Bundaberg Regional Irrigators Group

Representing member irrigators in the Bundaberg Irrigation Area

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SUBMISSION TO QCA
Draft Report
SUNWATER PRICE REVIEW: 2012-17

INTRODUCTION

Bundaberg Regional Irrigators Group (BRIG) was established to represent irrigators in the Bundaberg district across a range of commodity groups including sugarcane, grain and horticulture.

The Board and management of BRIG are all stakeholders and irrigators and have the resources, responsibility, maturity, infrastructure, ability and desire to deal with all issues that have impact upon us as irrigators in the Bundaberg Irrigation Area. Because we use the infrastructure and have done so since the inception of the scheme, we have a much better understanding of the system and how it operates, than others do.

BRIG believes that QCA has done a very commendable job, particularly when the disgraceful performance of SunWater in this process is taken into consideration. SunWater's inability to supply QCA, QCA's consultants and their own customers with accurate and timely information during this cost setting process requires an in depth investigation by the shareholding government ministers.

BRIG will be seeking to further progress such a review over the coming months.

Of particular note is SunWater's appalling record in relation to overhead expenditure with direct operating costs being \$2.3 million less than the consultant's forecast over the 2006-11 period while non-direct costs were \$7.8 million above forecast (refer page 164 of Vol. 1).

BRIG also intends requesting the State Government to improve its supervision of SunWater's management, governance and board procedures so that all expenditures are properly authorised.

We refer specifically to comments on the absence of board approval on page 24 of Vol. 2 Bundaberg Distribution and page 100 of Volume 1 where Aurecon found that a number of activities did not have a board approved budget.

It is also very difficult to have any confidence in the accuracy of the information supplied from SunWater's Brisbane office with factual errors being commonplace.

BRIG is very concerned that the QCA draft report suggests that customers did not show sufficient interest to comment on many issues. This is clearly not the case as in most instances this draft is the first exposure customers have had to the material. As the report states, SunWater was still changing its position and supplying additional information to QCA as late as October 2011. Customers now have a very compressed time frame to respond.

Once again this demonstrates the lack of respect that the current SunWater board and management have for their irrigation customers.

More specific comments on particular sections of the report follow:

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1. BRIG agrees that SunWater should immediately improve its record keeping so that the next price setting process can proceed in a timely and more accurate fashion. We concur with QCA that SunWater's Statement of Corporate Intent and relevant legislation be amended to require SunWater to consult with customers in relation to and publish on its website annually updated NSP's. (Refer page xli Volume 1)

2. BRIG does not agree with end of regulatory period adjustment for significant under or over recovery of costs in the current pricing. The currently proposed system for electricity costs is not acceptable as it could lead to large inter-generational shifts in price between years. This is of particular concern in the Bundaberg Distribution System where at least 1/3 of the cost is electricity. The price of electricity is uncertain over the coming 5 year period with the impact of the carbon tax still unknown. In addition the amount of electricity used per ML pumped can vary with delivery point, time of use and changes in pump efficiency and transmission losses in various channel sections.

   BRIG believes that an electricity cost pass through mechanism (a year in arrears) audited by QCA is the only transparent and acceptable option and that electricity should be a separate tariff component. This approach could be limited to schemes where electricity makes up a significant portion of the total delivery cost. BRIG proposes that the tariff structure be further unbundled to:

   Part A = Bulk Fixed Charge
   Part B = Bulk Volumetric Charge
   Part C = Distribution System Fixed Charge
   Part D = Distribution System semi variable volumetric charge
   Part E = Distribution System electricity volumetric charge

The uncertainty and impacts associated with the proposed carbon tax, the Authority's pending review of Queensland electricity tariffs and the proposed annual review of the cost differential between contestable and franchise tariffs mean that electricity costs cannot be estimated with any acceptable level of confidence.

With Part E operating as a cost pass-through mechanism for electricity only, the requirement to estimate uncertain future electricity costs is negated and it also removes the potential need for inequitable and clumsy end-of-regulatory period adjustments.

