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18 November 1998

The Presiding Commissioner
John Cosgrove
Impact of Competition Policy Reforms Inquiry
PRODUCTIVITY COMMISSION
PO Box 80
BELCONNEN ACT 2616

Dear Commissioner Cosgrove,

Colly Cotton Limited (Colly) is a publicly listed company principally growing irrigated cotton in northern NSW. The purpose of this letter is to make submission to the Inquiry into the impact of national competition policy (NCP) reforms on rural and regional Australia.

In summary, although financial benefits from the reforms in the electricity industry have been substantial, there has been no benefit to irrigators from water reforms. The reverse has occurred. Irrigation farmers are worse off in terms of the provision of services, lower water reliability and higher prices.

Electricity

The price of electricity to Colly has dropped since the implementation of the reforms. This is an important benefit because Colly is a large user of electricity, principally in its cotton gins and in the pumping of irrigation water from the northern rivers on to irrigated land and water storages.

Water

Unlike electricity, which, since deregulation, has become relatively competitive, water is stored and delivered by a monopoly supplier. This fact has been relied upon by the NSW Government and its water authority, the Department of Land and Water Conservation (DLWC), in their response to pressure for water management and pricing reforms. The DLWC has a total fixation on cost recovery without any regard for improving services, with no effective recourse to users. The pages below attempt to explain the difficulties experienced by northern NSW irrigators and us in the State Government's attempts to meet the reform requirements in relation to water.

The 1994 COAG Framework for Water Reform

Colly welcomed the 1994 agreement on a framework for water reform. We had expected that it would tighten up some of the many anomalies, misunderstandings and poor definition and implementation of policies in the management of water in NSW. However processes to date have, if anything, worsened the situation.

The NSW Government has taken the path of concentrating on water pricing and environmental issues under its NCP water obligations. In many ways this is sensible because many of the other features of the framework are already in force. For instance, quantity-based pricing and licensing have been in force for over 20 years in northern NSW valleys. Additionally, the principle of the separation of water rights from land titles, and the ability to buy and sell entitlements (albeit on a limited basis) have effectively been in force for many years.

As no doubt you are aware, the NSW Independent Pricing and Regulatory Tribunal (IPART) has been deliberating on bulk water pricing for the past two to three years. Colly has made numerous submissions to this Tribunal and attended a range of their hearings.

Our submissions have highlighted three major themes which we believe are completely in line with and necessary for the successful implementation of COAG's proposals: (1) the need to base water charges on an incentive based mechanism, (2) the need for the DLWC to become more efficient, service oriented and transparent in its operations, and (3) the need to recognise the inequities which exist between the highly reliable southern river systems and the unreliable northern rivers. The authorities associated with water reform in NSW have not addressed these fundamental points. We deal with them briefly below.

1. In the light of its monopolistic control of the water resource, the NSW DLWC must base its water charges on an incentive-based mechanism. For this purpose, we suggested a system of standard costs (or "zero-based" budgeting) based on the efficient operation of the supply and delivery system. These base costs should result from a consultative process between water users and the Department.

Regrettably, all the DLWC submissions to IPART provided financial data for cost recovery only, made no effort to justify the costs, and proposed ineffective efficiency indicators for the future. The result was a finding by IPART which was quite unsatisfactory from a water user's point of view. The findings based charges entirely on cost recovery. They provided no incentive for DLWC to improve their service to irrigation farmers.

2. Following on from the first point, Colly stressed the need for DLWC to become more efficient, service oriented and transparent in its operations.

DLWC is undoubtedly under pressure from many sources. But this is not the fault of the irrigator: The Department has, if anything, become less service oriented and less efficient. For instance, the Gwydir Valley Irrigators Association are now even less satisfied with the service being provided them than they were at the start of the IPART Hearings. In a recent survey they rated access to officers as very poor, customer relations as absolutely awful, and noted that agreements are not honoured. Services have contracted further and now there is no management in Moree, so the DLWC's presence is diluted even more - all at a time when water charges are being increased.

3. IPART and DLWC must recognise the inequities that exist between the highly reliable southern river systems and the unreliable northern rivers.

In the years 1981/82 to 1995/96 the average actual allocation in the Macintyre and Gwydir was 30% and 45% respectively. In the Murrumbidgee and Murray the average actual allocation over the same period was 117% and 125% respectively - around three times the reliability of the two northernmost rivers.

