CANEGROWERS
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Queensland Competition Authority
GPO Box 2257
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**Re: CANEGROWERS Isis Ltd Response to Irrigation Price Review 2020-24**

## Introduction

The Bundaberg Irrigation Scheme (BIS) was developed as a nation building project by both the Federal and State Governments. The scheme took an unacceptable period of time to build and was never fully built to the original design specifications, with some potential customers cut from the final design. In fact, other schemes in Queensland were started after this scheme and completed significantly before this scheme was finally completed.

The pressure that was applied to finish the scheme, resulted in it being completed at the lowest possible construction costs, not to a level that would deliver the maximum amount of water efficiently. This has resulted in the current problem of out of control, escalating electricity prices forcing the cost of delivering water (combined with the electricity prices that irrigators are being forced to pay) to a level that the local sugar industry is already finding unsustainable with sugar prices below the cost of production. Despite this the sugar industry has been in this region for over 130 years and has stood the test of time.

Canegrowers are often advised or encouraged to transition to high value crops, but experience has taught us to be wary. High value crops can quickly become low value due to market over supply. Sugar is a globally traded commodity which, though is subject to cyclical price movements has a degree of price stability which provides a certain level or foundation of economic stability for the region.

The demise of the sugar industry would lead to a huge inventory of stranded assets such as sugar mills, farm machinery, irrigation equipment specifically for the growing and harvesting of cane. It should be remembered that all forms of agriculture that require water for irrigation are price takers and cannot pass on any increases in water prices like all other increases in cost of production onto their customers. Even a standard CPI increases in costs of production to most irrigated reliant businesses has a major impact on viability.

Due to increasing impact of climate change such as extreme rainfall events and prolonged periods of drought, farming is becoming difficult without consistent irrigation. The purpose of the BIS is to underwrite agricultural production in the region. This provides benefits not only to farmers but to local workers, commercial businesses, sugar mills, recreational users and local, state and federal authorities. However, for these regional economic benefits to be achieved it is necessary for water to be affordable to Sunwater customers. Their capacity to pay is crucial to the success of the scheme.

Sugarcane production uses approx 70% of the water provided by the BIS in this region and is essential for the scheme's survival. If water use is priced above marginal revenue canefarmers will not apply it leading to a disastrous drop in production. Rather than focussing on costs, the government should look to developing an optimal price for water that allows for the BIS to realise its full potential for all stakeholders and the regional economy.

**Cost Reflectivity**

As the Bundaberg Irrigation Scheme was built as a nation building project before COAG and the NWI and it still is a major driver of the Bundaberg and district economy, it is our belief that there should be a Government Community Service Obligation (CSO) in place. The Scheme was never intended to be a stand-alone commercial venture and if the current pricing methodology was in place then it would not have been considered nor constructed as it would be unviable.

The cost increases recommended by Sunwater in the first year of the price path will be 18% in the Bundaberg Irrigation Scheme if QCA does not consider and recommend under section 1.4a) of the referral notice "balancing the legitimate commercial interests of the businesses with the businesses of customers, including less than cost reflective volumetric prices which are necessary to moderate bill impacts for customers". In the final year of the proposed price path the potential increase is 40% in the BIS. This is unaffordable and unsustainable.

In summary, it is our view that the base premise of cost reflectivity in this price path is flawed due to:

- the BIS scheme providing a major regional economic benefit; and
- loading all costs onto one group of beneficiaries ie irrigators is unfair and doomed to failure

**Moderate Bill Impacts – Capacity to Pay**

In our view the term 'modify bill impacts' directly relates to *capacity to pay* over this price path period and should be defined as such.

CANEGROWERS Isis Ltd has engaged the experienced (45yrs), independent and certified irrigation consultant Pat Daley (Daley Water Services) to prepare a report detailing the capacity to pay issues facing irrigators in the Isis- Bundaberg region - refer Attachment 1a).

This report uses three actual case studies (high pressure winch, centre pivot and furrow flood) to demonstrate significant capacity to pay issues under the current and proposed price path for water. The report is underpinned by a Water Price Analysis Tool which compares marginal costs against marginal revenue for application of irrigation water (refer Attachment 1b). This Tool, which provides a calculator, sensitivity analysis, output tables and graphs, was developed to help demonstrate the impacts to grower's profitability and sustainability of water and pumping cost variations for each of the common irrigation system types used in the Southern Cane growing regions of Bundaberg, Isis and Maryborough. This work has demonstrated that irrigators do not have the current or future capacity to absorb any more price increases for water. In the short term it is also not possible to transition to other crops or more efficient irrigation systems to offset rising prices in water, refer Attachments 1a & b.

