MURRAY IRRIGATION LIMITED

NCP PRESENTATION – ALBURY

1 July 1999

Speaking on behalf of Murray Irrigation Ltd which is also a member of the Watering Australia Foundation, I fully support the Hon. Ernie Bridge in his condemnation of the policy and framework of COAG and the disastrous effect it is having on rural Australia.

As Chairman of Murray Irrigation Ltd I can speak with practical experience in water reform. From the outset, I want to say that MIL was not formed as a result of COAG. To the contrary, MIL was formed as the result of Murray irrigators demanding a better service and being prepared to accept responsibility for the running of a private company to achieve this aim.

Beginning as an Advisory Board in 1989 when irrigators rejected a proposed increase of 22% in water prices, eventually achieving a privatised Company in March 1995. The shareholder elected Board of MIL have transformed the inefficient Commercial Arm of Government Water Resources into a viable, efficient business. This has been achieved without substantial water price increases. Our submission to this commission dated December 1998 gives a detailed list of MIL responsibilities and achievements and these have been further developed to this time July 1999.

I put to you that good economic results can be achieved without implementing the horrendous water reforms being pursued by the NCP. Examples show that as much as MIL tries to implement beneficial changes for the business, the same endeavour is not being undertaken by the Government Agencies. The gains that MIL have made, and acknowledged by the Barraclough Report as the outstanding operator for irrigation businesses in Australia, have been burdened by the lack of corresponding reforms in bulk water and delivery infrastructure management. Pricing reforms that promotes economic efficiencies cannot be achieved without institutional reform. The DLWC can simply increase bulk water prices to achieve full cost recovery but this is resulting in our industry having to support inefficient monopolised service delivery.

MIL will seek to collect sufficient funds in water charges to maintain appropriate levels of service and ensure intergenerational equity. We have been able to successfully achieve this incorporating Sinking Funds for refurbishment of assets, a Supply Variation Fund to buffer extreme variation in resource supply as well as funds available for the business operation and Contingency Reserves.

NCP water reform promotes higher prices for bulk water. Quote: "Higher prices for bulk water are needed to promote better use of scarce water resources and halt the degradation of rivers, rising salinity in groundwater and soils in farming areas and depletion of fish stocks".

This is ridiculous! What a Policy! Put the price up – so it is uneconomic for irrigators to use and so you think this will fix everything particularly the environment and I quote NCP again: "The environment is given explicit consideration in the NCP public interest test and ecological concerns are a driving force behind the NCP water reform package".

There is no mention of productivity and the consequences of this policy. MIL is highly conscious of the environmental needs and has a staff of 10 people to fulfil our EPA Licence needs and those of our shareholders.

Further, NCP graciously explains that farmers can expand their incomes by trading and adjust to higher charges or to be removed from their enterprise by encouraging restructuring schemes to Governments.

In short, put the price up, reduce farmers and everything will be O.K. What a defeatist proposal! Australia needs increased production, needs additional storages and the needs of the environment will be achieved if the first two are supported equally.

This is a political not economic argument to increase water prices. Where is the benefit in higher prices? I suggest the NCP Policy is wrong in this area and will be unsuccessful if pursued as it is now structured.

Trade has been promoted as the answer to everything. MIL have introduced a very fast low cost transfer system. By contrast transfers on the river take up to 8 weeks which is processed by DLWC. MIL internal transfers are done instantly through computerisation. Why does the DLWC take so long and has the NCC looked at this inefficiency? The MDBC and DLWC are setting up 2 Independent Water Businesses. Has the NCC looked at the wisdom of this? The user will be paying again!

Environmental users are not subject to COAG principals – full cost recovery, renewals, etc. NCC academics and media fail to recognise the fact that the long term averaged diversion flows from the Murray River by the three States (NSW, Vic, SA) is 4,085 gls or 36% of the total average inflow into the river – Quote DLWC 25 Aug. 1995 (Murray Valley Strategic Water Management Plan) (1995 – 2000). This means 64% is not diverted and used as environmental flows.

The Fitzpatrick Report acknowledges the importance of irrigated agriculture to Australia and environmental needs to be gained by efficiency gains and Government buy-back schemes. Scientists have no clear idea what levels of environmental flows are needed to achieve ecological benefits. Dr Stuart Bunn, Associate Professor for Griffith University stated this recently and added "it was like walking towards a cliff in the dark".