Price signal transparency is also achieved and allows end users to better match marginal cost and marginal benefit to use of additional water. (Refer page 49 Volume 1)

3. Similar comments to those made in 2 above can be made in relation to the renewals annuity. BRIG understands that QCA is currently reviewing the split of the existing Bundaberg renewals annuity balance between the bulk and distribution systems. BRIG believes that the current split is clearly unfair as the river irrigators that have paid above lower bound for many years are now incurring higher charges because their balance as proposed by SunWater is negative while the distribution system has a positive balance. BRIG awaits the reviewed proposal with interest.

4. BRIG also believes that SunWater has been unable to justify the high level of overhead costs as currently being presented in the NSP's. Inaccurate time keeping during the current price path is acknowledged and as this drives the distribution of these costs, SunWater can hardly expect customers to accept what appear to be ridiculous levels of overhead charges. BRIG understands that time keeping has now been improved. BRIG proposes that QCA review this new data on an annual basis during the 2012 to 2017 period until transparency is achieved.

5. Clearly labour is the largest component of SunWater's costs even where high electricity costs are incurred. Further to 4 above, BRIG believes that SunWater has not demonstrated any ability to manage its labour costs in an efficient manner:

    - BRIG is surprised that QCA has not commented on SunWater's inability to use a zero base budgeting approach
    - SunWater appears to adopt a budgeting approach that keeps employee numbers constant even though it justifies some capital expenditure by claiming labour savings
    - BRIG requested the QCA consultant examine the question of whether SunWater had appropriate levels of staffing and mix of contractors and its own employees at its operating locations. This issue does not appear to have been addressed in any detail. BRIG acknowledges that this issue was investigated at head office.
    - On page 233 of Vol. 1 QCA quotes a Deloittes report which suggests SunWater's treatment of unutilised labour is unusual.

6. BRIG supports the QCA proposals in regard to improved consultation between customers and SunWater. (Page 83 Volume 1). Local management in some form is

clearly required. BRIG believes that QCA should strengthen its current recommendation by recommending specific changes to the legislation so that SunWater **is required** to meet these targets. SunWater's comments made on this matter in their NSP could at best be called inaccurate and are simply not true.

7. BRIG does not accept that SunWater is entitled to interest on working capital charge however small it may be. Customers pay their allocation charges quarterly in advance and this, along with the credit terms provided by suppliers should be more than adequate to provide the working capital requirement of the irrigation schemes. It is also reasonable for irrigation customers to suggest that irrigators are providing all of SunWater's working capital requirement. A much more detailed justification will be required before BRIG will accept that this new additional charge is justified.

8. Insurance is a very significant cost in the distribution system. The draft report clearly states that SunWater purchases its insurance in a relatively transparent and competitive manner. However, QCA and its consultants have not yet addressed questions raised previously by BRIG:

   - What types and levels of insurance is SunWater purchasing?
   - Does SunWater have the most cost-effective blend of self-insurance and insurance?

   The statement on page 187 of Vol. 1 attributed to SunWater is nonsense.

   BRIG is of the opinion that SunWater will over-insure to avoid any risk as its customers pick up the entire cost. There is no incentive at present for SunWater to optimise its insurance cover. BRIG requests that QCA examine this matter further.

9. BRIG can understand SunWater needs professional indemnity insurance for its consulting business and is well aware of the costs involved. SunWater has not yet presented an acceptable argument to justify the need for this particular insurance when operating existing irrigation infrastructure. Again BRIG requests QCA examine this issue in more detail.

10. BRIG believes that SunWater's service standards and costs are linked. The Bundaberg Scheme has already suffered a unilateral lowering of standards by SunWater. In particular, SunWater is unlikely to maintain service standards on the higher cost sections of the scheme where pumping costs far exceed the proposed Part D charge. BRIG requests that QCA monitor service standards as these are linked to SunWater's costs.