Also highlighted in this report are a number of critical factors constraining irrigators in this region and impacting directly on their capacity to pay including:

- capacity to convert water to crop yield which translates into productivity and profitability to help buffer escalating input costs the key ones being water and energy ie ***" Crop yield is pivotal to help dilute the cost of all other grower's inputs and is critically linked to water costs, water***

***availability, Irrigation Water System (IWS) system capacities and farm irrigation system efficiencies".***

- The delivery system, managed by Sun Water, has not been designed or maintained to cope with the current or projected water supply demand. Therefore, buying additional IWS allocation or paying more for existing allocation entitlements makes little to no sense, if irrigators cannot increase the instantaneous flow as required and take advantage of potential increases in productivity and profitability.
- Uncertainty of new power tariff cost, water cost and SunWater's ability to deliver allocations at consistent flows make it difficult for growers to calculate return on investment on any proposed system upgrades.
- Increased costs and decreasing crop value are preventing many growers from investing in more efficient irrigation systems; and
- The current set price of irrigation water and required energy to deliver that water to its source is already unsustainable for those irrigators that have no other option but to use high pressure systems on their farms. These options are often limited by farm layouts or design required to suit both landscape topography and or soil conservation requirements. The current set price is also having huge impacts on the profitability and sustainability of other irrigators operating high capital cost irrigation systems.eg. Centre Pivot, trickle systems; and
- Any further water resource or electricity price increases will undoubtedly result in growers having to reduce or cease irrigating due to their inability to cover water costs. In addition, they will be required to re-assess their ability to implement improvements to irrigation infrastructure due to extended Return on Investment ROI) timeframes ie a poor return on capital.

In summary, it is our view, capacity to pay impacts also include:

- Currently sugar price is below the cost of the production and even at average long term sugar prices the cost of water does not justify irrigation (refer Attachment 1a & b – consultant report) – below cost of production; and
- It is not simply a case of planting higher value crops because of the long lead/ lag time until they generate any income or profitability combined with huge initial capital investment. High value crops do not necessarily equate to high profit as is sometimes assumed. Often high gross income equates to high risk with an ever-increasing risk to 'whole of crop' loss as climate becomes more variable. Effectively, growers cannot afford to transition to other crops eg 10 years to transition to a macadamia crop to be profitable. During the last price path review tomatoes were regarded as a high value crop option, tomatoes are now only a minor crop in the irrigation area, this goes to show that the value of crops does change over time and that changing crops is not the answer to water affordability.

**Electricity**

Reviewing the data presented by Sunwater for electricity it would appear not to reflect the step increases in 2020 for the proposed electricity demand tariff changes. We strongly urge Sunwater and QCA to focus on ensuring the correct price for electricity is utilised. This includes defining the cost as fixed or variable.

It is our view that fixed charges should be treated as a fixed cost eg electricity should be treated like any other expense with fixed and variable components with the fixed component as part of the allocation charge (Part A & C) and the variable to the volumetric charge (Parts B & D).

Fixed components of electricity charges such as the flat daily connection should be allocated to the fixed component of water charges. This is consistent with the QCA's principles established in Volume 1 of the

previous SunWater review, where it recommended that fixed costs be recovered via fixed charges and variable costs be recovered via variable (water use) charges.

The demand charge also be treated as a fixed cost as it does not vary directly with water use. This charge typically incurred whenever a pump is turned on during the month, whether for 15 minutes or for 30 days. Accordingly, the demand charge is paid in most months, however, the volume of water supplied is very variable.

We have some concerns in regard to electricity being regarded as a direct pass through cost as it takes away any incentive for Sunwater to attain any improvement in efficiencies eg using the correct tariffs or in making any improvements in how they deliver water throughout the scheme more efficiently. By having a CSO involved it would be a way of the Government encouraging Sunwater to find efficiencies.

**Termination Fees**

Growers do not have any negotiating power due to the high termination fees. Growers cannot refuse to accept Sunwater's product without paying a prohibitive cost to opt out of the scheme. In our view this is anti-competitive market behaviour as it removes irrigator's ability to negotiate.

Termination costs need to be reviewed in relation to deemed service contracts. Termination costs to this extent do not apply to any other form of distribution system eg electricity. When deemed service contracts were first established the mix between fixed and variable was different and has changed with every price path review, with no consideration on the impact of termination fees.

**Annuity**

We have great concern around how the annuity accounts are operated. We believe there needs to be a clear definition and clarity around the purpose and the use of these accounts. In summary we believe that the shortfall in annuities should not be borne by current irrigators.

