemetry networks before a change to the methodology and charges could possibly be considered.**

As a matter of importance, NSWIC emphasises 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 currently exists that complies with these standards. As such, a proposal to amend the current metering service charges and other charges associated with the scheme are significantly premature and should not proceed.

> **NSWIC submits that no amendments to the current metering charges should be made until such time as meter standard compliant products are available.**

<u>NSW Metering Scheme</u>

NSWIC notes SWC's comment that;

> *"the metering scheme is intended to deliver water savings that will be shared between the environment and community"[61].*

Not only would NSWIC like further evidence of the achieved water savings through the metering project, but we would also like to emphasise that the funding for this project required a return of entitlements to the Commonwealth. We remain concerned as to how the NSW Office of Water (NOW) intends to provide these entitlements and, until full details are disclosed, NSWIC reserve its right in respect of support for the entirety of the programme.

In addition, NSWIC would like to refer to SWC's point;

> *"The metering scheme will involve moving from customer-owned meters to meters owned by State Water and the government, provided by the Commonwealth in the Murray Darling Basin (...)".[62]*

Whilst this transfer might be applicable in certain circumstances, NSWIC submits that there remains considerable doubt over ownership of future meters, particular in the northern valleys. Until such time as these issues are resolved, NSWIC submits that such a universal broad scale comment by SWC should be removed.

> **NSWIC submits that SWC must remove any comments and proposed metering charges from its submission that are based on hypotheses.**

[61] Page 162, SWC submission to ACCC
[62] Ibid.

Furthermore, SWC suggests that;

> *"By the end of the 2014-17 determination period this will have increased to approximately 3000 meters, with almost all being connected to a centrally controlled telemetry network. In the unregulated and groundwater systems approximately 5600 meters will be installed by the end of the determination period"*[63]

NSWIC considers it absurd that SWC is proposing to exponentially increase the amount of meters being installed without a guarantee that such meters will be compliant with the recently agreed metering standards and in the absence of a firm commitment from government to proceed. In particular, without a suitable product being developed, NSWIC does not see how any accurate costing for these meters could possibly take place or any comparison can be made whether the currently installed meters are the most cost effective alternative.

The current installation of meters is inefficient, ineffective and costs could blow out significantly and hence we urge the ACCC to put an urgent hold on the current installation process until such time as the primary issues around the programme been resolved.

Benefits of NSW Metering Scheme

NSWIC acknowledges that an outline of the benefits from the NSW metering scheme are important, however we would like to point out that the opening paragraph of Chapter 15 indicates that the metering scheme is intended to deliver water savings which will be shared between the environment and community[64]. Section 15.1.1 however makes no reference to any achieved water savings. NSWIC believes such an inconsistency warrants further explanation.

We refer to our Metering Policy available on our website for further detail in respect of the scheme.

Costs of NSW Metering Scheme

NSWIC notes that SWC clearly states that;

> *"As the NSW Metering Project is still in its infancy, complete and accurate actual operating and maintenance costs were not available and those included are the best available at the time of making this submission."*[65]

Given the lack of complete and accurate actual data on the maintenance and operational costs as well as the absence of a meter standard compliant meter, NSWIC cannot see how SWC could possibly claim that the current metering charges will *"significantly under-recover the costs to operate and maintain the meters and telemetry network."*[66]

Furthermore, NSWIC submits that significant ambiguity exists whether SWC proposes to levy a MSC per meter or per site. It must be recognised that several meters are often

[63] Page 162, SWC submission to ACCC
[64] Page 163, SWC submission to ACCC
[65] Page 166, SWC submission to ACCC
[66] Page 164, SWC submission to ACCC

installed per site and hence the proposed charges could cause significant cost increases for Water Access Licence Holders. We request that SWC provides clarity on this issue.

In addition, we are not content to accept costs based solely on an 'internal review' that would see metering service charges increase by over 300 per cent in some instances.