The problem lies in how this environmental need has been assessed. Large funding for research, research, research ... Before any conclusions are arrived at, outlandish statements in media:

"Rivers sucked dry"
"Rivers left to a trickle" etc.

Almost every day, promoted by prominent researchers, Bureaucrats and NCC without detailed facts and planned management. NCP means you could never have another Snowy Scheme. I say the economic rationalist formulae is wrong. NCC is not supporting irrigated agriculture.

I presented a proposal to an audience of 1,500 people at Deniliquin on February 3rd 1999. The meeting was protesting about the water reforms in NSW. I called for the establishment of both an Inland Engineering Taskforce and Regional Environmental Trust. Australia is fast losing our expertise in

Engineering. We need to look at our ageing infrastructure and planning for future needs. No new significant infrastructure has been built in NSW for more than 20 years. Environmental Trusts, now successfully spreading across USA, put environmental care issues in the hands of regional communities, thereby creating a greater sense of ownership and responsibility.

I ask the NCC to support this proposal,

When will NCC insist on community democratic representation and voting criteria on the innumerable committees on water reform in NSW?
Government Agencies dictate agenda, have voting rights and give community reps little opportunity to implement their proposals. Examples:

1. Recent voting at Murray CRC Meeting. Vote which 20 For – 3 Against for a change of policy. Chairman would not allow it and said it had to be consensus.
2. MIA Environmental Flows Committee. Similar position, votes for a change desired by community was a majority but overruled by Minister. However, he accepts in majority vote rules in his Governments Caucus and Cabinet meetings.

An interesting comment recently by Minister Mark Vaile – "National Competition Policy should not be implemented for its own sake, but because there are identifiable and worthwhile benefits and approaches need to be developed which minimise the downside".

NCP Water Reforms are having a big negative effect in our area of operation. I note the Productivity Commission has asked for details of the extent of the sleeper/dozer issue. I will state our position now.

A recently competed analysis of Murray Irrigation Limited customers has revealed that over two-thirds of Murray Irrigation Limited customers have historic usage patterns in excess of long term cap levels. Average usage within Murray Irrigation Limited is approximately 111% of allocation (90% of Murray Irrigation Limited shares), which is 19% above long term cap limit of 92% given the full activation of sleepers and dozers.

In comparison with this statistic, Murray Valley private diverters and pumped districts use on average about 54% of their combined allocation, including high security. The Cabinet decision to allow this under-usage to be activated has come at the direct cost of the two thirds of customers within Murray Irrigation Limited that were encouraged by the DLWC to invest, expand and make use of the resource.

High security water users have experienced no pain as a result of the Cap to date. Indeed, the more the Cap takes effect the greater is the gain to high security water users. Irrespective of reduced allocations resulting from Cap implementation and potential penalties, high security water users have and will continue to receive their full entitlement in all but the driest 1% of years.

The new Cap for Murray Valley is now 87% which makes the position 5% less than before. The MDBC Cap was introduced on 1994 development levels. The State implemented it on a Valley basis, totally ignoring the development levels within MIL. As a result, MIL loses 260,000 mls. – 19%. Pumpers gain 50%. If you value permanent transfer at $400, this represents a loss of $104 million just to maintain farms at 94 levels.

The Cap has resulted in a cut for many water users in the Murray Valley – most of whom are shareholders and customers of Murray Irrigation Limited. The structural adjustment pressures being experienced within the MIL region are disproportionately large and potentially catastrophic to the socio-economic wellbeing of the Southern Riverina community.

Two-thirds of MIL customers are above long term Cap usage as a result of the decision to allow sleeper and dozer Licenses to be activated. Unfortunately, the customers that are most severely impacted appear to be those customers that have made the greatest efforts to improve sustainability and generate regional wealth.

It is effectively a transfer of wealth, sleepers and dozers will be able to sell water at the expense of already developed productive farms where the capital has already been invested.

Each user group should have their own Cap and the economy of each group would not have been effected. The basic problem was with the Government issuing too many licenses, 300 of which were never used at introduction of the Cap. By having a Cap on each group, expansion would take place more fairly via the transfer market.

On top of this loss to MIL, we are faced with water to be taken for:

Environmental Flows
Government, Conservationists and Scientists are working on proposals to increase flows.

Snowy River
If 28% increase in flows is granted, this will equate to drying out 475 Murray Irrigation farms – 360,000 megalitres.