11. The Authority's analysis on page 151 of Vol. 1 2nd last paragraph is incorrect. BRIG is aware that the design of the Bundaberg Scheme attributes flow rate limits to each outlet based on the amount of nominal allocation held. There are also outlets with no peak flow rate allocated. In the Bundaberg System WAE holders do have an entitlement to peak flow rate and a share of the system capacity.

12. Refer to page 237 of Vol. 1 where SunWater's view on cost allocation is repeated. SunWater appears to have conveniently forgotten that new Burnett Water (Paradise) allocation is delivered through the old Bundaberg Distribution System. This adds much complexity to the cost analyses as there is medium off peak (no flow rate entitlement), medium peak (has flow rate entitlement) and high priority water entitlements currently in use and unsold. It can be argued that the unsold peak water has an entitlement to some channel capacity and as such Burnett Water should be paying the Part A and Part C charges on this water.

13. Refer to Table 7.4 on page 291. Many of these semi-variable costs are only variable because SunWater has a large fixed labour pool. If there were less permanent labour, these costs would become variable. At an initial viewing it could be argued that QCA have placed too much of the scheme costs in the variable Part B and Part D tariffs thereby having big users subsidize the costs of sleepers and dozers. However, BRIG now understands that the split proposed by QCA is appropriate as it will force SunWater to control costs when water consumption is low. It will also provide an incentive for SunWater to increase usage in at least some parts of each scheme. Removing electricity from the Part D calculation as outlined in 2 above will significantly change the magnitude of Part D and the impact of varying the split between fixed and (semi) variable costs.

14. In the same vein as point 13 above, BRIG supports the cost containment recommendations made by Indec as detailed on pages 293 and 294 of Volume 1.

15. BRIG agrees that termination fees should be calculated in such a way that the remaining customers do not incur any additional costs from the transfer of water back to the river. It is clear from the current process that SunWater must be instructed to maintain proper accounting of such payments so that QCA can monitor these payments. However, there are also instances where SunWater could reduce costs as water allocation is moved throughout the system. In the past SunWater has refused to accept these cost cutting changes when requested to do so by customers.

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16. BRIG believes that the current draft reflects the issues raised in its previous submissions.

17. At the present time QCA has been unable to advise what parameters were used in the IQQM model to calculate to apportioning of Gin Gin channel costs between bulk and distribution systems. BRIG believes that very little bulk water (if any) will be transferred at the current level of sales from Paradise Dam. BRIG requests that QCA examine this matter further.

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18. BRIG believes that the level of use recorded over the 8 year period 2002-3 to 2009-10 but excluding 2002-3, 2007-8 and 2008-9 does not reflect the usage expected over the coming price path. Reasons for this position are presented below:

    - Storage levels were low for much of the recent past. This impacted on the level of announced allocation at the start of the water year (1st July). This restricts water use during spring as growers hold back irrigation in case a dry wet season ensues. Often rain falls later during summer, irrigation demand is low, announced allocations are increased in response to storage levels and the water remains unused. Announced allocation levels at year end do not reflect the availability of water during that water year. Grower records for 2009-10 show announced allocations on July 1 being 85% north side and 50% south side. These were increased to 100% on 22nd February. In 2002-2003 the records show announced allocations of 30% in February and 35% in March. In the 2005-6 water year the announced allocation was 91% at the start of the water year while in 2006-7 it was 46% for the entire water year.
      Given the current levels of both Paradise and Fred Haigh dams it is expected that storage levels will be good at the start of the 2012-13 water year.
    - The Bundaberg Irrigation Scheme is supplementary in nature with rainfall supplying most of the crop demand. The storages are too small to supply full crop demand during lengthy dry periods and the main crop, sugar cane, does not require irrigation during better rainfall periods. As a result, irrigation water use is only high during dry periods which follow a period of better rainfall. As an example some 33,400 ML have been pumped this year between July and November (100% announced allocation, low rainfall and good sugar prices). This compares with use of only 14,400 Ml in the same period of 2010.
    - Sugar prices were low during much of this eight (8) year period. They are now much higher with the industry now having the ability to lock in prices five years in advance.
    - Examining water use records for the scheme's largest irrigator shows that they used an average of 55% of allocation across the 5 years used by QCA in its calculations. This includes the 2006-07 year where announced allocation was 46%. They used 98% of their announced allocation in that year.
    - Excluding the dry 2006-07 year the largest irrigator in the Bundaberg Scheme used an average of 57% across the 4 wetter years.
    - In its NSP, SunWater proposed using a usage level of 50%. It would be expected that SunWater would be very conservative in making this estimate.