> **Without any further information or a peer reviewed business case, NSWIC submits that the charges specified in the 2010 determination should be maintained.**

Furthermore, NSWIC emphasises that the initial objective of the metering program and - more particularly - the installation of telemetry, was designed to achieve efficiency gains, which should have translated into lower costs to customers. NSWIC has found no evidence of such cost savings and to the contrary, SWC proposes to increase the metering service charges significantly. This development is very concerning for NSWIC and we submit is contrary to the initial objectives of the metering program.

> **NSWIC submits that the objective of the metering program was to achieve efficiency gains and that the efficiencies must translate into lower costs for customers and/or improved service standards.**

<u>Funding Source</u>

NSWIC rejects SWC's hypothesis that there

> *"may be cases of State Water funded meters* (and that) *to ensure a revenue source is available to accommodate these scenarios, State Water proposes that metering service charges levied from these customers include an allowance for a return on capital and depreciation for the investment these assets."*[67]

Until and unless SWC can provide evidence that governments intend for SWC to fund meters, such hypothetical scenarios should be ignored. Only factual costs must be considered.

> **NSWIC submits that only factional costs can be considered in the pricing submission.**

<u>A. Operational Costs</u>

<u>Commonwealth-funded meters</u>

NSWIC disagrees with SWC's assessment that Commonwealth-funded assets have a nil capital cost as there is an explicit exchange of funding for meters and entitlement transfers to the Commonwealth. As such, NSWIC considers this project not to operate on a 'nil cost' basis but, to the contrary, the costs associated could in some cases significantly outweigh the capital costs of the actual funded meter.

> **NSWIC submits that costs associated with Commonwealth-funded meters can outweigh the actual meter capital cost.**

[67] Page 167, SWC submission to ACCC

State Water-funded meters

NSWIC reiterates that no meter standard compliant meter is currently available and that current costings are purely based on a single pilot program in the Murray Valley. We urge the ACCC to thoroughly consider submissions from our members in this valley to inform the Commission on costs, benefits and any problems that arose during the pilot project.

Finally, NSWIC questions the significant deviation between metering charges with and without telemetry. We reiterate that the installation of meters - in particular with telemetry - was designed to achieve efficiency gains and ultimately cost savings. SWC's charges suggest the opposite with metering charges being significantly higher than metering charges without telemetry. We strongly object to such a proposal.

Telemetered metering solution costs

NSWIC vehemently rejects SWC's proposal to cross subsidise the telemetered metering solutions costs by charging all customers (with and without telemetry) for a centralised information technology that will receive, process, store and analyse the telemetry data. We do not currently see how these services will benefit users without telemetry and hence reject SWC's proposal in this regard.

> **NSWIC vehemently reject SWC's suggestion to cross subsidise the telemetered metering solution costs.**

In addition, as SWC claims that the system will run remotely, we question the need to employ 3.75 additional full time equivalent staff (FTE) to run this system[68]. SWC has provided absolutely no evidence that supports such a requirement.

> **NSWIC submits that no evidence has been provided that would justify an increase in staff based on the telemetered metering solution.**

Finally, NSWIC rejects SWC's proposal to include an allowance for the telemetered metering solution cluster infrastructure[69], given that these costs are based on forecast projections of growth in the metering program. NSWIC submits that its members should not be charged in anticipation of an outcome that may not eventuate and against inefficiencies that may or may not be realised.

> **NSWIC rejects the proposed allowance for the telemetered metering solution cluster infrastructure given that these costs and the supposed benefits are far from certain.**

C. Corrective maintenance

NSWIC questions the percentages proposed by SWC in respect to replacement and repair rates and urges the ACCC to request from SWC an independent review of these figures[70].

[68] Page 173, SWC submission to ACCC
[69] Page 174, SWC submission to ACCC
[70] Page 176, SWC submission to ACCC

Meter replacement

Whilst NSWIC is content to accept return of capital, we reject SWC's proposal for a return on capital in respect to meter replacement costs. As SWC states in its submission, the current meters should be under warranty.

We consider the hypothesis put forward by SWC as having a remote probability and hence no further allowance cost should be included in the metering service charges. In addition, we vehemently reject the proposal to include any metering service charges into the RAB. We consider this proposal a blunt attempt to increase SWC's RAB without any justifiable explanation.

