CANEGROWERS

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Mr Charles Millsteed
Chairman
Queensland Competition Authority
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By email: charles.millsteed@qca.org.au

Dear Mr Millsteed

Rural irrigation pricing review 2020-24

Thank you for the opportunity to make a submission to QCA's Rural Irrigation Price Review 2020–24.

Representing around 75 per cent of Australia's sugarcane growers, CANEGROWERS is the peak body for the sugarcane industry in Australia. The Queensland sugar industry relies heavily on irrigation. The cost of the electricity used in that task is threatening the international competitiveness of farmers in our industry and in other agricultural industries across the state.

CANEGROWERS is also an active member of Queensland Farmers' Federation (QFF) and endorses the points raised in the QFF submission to this review and its accompanying response to the QCA Consultation Paper – Apportionment of Dam Safety Upgrade Costs.

CANEGROWERS is seeking prices that encourage the efficient use of irrigation water across Queensland's irrigation schemes.

The connection between water and energy costs and policy settings for the efficient delivery of water is a major issue for irrigated agriculture in Queensland. CANEGROWERS is deeply concerned about the cost of delivering irrigation water on farm and the hike in irrigation water prices that is likely to flow from the irrigation pricing review. Already, the cost of irrigation water combined with the cost of electricity to pump that irrigation water is causing many growers to reconsider their use of irrigation water and irrigation practices. For some, this means taking the risk of deferring irrigation in hope of rain. Others are switching intensive (irrigated) to extensive (dry land) agriculture in search of cost savings. The diversion of resources is reducing the efficiency and value of agriculture across the state.

CANEGROWERS members have been active participants in the State government's process aimed at enabling the transfer of management of SunWater's irrigation distribution systems to Local Management Arrangements (LMA). This process has resulted in the participants developing a clear understanding of the costs of delivering irrigation water in each of SunWater's channel irrigation schemes. It is important that the 2020-24 price path is based on the prudent and efficient cost of delivering irrigation water. SunWater's processes produce inflated cost structures in several areas.

Non-Routine expenditure

Insurance

According to SunWater, flood damage has been a major contributor to large negative annuity balances in Bulk schemes. Some of the increase in negative annuity balances is attributed to unresolved insurance claims. It is important that the costs of damage associated with any unresolved insurance claims are excluded from the relevant SunWater annuity balance for use in the calculation of costs and prices in the 2020-24 price path.

Asset Management

The processes embodied in SunWater's Asset Management System (AMS) are inefficient and are driving up the cost of non-routine expenditure. For example, the cost of conducting asset condition assessments is high. In some cases, these reports have been used to extend asset lives. For relatively small assets, the cost of producing the asset report can be higher than the values of the asset being reviewed.

In setting the current price path, QCA made an allowance totalling $69.16 million for non-routine expenditure for 2013-18. SunWater's actual/forecast non-routine expenditure for the same period was $146.57 million. This significant overrun calls into question SunWater's internal cost control systems, the integrity of its financial model, and operating and capital expenditure forecasts.

Routine expenditure

Overheads

CANEGROWERS is concerned at the large increases in overheads for most of SunWater's distribution schemes in 2017-18 and 2018-19 years. The allocation to irrigators is up $6.5 million (a 59% increase) over the two years.

The cause of these increases is not well explained, and SunWater's cost allocation methodology is opaque.

Operating expenditure

There has also been a $7.6 million (19%) increase in SunWater's operating expenditure attributed to irrigation over the same period. SunWater's modelling has this expenditure increasing over the 2020-24 price path.

Electricity

Accounting for approximately 20% of SunWater's routine expenditure, electricity has become a major component in the cost of delivering irrigation water. The treatment of electricity in the present review is likely to have a significant impact on the price of water in the 2020-24 price path.

The review is occurring at a time when Energy Queensland is reviewing its network pricing structure for both its Energex and Ergon distribution networks. Reflecting the AER's new Rate of Return guideline, the cost savings Energy Queensland is targeting for its networks and the new tariff structures under consideration, it is likely that there will be a significant reduction in network prices in the forthcoming electricity regulatory period. It is important that these expected reductions are taken into account in the new irrigation water price path.

Rather than being a simple pass through of electricity costs to users, it is important that the treatment of electricity provides SunWater with incentive to optimise its use of energy and the efficiency of its pumping systems.

Insurance

If the full cost of insurance is to be passed on to water users, QCA needs to ensure all works that are relating to possible claims are removed from the non-routine costs.