Translucent Dams
Proposal to mimic natural flows prior to dams being built. Recent example in MIA - 2,200 megalitres flowed into dam - 1,900 megalitres was allowed to flow out.

Additional water for Barmah-Millewa Forest
Victorian and NSW Governments originally allocated 50,000 megalitres. Government then increased it to 100,000 megalitres. Now a proposal for 150,000 meglalitres and on top of this there is a proposal for the storage of 700,000 megalitres which could be released in one season for the environment. This again will reduce storage space for production.

Uncertainty over the impact of dryland salinity
The suggestion is that dryland salinity will increase and have an impact on water quality in the river. Then more water will be needed for flows.

Reduction of original cap a further 5%.
New maths developed to further reduce our allocation.

The return of 30,000 megalitres of water to Government for environmental use.
We originally agreed to give this amount for the environment at privatisation unaware of all these additional reductions.

All could equate to a further 21% reduction. Total in all 40% reduction. This is environmental extremism, and economic rationalism gone mad! All of this with no compensation, and no Property Rights which will continue the demise of the most important food processing industry in Australia.

The NSW Government have failed to confirm Property Rights. I therefore contend that the second tranche of competition payments should be withheld until they establish in perpetuity, Property Rights in water.

The ~~Fitzpatrick Report~~ ~~said that~~ environmental flows should be part of the normal water market and called for farmers to be compensated for water transferred to environmental uses and that Property Rights in water were needed urgently.

Yet the NCC is actually rewarding the very people who are implementing these horrendous reforms. $641 million will be distributed to the States this year alone and quote "Lower than predicted inflation and population growth have kept the dollar value of the incentives much lower than was first expected" – LAWN June '99.

Early predictions were for a $16 billion payment by 2004/2005 but will be reduced by GST. What about using some of that payment to buy back water stolen from our shareholders? I suggest the NCC should also be proposing a Ministry for water for Federal Parliament.

MIL is not opposed to a Cap, based on our development levels in 1994, but are opposed to a 19% reduction of our resource. How could you expect us to be satisfied with the present situation when we:

1. Gained agreement at privatisation to conduct the business of MIL which the business plan, insisted upon by Government, to have a minimum of 105% allocation.
2. MIL committed its shareholder members to expend $380 million over 30 years in a joint venture with Governments for Land and Water Management Plans for a total value of $500 million.
3. Agreement by State Government for a Dowry grant to fund neglected infrastructure over a 15 year period.

We are now challenged by the Australian Tax Office for:

1. Tax to be paid on Dowry.
2. A retrospective tax law amendment passed recently which will decrease asset values and depreciation claimed.
3. Land Tax to be charged on land on which our supply channels carry water. This is contrary advice provided prior to privatisation.
   MIL and MIA Boards are putting proposals to the Tax Office for the treatment of reserved infrastructure funds etc. If the NCC is sincere in supporting the rural community who are leading the way in institutional change then action needs to be taken immediately to arrest the de-

stabilisation of our irrigation industries. Irrigation is already a risky business because of the effects of climate on water supplies and the marketing risks of irrigation production.

Outcomes arising from events since privatisation:

1. Uncertainty, driving investment away.
2. Reduced farm income.
3. Reduction in Commercial service industries.
4. Reduced ability of irrigators to fund environmental programs.
5. MIL having to defend water in Yorta Yorta case costing the Company $800,000 and an appeal soon to be heard.

The ~~problem -- economic rationalism is~~ de-stabilising our communities. Our sparsely populated nation requires Government investment in existing infrastructure and plan future investment in hospitals, schools, roads, water and Government services.

Regional Services Minister John Anderson stated recently that the bush is dying and the Human Rights Commission has said the bush is losing key services in health, education, industry, social and cultural rights.

Politicians particularly are saying the rural community has to increase food production for export but on the other hand are doing nothing to assist producers to achieve this. Opposing this view, Ken Mathews, a bureaucrat from agriculture suggested "Bush is leader in growth" – I question the accuracy of this statement.
Has the Politician's role been overtaken?

I would ask the Productivity Commission to note and act upon the following MIL concerns:

1. The willingness of the NCC to branch out into crude environmentalism and support this area to the detriment of irrigation production.
2. NCC failure to support existing irrigators rights to water and prioritise the implementation of water Property Rights and water allocation requirements.
3. The Productivity Commission recognises that prices of electricity and gas can be expected to fall but water for irrigation is treated as an exception and promotes an increase in price.
4. Taxation provisions should not be biased against privatised initiatives.