> **NSWIC rejects the inclusion of an allowance for meter replacement costs. In addition we reject that any meter charges should enter the RAB.**

Chapter Sixteen - Miscellaneous charges

<u>Allocation trade administration costs</u>

NSWIC rejects the proposed increases in temporary transfer charges as no evidence is provided that would suggest such a change is necessary.

We do not concur with SWC's assessment that an increase in charges is necessary as a result of increased complexity in water trading. To the contrary, should the market mature further then this should lower costs - not increase them. The fact that complexity exists within the temporary water market is neither the fault of SWC or its customers but rather a result of the inefficiencies inherent in the market. We cannot see how these inefficiencies have caused an increase in costs for SWC over the current Determination.

According to our understanding, SWC merely processes an application based on a predetermined template and inconsistent with current rules and regulations. As we are not aware of any changes to the template or the rules, we consider there to be no need to change the current charges.

> **NSWIC submits that that the temporary transfer charges under the current Determination are appropriate and should be continued.**

Chapter Seventeen - Customer consultation undertaken in preparing this application

NSWIC appreciates SWC's commitment to consult with stakeholders, however we note with considerable disappointment that our feedback has, in many instances, been ignored.

In particular, NSWIC would like to point to section 17.9.2 - pricing forum feedback. Stakeholders, including NSWIC, expressed their interest in obtaining further information on a dual tariff structure option that would allow customers to choose one of two tariff structures that aligns with their risk preference. We considered this request valid and important in light of SWC's proposal to move to a higher fixed charge tariff structure.

In response to our request, SWC outlined that;

> *"Due to several issues identified with this arrangement and time and budget constraints, it was decided that this was not a viable option of this determination period. However, State Water will investigate this option as part of preparations for the next determination period*."[71]

As outlined earlier in this submission, NSWIC does not agree with SWC's assessment that insufficient time was available, especially in light of SWC's submission being two months delayed. In addition, we note that we were unable to find any indication in SWC's submission that further operational budget allowances were sought by SWC to undertake such an analysis. If SWC was serious about investigating such an option, NSWIC had expected that SWC would ask for such an allowance. As such, NSWIC must conclude that there is simply a lack of 'willingness' to assess such an option, rather than a 'budgetary constraint'.

[71] Page 191, SWC submission to ACCC

Appendix A:

NSWIC
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Consultation

The Expectations of Industry

090303

Andrew Gregson
Chief Executive Officer

Member Organisations: Bega Cheese Limited, Border Rivers Food & Fibre, Coleambally Irrigation Co-Op Ltd, Cotton Australia, Gwydir Valley Irrigators' Association Inc., High Security Irrigators Inc, Hunter Valley Water Users' Association, Lachlan Valley Water, Macquarie River Food & Fibre, Mid Coast Dairy Advancement Group, Mungindi-Menindee Advisory Council, Murray Irrigation Limited, Murray Valley Water Diverters' Association, Murrumbidgee Groundwater Inc., Murrumbidgee Irrigation Ltd, Murrumbidgee Private Irrigators' Inc., Murrumbidgee Valley Food and Fibre Association,Namoi Water, NSW Farmers' Association, Ricegrowers' Association of Australia, Richmond Wilson Combined Water Users Association, Riverina Citrus, Southern Riverina Irrigators, South Western Water Users', West Corurgan Private Irrigation District, Wine Grapes Marketing Board

Introduction

NSW Irrigators' Council (NSWIC) represents more than 12,000 irrigation farmers across NSW. These irrigators are on 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.

This document represents the views of the members of NSWIC. However each member reserves the right to an independent view on issues that directly relate to their areas of operation, or expertise, or any other issues that they may deem relevant.

Executive Summary

This document sets out the consultation process that the irrigation industry expects from Government on policy matters affecting the industry.

Specifically, the industry expects that the contents of this document inform the consultation process with respect to preparation of the Basin Plan by the Murray Darling Basin Authority.