CANEGROWERS supports QFF's recommendations that:

- All flood damage costs that are, or could be, related to an insurance claim be removed from the non-routine expenditure.
- Any outstanding claims be removed from the calculations of the annuity as QCA recommended for the previous pricing review.
- A detailed review of insurance costs be completed to establish the correct allocation of the costs as well as the prudence and efficiency of the costs being proposed by SunWater.

Inspector-General Emergency Management (IGEM) costs

SunWater has an active role in Queensland's flood management activities, including emergency action, as required for planning for flood mitigation as well as monitoring and reporting of seasonal flood events. The cost of SunWater's 'flood room' is $2.5 million.

The information gathered and distributed by SunWater, used by the Bureau of Meteorology, and Queensland and local government agencies including local disaster management groups, is a community service. The benefits of this community safety and awareness program flow to the wider downstream community, not just to irrigation water users. The costs associated with this public service should be borne by the state government as a community cost. They should not be treated as private costs.

Bulk water costs for distribution losses

There has been an increase in calculated distribution losses arising from changing Headworks Utilisation Factors (HUF) and Dam Improvement Plans (DIP) to address dam safety. Against this, following the LMA process, SunWater has an increased ability to deal with unused distribution losses. These can be seasonally transferred (traded) and, in some schemes, carried over.

The net effect of these changes is an increase in management flexibility to minimise distribution losses, not an increase in actual distribution losses. With additional water available for productive use, the charge on users for distribution losses should be lower than in previous periods.

Implementation of cost reflective Part B & D prices

Based on information contained in SunWater's financial model, there will be a significant increase in irrigation water prices in the first year of the 2020-24 period. Such an outcome would be unwelcome news for the irrigated agriculture across Queensland.

The referral notice for the present review requires QCA to balance '*the legitimate commercial interests of the businesses with the interests of the customers, including considering less than cost reflective volumetric prices which are necessary to moderate bill impacts for customers*.'

In the present irrigation water price, where prices are seen to be below cost reflective levels, the total price has increased by $2 per megalitre plus CPI each year. The referral notice specifies an annual price increase of $2.38 per megalitre plus CPI, for the fixed components (parts A & C), where the prevailing fixed price is below cost reflective level. Parts B & D are to be increased to cost reflective levels immediately, subject to there being a moderate bill impact.

CANEGROWERS recommends that the QCA recommend the continuation of the government's present pricing policy so that where prices are below cost reflective levels the total price increase (Parts A, B, C & D) be limited to $2.38 per megalitre plus CPI.

Dam safety
CANEGROWERS is concerned that the increases in dam safety requirements will impose significant additional costs and result in significantly higher bulk water prices, with increases of more than 200% in some schemes. These increases, if passed on in full, would significantly reduce the viability of SunWater’s irrigation distribution schemes.

Governments and the community more generally, have a wider perspective than private economic benefit from water use. Reflecting this, legislative and regulatory compliance are primary drivers for the dam safety upgrades. The additional measures are designed to protect the downstream communities. The dams themselves provide flood mitigation services by enabling the storage of water, and in most years, the management of water discharges. Flood mitigation has enabled the growth and development of urban communities on the downstream flood plains.

The provision of water for irrigation purposes does not carry solely private benefits. The schemes contribute to the social and economic fabric of the regional communities they help sustain. Significant public benefits flow from the growth and development of vibrant regional communities. It is important that this community service role is taken into account when considering investment decisions such as dam upgrades and determining the private/public mix when calculating cost recovery contributions.

Where the government requires dam owners such as SunWater, to carry out activities or make investments that they would not otherwise do on a private basis for commercial gain, those activities and investments should be seen as activities intended to meet a government objective, with the associated costs met by government in the form of a community service obligation (CSO) payment.

The regulated increases in dam safety and associated costs are designed to provide a public benefit to the downstream urban communities, not irrigators.

CANEGROWERS recommends dam upgrade costs be treated as a public expense not as a private charge on water users.

Conclusion
Significant community benefits flow from having vibrant regional communities. In many regional areas, irrigated agriculture is a cornerstone of those communities. The long-term viability relies on irrigation water being delivered efficiently and cost effectively. SunWater’s processes has produced a cost structure higher than a prudent and efficient level. These costs will be further inflated, unless the public benefit of regulated increases in dam safety requirements are taken into account and borne by government as a CSO payment.

Yours sincerely

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Chief Executive Officer

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