BRIG Requested QCA to model the effect of 55% usage in both the Bulk and the Distribution components of the scheme.

- Bulk Supply:
  - forecast irrigation usage changed from 46.7% to 55.0% of WAE
  - forecast urban and industrial usage changed from 46.7% to 55.0% of WAE

- Distribution System:
  - forecast irrigation usage changed from 43.1% to 55.0% of WAE
  - forecast urban and industrial usage changed from 43.1% to 55.0% of WAE

The impact on cost reflective prices and recommended tariffs is as follows:

Tariff Category	Draft Report		Revised Usage 55.0%	
	Cost Reflective	Recommended	Cost Reflective	Recommended
Bundaberg Bulk Supply:				
Part A	$5.94	**$11.14**	$5.94	**$11.21**
Part B	$1.10	**$1.10**	$0.93	**$0.93**
Bundaberg Distribution System:				
Part C	$45.21	**$31.27**	$45.21	**$37.68**
Part D	$63.36	**$63.36**	$48.79	**$48.79**

BRIG believes that 58% would be a more appropriate level of water use on which to base the Part D calculation. The impact of variation between the use estimate and actual use is significantly reduced if the electricity costs are passed through as outlined in 2 above.

19. The 2012-13 Dinner Hill pump station replacement project refers to labour savings. There is no indication that these have been considered in the operating cost budget.

20. Contrary to the approach taken in other schemes QCA has not taken reduced the renewals annuity costs associated with Gin Gin channel relining. A reduction of some $4M could be achieved by replacing the concrete with plastic. BRIG believes that would be a prudent change. Once again a capital expenditure project would reduce water loss and pumping costs and it is expected that such savings would be factored into future operational cost calculations.

21. If large amounts of new water allocation are sold during this price path, BRIG believes that this price determination should allow QCA to recalculate these tariffs, with the additional SunWater income included.

22. BRIG will continue to dispute the competence of the SunWater systems in relation to pipeline replacements that impact significantly on the reliability of supply to a small number of outlets (refer page 31 of Vol. 2). They have no incentive to do this when the cost of delivery to some channel segments exceeds their Part D return.

23. Refer to page 47 of Vol. 2. The issue of ROP compliance costs is complicated as the ROP applies to the new Burnett Water and the old water. It can be argued that the ROP compliance costs were not incurred until the new storages were built and that Burnett Water should pay all of these costs. At the very least these costs should be spread across all of the allocation and just not the allocation that is in use. BRIG requests QCA examine this issue to ensure these costs have been correctly recorded and split across the two sources of water.

24. Refer to page 51 of Vol. 2. Distribution. The last para on this page suggests that irrigators are paying a share of the overhead costs associated with SunWater's Infrastructure Development Unit. BRIG is unclear as to the functions of this unit but assumes that it deals with "new water" projects and if this is the case BRIG believes that these costs should not be paid by existing schemes.

Additional Comment and Further Submissions

This submission has been developed in response to the information provided in the QCA draft reports released November 2011.

BRIG anticipates that further information will become available to allow stakeholders additional informed comment on the issues to be addressed.

As such BRIG may raise additional issues, or provide further detail on issues identified in this submission to QCA.

Should any further information or clarification on any aspect of this submission please contact Mr Dale Holliss, Co. Secretary, Bundaberg Regional Irrigators Group Ltd on (07) 4151 2555.

Yours faithfully

[redacted]

MA Smith
Deputy Chairman