Background

Industry has been critical of consultation processes entered into by both State and Commonwealth Government entities in the change process with respect to water policy. Irrigators have significant sums invested in their businesses, all of which are underpinned by the value, security and reliability of their primary asset – water.

Irrigators recognise the imperatives for change and are content to provide advice on policy measures to ensure effective outcomes for all involved.

In light of these two factors, it is not unreasonable that irrigators request adequate consultation.

Recent consultation efforts have ranged from excellent to woeful[72]. Irrigators believe that a method of consultation should be determined prior to the commencement of a policy change process. To that end, this document sets out the methods which we believe are acceptable and ought be adopted by Government both State and Commonwealth.

In particular, this document aims to inform the Murray Darling Basin Authority in its work developing the Basin Plan.

Forms of Consultation

We consider two forms of consultation to be acceptable – Direct and Indirect. The preferred option will be dictated by circumstances.

[72] See case studies later in this document.

Direct Consultation

This method involves engaging directly with affected parties, together with their representative organisations. As a default, it ought always be considered the preferred method of consultation.

Irrigators acknowledge that practical exigencies must be considered to determine if Direct Consultation is possible. Such considerations will include:

- The number of affected stakeholders (the smaller the number, the more ideal this method);

- The timeframe available for implementation (the longer the timeframe, the more ideal this method)[73]; and

- The geographical distribution of stakeholders (the closer the proximity, the more ideal this method).

Indirect (Peak Body) Consultation

This method involves engaging with bodies that represent affected parties. NSW Irrigators Council is the peak body representing irrigators in this state. The National Irrigators Council is the peak body in respect of Commonwealth issues.

Irrigators acknowledge that there will be occasions on which consultation with peak bodies is necessary for practical reasons. Such reasons may include:

- An overly large number of affected stakeholders;

- A short timeframe (not artificial) for implementation;

- A large geographic spread of stakeholders; and

- An issue technical in nature requiring specific policy expertise.

This form of consultation requires some specific considerations that must be addressed in order for it to be considered acceptable;

- Timeframes

  Indirect Consultation is, in essence, the devolution of activity to external bodies. That is, the task of engaging with affected stakeholders to assess their views and to gather their input is "outsourced" to a peak body. That peak body cannot operate in a vacuum and, as such, must seek the views of its members lest it become unrepresentative. Dependent on the nature of the issues and the stakeholders, this

[73] Although note specifically that artificial timeframes, such as political necessity, will not be well received by irrigators.

may take some time. It is vital that peak bodies be requested to provide advice on necessary timeframes prior to seeking to engage them in an Indirect Consultation model.

- Resource Constraints

  Peak bodies do not possess the resources of government. In most instances – and certainly in the case of irrigation industry peak bodies – their resources are gathered directly from members and hence must be well accounted for.

  Peak bodies engage in a significant range of issues and activities, many of which feature their own time constraints.

  Prior to commencing the consultation process, discussions with peak bodies must be held to ensure that the needs of stakeholders with respect to resourcing and timeframes are respected. This may include ensuring that consultation does not occur during times of known peak demand; coordination with other government agencies to avoid multiple overlapping consultation processes; and coordination with peak bodies existing consultation mechanisms (for example, NSWIC meeting dates are set annually and publicly available. These are an ideal forum for discussion as they provides access to key stakeholders with no additional cost to stakeholders).

Stages of Consultation

Irrigators believe that a multi-stage consultative model, in either the Direct or Indirect applications, is necessary.

(i) *Identification of problem and necessity for change*

Irrigators are wary of change for the sake of change. In order to engage industry in the process of change, an identification of its necessity is required. This should take the form of a published[74] discussion paper as a minimum requirement.

(ii) *Identification of solutions and method for implementation*

With a problem identified and described, a description of possible solutions together with a proposed method of implementation should be published.

It is imperative that the document clearly note that the proposed solutions are not exhaustive. The input of stakeholders in seeking solutions to an identified problem is a clear indicator of meaningful consultation.

It is likely, in practice, that steps (i) and (ii) will be carried out concurrently. This should take the form of a document seeking written submissions in response.