One cannot stress the importance of maintaining and increasing population in rural Australia.

Less water means:	Less production
	Less exports
	Less people
	Less services

Which all equates to shrinking rural communities.

Rural Australia is hemorrhaging in MIL's area as a result of these outrageous water reform policies without any real consultation with the communities affected.

The opportunities are immense to achieve highly productive outcomes for industry and the environment but each must be treated as a joint process to get the best value for Australia and its populous.

W L Hetherington
Chairman
Murray Irrigation Limited

Murray Irrigation Limited

Presentation to Productivity Commission NCP Inquiry
1 July 1999

Water Threats

- Environmental flows
  - Translucent dams
- Snowy River flows
- Barmah/Millewa forest allocation increases
- Impact of dryland salinity
- 30,000 Megalitres for environmental use

Outcomes since privatisation

- Uncertainty - driving investment away
- Reduced farm income
- Reduction in commercial services
- Reduced ability of irrigators to fund environmental initiatives
- Yorta Yorta - Native Title Case

Impacts of Reduced Water Availability on Production Systems

Expected percentage reduction in farming activity under three different scenarios of reduced water availability.

Management Strategy	10% Reduction	20% Reduction	30% Reduction
Reduce rice production	12.16	26.50	54.92
Reduce water on summer pastures	17.13	31.37	45.43
Reduce water on winter pastures	21.68	47.54	62.65
Reduce water on winter crops	15.04	33.14	44.07

Water Pricing

- Concept of full cost recovery
- Return on capital
- Depreciation
- Sinking funds

COAG - Full Cost Recovery

- An ambiguous concept
- Pricing principles based on economically defensible principles
- Implicit assumption that higher prices for irrigation water is the solution to more efficient use

• COAG, SCARM and subsequently the NCC imply that full cost recovery is unambiguous.

• Murray Irrigation Limited in our first submission to the Productivity Commission alerted you of the difficulties with concept of the full cost recovery

• In the irrigation industry a major issue is charging for the costs of existing assets that have no alternative use. Water pricing should be based on economically defensible principles

• The simple assumption that higher water prices will lead to more efficient water use is a narrow and superficial view of the economics of irrigation farming.

•Water is only one input to on irrigation farms and product prices are only one determinant of the profitability of irrigation farms. The operations of the farm as a whole must be accounted for.

IPART

- **COAG full cost recovery agenda needed revaluation**

- **COAG, SCARM and NCC have not recognised IPART's contribution to unravelling the confused full cost recovery debate**

• Murray Irrigation Limited consider the NSW IPART process has made a significant contribution to unraveling the confusion over full cost recovery.

• There is a distinction between existing assets and new infrastructure.

• Encourage Productivity Commission to look at IPART's reports and understand the difficulties with the COAG approach to water pricing.

Charging for long-lived capital assets

- **Capital costs**
  - **Depreciation and sunk costs**
  - **Capital costs of existing infrastructure are sunk**
  - **A forward looking approach is required**

• The costs of existing capital costs are sunk. What irrigation schemes cost to create is of historical interest only.

•They have no alternative use

• In this case IPART recommended

> The proper maintenance of some infrastructure assets will extend their useful life indefinitely. No depreciation charge should be levied against them

• In addition

> Where existing assets have no opportunity cost, no rate of return is warranted in water charges

Charging for refurbishment and maintenance

- **Long-lived infrastructure must be maintained to extend its life indefinitely**
- **A mixture of debt financing and an annuity for planned expenditure**
- **Based on engineering assessment of the cost of repair and maintenance**

• Annuities approach demands answers to questions that cannot be answered with confidence

Will the asset be replaced?

When will the asset be replaced?

How much will it cost to replace the asset in today's costs?

What technology will apply?

Murray Irrigation Limited Approach

- **Cost recovery**
- **Improved environmental outcomes**

• The Government run water industry like other monopolies was subject to cost inefficiencies. The change to Murray Irrigation Limited's operation since the introduction of the an advisory board and subsequent privatisation is evidence of this.

• Other industries have seen prices fall under full cost recovery.

•There is no reason to assume that Government bulk water supplies are efficient and there is not in fact an opportunity to reduce the costs of providing irrigation water.

• Environmental issues need to be addressed directly and not indirectly through the water price.

• Murray Irrigation Limited's policies are an example of this - total farm water use, rice water policy, pollution control licence, Land and Water Management Plans.