The charging mechanism is iniquitous because fixed charges have increased (and will increase further) to cover the DLWC's inefficient operation costs. The impact of these increases on users in the less reliable valleys is to increase the cost of water delivered very significantly (on average by three times). Gwydir and other northern river users continue to ask why they have to pay the huge fixed costs of the DLWC when their water reliability is so low. Colly believes that it would be perfectly acceptable to pay reasonable water charges in the north provided the river reliability was satisfactory.

Colly made numerous submissions on this issue of water reliability but neither IPART nor the DLWC included river reliability in their deliberations. DLWC assumed that there was sufficient commonality in the nature of the "products" (as they called their services) to allow cost sharing to be assessed at a statewide level. Then in converting costs to charges, the DLWC prepared an impact assessment. This assessment was extremely poor and misleading because:

- a. No data were provided;
- b. It is based on gross margin analysis which does not take into account the variation in overheads between enterprises;
- c. It takes no cognisance of differences in river reliability between valleys;
- d. Water requirements are questionable; and
- e. It does not take into account all costs and does not therefore include full cost recovery.

Colly also remains very concerned about the last point. The analysis of tariff structures and their impact conducted by the DLWC is based on the 1998/99 year, which is not a year of full cost recovery. Of major concern to irrigators is where these cost and pricing decisions will lead. By extrapolation of figures provided, we expect something like a fivefold increase in fees by 2002. The impact analysis does not deal with this at all. Such an increase will have a major impact on the irrigation industry in the north of NSW.

The above serves to illustrate the importance of considering all aspects of water supply and delivery by a monopoly supplier in non-competitive pricing decisions. We hope that it also illustrates that irrigators, rather than seeing some improvement in the definition of and rules surrounding their entitlements, are more confused and uncertain than they were in 1994 at the time of the COAG agreement.

Other matters

Several issues very important to irrigators seem to be bound up in political agendas over which we have no control. In particular, we thought agreement had been reached on the Barwon that all "sleepers" licences (those not developed and used) would not be renewed at time of expiry. The effect of this action would be to improve security to the environment and existing users and to fairly establish the "Cap" imposed by the Murray Darling Basin Commission. This is a particularly important issue on the Barwon, which whilst being an unregulated river, already has volumetric allocations which are transferable (within limits). However, we are now advised that "sleeper" licences will be renewed; apparently because it is politically too difficult to do otherwise. This is totally unacceptable. It clearly demonstrates a lack of capacity and desire to come to terms with important water reform matters.

There is considerable confusion about the treatment of users on the Barwon River. Suddenly, the level of the "Cap" has been reduced by 30%, for no given reason. We

can only conclude that it arises from the need to compensate for other streams in the Murray/Darling Basin which have been overallocated. This is also now inconsistent with the end-of-flow regime for unregulated rivers as it is also inconsistent with the licence classification system currently in force on the Barwon River (licences being classed as to river heights at which pumping may commence).

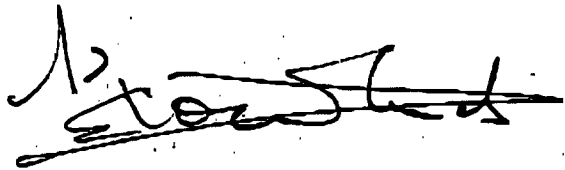
Whilst we would be pleased to provide you with more detail, we have kept our letter as brief as possible to try to illustrate that the Water Reform process has been a considerable disappointment to irrigators and their livelihood. Part of the reform process in NSW included agreement that irrigators would obtain a more secure title to their entitlements. In effect, they have become much less secure and more subject to the political influence of a wider range of groups.

Finally, we wish to point out an inaccuracy on page 11 of the Issues Paper in which it is stated that "...90 per cent of water is used in country Australia for irrigation." The percentage of flows extracted from the major inland rivers is about 30%. Thus around 70% is used for environmental, recreational, natural flooding and losses. These users get priority in poor years. An even more startling figure is the average amount of water used by irrigators in the Macintyre, Gwydir and Namoi Rivers combined, compared with the estimated evaporation from the DLWC's Menindee storages. In the period 1988/89 to 1992/93 the average diversion for these rivers together was 770 GL, and the estimated evaporation losses from the Menindee storages was 700 GL. We believe there should be a sensible balance of water use between commercial and industrial users and the environment. However, in NSW, we think much too much emphasis is placed on increasing the flow to the environment because many decision makers are ill-informed as to the facts.

We would be happy to supply you with copies of our submissions to the NSW Government if you thought they would assist with your deliberations.

We look forward to the positive recommendations that will result from your Inquiry.

Yours sincerely,



BUCKY ROWLANDS
GENERAL MANAGER OPERATIONS