[74] We accept that "published" may mean via internet download, but require that hard copies be made available free of charge on request.

The availability of the document must be widely publicised[75]. The method for doing so will vary depending on the method of consultation. As a threshold, at least 90% of affected stakeholders ought be targeted to be reached by publicity.

(iii) *Summary of submissions, identification of preferred approach*

Subsequent to the closing date, a document ought be published that summarises the submissions received in the various points covered. It must also append the full submissions.

Acknowledgement of a consideration of the weighting of submissions must be given. As an example, a submission from a recognised and well supported peak body (such as NSWIC) must be provided greater weight than a submission from a small body, an individual or a commercial body with potential commercial interests.

There are no circumstances in which submissions ought be kept confidential. Whilst we recognise that identification of individuals might be restricted, any material on which a decision might be based must be available to all stakeholders.

The document must then identify a preferred approach, clearly stating the reasons why that approach is preferred and why alternate approaches have been rejected.

Where the need for change has been questioned by submissions, indicating that a case has not been made in the opinions of stakeholders, further discussion and justification of the necessity must be made in this document.

(iv) *Explanation of interim determination and final feedback*

The document prepared in stage (iii) must now be taken directly to stakeholders via forums, hearings or public discussions. All stakeholders, whether a Direct or Indirect model is chosen, must have an opportunity to engage during this stage.

The aim of this direct stage is to explain the necessity for change, to explain the options, to identify the preferred option (together with an explanation as to why it is the preferred option) and to seek further input and feedback. Further change to a policy at this point should not, under any circumstances, be ruled out.

(v) *Publication of final determination*

Subsequent to stage (iv), a document must be published summarising the feedback received from that stage, identifying any further changes, identifying why any particular issues raised across various hearings at stage (iv) were not taken into account and providing a final version of the preferred solution.

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[75] Regional newspapers, radio stations and the websites of representative groups and infrastructure operators are useful options in this respect.

What Consultation Is Not

"Briefings" after the fact are not consultation (although they may form part of the process). Stakeholders will not be well disposed to engagement where prior decisions have been made by parties unwilling to change them. Briefings in the absence of consultation will serve to alienate stakeholders.

Invitations to attend sessions with minimal notice (less than 10 days) is not consultation. Consideration must be given to the regional location of parties involved, together with the expenses and logistical issues of travel from those regions.

Case Study One

Australian Productivity Commission (Review of Drought Support)

Getting it Right

During 2008, the Australian Productivity Commission commenced a review of Government Drought Support for agriculture. The review commenced with the publication of a document to which submissions were sought. A significant period of time was allowed for submissions.

Subsequent to the close of submissions, a draft position was published which took into account written submissions that were received, identified issues raised in submissions and identified a number of changes considered subsequent to submissions.

The Commission then engaged in a large series of public hearings in areas where affected stakeholders were located. Parties were invited to provide presentations in support of their submissions. Parties who had not lodged written submissions were also welcome to seek leave to appear. The meetings were open to the public, who were also given the opportunity to address the hearing.

A series of “round tables” in regional areas was conducted with identified and self-disclosed stakeholders. These meetings gave those who were unable or unwilling to provide presentations in public the opportunity to have input. At the same time, no submissions were kept confidential, the Commission recognising that the basis for its determinations must be available to all.

Importantly, present at the hearing were three Commissioners. It is vital that the decision makers themselves are available to stakeholders, rather than engaging staff to undertake this task.

We understand that a final publication will be made available in 2009.

Case Study Two

CSIRO (Sustainable Yields Audit)

Getting it Wrong

In early December, CSIRO (in conjunction with a number of other Government entities) conducted a regional "consultation" series with respect to the Sustainable Yields Audit. The series was, in our opinion, ill-informed, poorly organised, poorly executed and poorly received.

In late November, CSIRO sought advice from NSWIC over the format and timing of the series. We provided advice that:

- The series did not cover sufficient regional centres to engage all stakeholders. In particular, Northern NSW had not been included;

- The series should not be by invitation, but should be open to all comers given the implications not only for irrigators but for the communities that they support;

- Ninety minutes was vastly insufficient to cover the depth and breadth of interest that would be raised by attendees; and

- That the timeframe between invitation and the event was insufficient.

None of that advice was adopted.

Invitations were sent to an undisclosed number of stakeholders who had been identified by an undisclosed method. In the short space of time available to advise attendance, CSIRO threatened to cancel a number of sessions on the basis of low responses. Given the limited notice and invitation list, NSWIC became aware of a number of stakeholders who wanted to attend but were unable to.

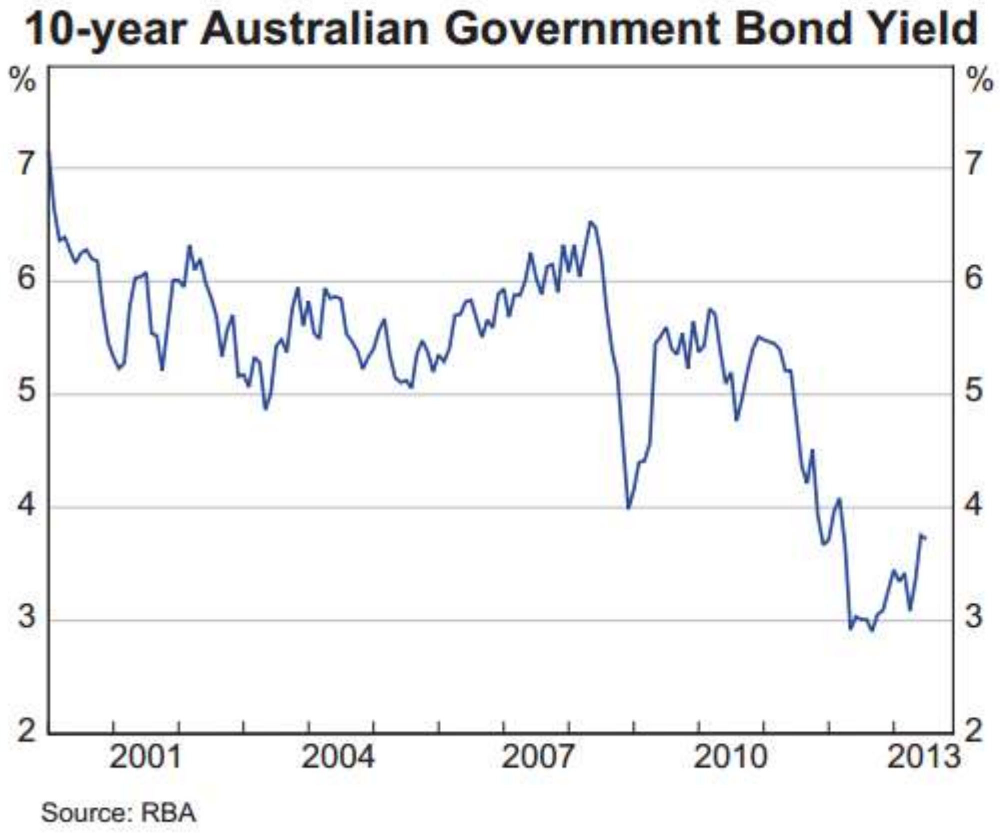
During the sessions, information was presented as a "briefing" despite being described as consultation. As such, extremely limited time was available was questions to be addressed – a key feature of consultation. Moreover, where information that was presented was questioned, a defensive stance was taken – a key feature of lack of willingness to engage stakeholders in a consultative fashion.

In particular, NSWIC is particularly concerned at the lack of willingness to engage on factual matters contained within the report. Where glaring inaccuracies were pointed out, defensiveness was again encountered. In several instances, inaccuracies that had been advised by stakeholders were perpetuated in later documents.

Further, several presenters were clearly not aware of the full range of detail surrounding the matters that they discussed. It is imperative that those seeking feedback on a subject understand that subject in depth prior to commencing consultation.

Appendix B

<u>The Australian Economy and Financial Markets - August 2013</u>



http://www.rba.gov.au/chart-pack/pdf/chart-pack.pdf