It is noted that during the last price path that these accounts have been used to repair damage arising from floods, we believe that this is inappropriate as we believe these accounts were for future asset replacement by charging current users for their share of wear and tear so as future generations are not responsible for their total replacement when required.

These irrigation assets are owned by government and should be treated the same as other government assets. If a fire or flood damages a public school, it is not the students who are responsible for repairing the asset, if a hospital suffers similar damage it is not the patients responsible for repairing the asset, damage done to the state's road network as a result of flood is not passed directly to road users to recover repair costs.

In addition, the irrigation assets were passed over to Sunwater to manage, but at that point in time they were not given a separation payment to cover what should have been the annuity balance calculated from the day the scheme was formed. We understand the need for an annuity balance to cover our share of future asset replacement, however we do not believe that we should be responsible for the wear and tear that can be attributed to previous generations in determining what the current annuity balance should be.

**Non-Routine Expenditure**

With declining annuity balances being attributed to flood damage by Sunwater without any asset replacement, it is important that QCA exclude the cost of damage that is related to any insurance claim or potential claim that has incurred during this price path.

In our view there needs to be a major review of Sunwater's Asset Management System (AMS). The failure of the AMS to deliver is driving costs of the non-routine expenditure. This is due to the cost of running the AMS and the inefficiencies of the approach.

The asset condition assessments have and are continuing to push the assets replacements into the future but at the same time are consuming the annuity balances set aside to replace them through very expensive asset condition reporting. There has to be a better way with some of this work potentially being able to be done 'in house' at a lower cost.

**Insurance**

In our view there is a need to ensure that uninsurable assets are not being insured when in all likelihood insurance claims will not be approved. It may be prudent that Sunwater has some form of self-insurance for some of its assets and/or to appropriate parts of the scheme.

**Inspector-General Emergency Management (IGEM) Costs**

It is understood that most of the data used and made available by Sunwater's control room is publicly available. The dams do not make or cause floods and in most cases reduce the flooding impact caused by upstream rainfall – a flood mitigation tool.

The IGEM recommendations are passing on the responsibility to Sunwater of the work BOM and the local disaster management groups (LDMG) have failed to do well in the past. Sunwater is now attempting to pass on these costs to water users, not back to Government or to the broader community – the beneficiary. This work by Sunwater will be important however cannot be used by Sunwater in making available public forecasts during any flood event which would be done by BOM and the Local Disaster Management Groups – the beneficiaries.

If the dams were not in place there would still be a requirement to manage the risk during events to assist populated areas within these areas. The requirement to manage the risk is not brought about by the capture of water, so the cost should not be passed onto the people using the water.

Again, our question is "why should irrigators have to cover the costs that benefit the whole community and government"?

**Dam Safety**

Governments have a duty to adequately inform communities about policy reform. In this case consultation has been about the need for dam safety measures to protect communities from the impacts of dam failure in the case of unprecedented climatic events. Dam safety has not been included as part of pricing investigations to date.

The Qld Government has made no attempt to consult on this policy change or direct the water authorities to consult on the matter. In the absence of formal direction, irrigators have assumed that these costs would be a community responsibility and made their investment decisions based upon current policy settings and commercial demands.

In our view flood mitigation benefits the downstream community however in this benefit is not recognised. These costs should be recovered from the community which benefits.

**Distribution Losses**

Distribution losses for bulk water costs are becoming a major part of the distribution scheme costs. In this review Sunwater is proposing all the bulk water distribution losses allocation costs be transferred to the distribution schemes. Through the LMA process there was agreement that unused distribution losses allocation could be seasonally transferred and potentially be carried over.

In our view water users should only be costed the prudent efficient requirement for losses allocation as Sunwater has the ability now to seasonally trade the unused component. A major review of the requirements of distribution losses allocations needs to be done to maximise the allocation availability for productive use as well as ensuring efficient water charges for distribution customers.

The cost of distribution losses is increasing materially due to the projected increases in bulk water charges, driven by substantial increase in SunWater's operating and capital costs for this scheme including increases in the renewals expenditure and potential inclusion of a portion of dam safety costs (which CANEGROWERS Isis does not support on the grounds of beneficiary pays and capacity to pay).

In addition, we are of the view that distribution losses need to be verified and efficiencies achieved.

**Recreation Costs**

We agree that recreation costs should be excluded and not passed onto irrigators as the whole of community benefit from the provision and maintenance of recreational facilities.

It is our view that we would still like to understand the methodology in calculating recreation costs – inclusions and exclusions especially if it is proposed to be included in future price path processes.

**Conclusion**

In our view, given that the benefits of the Bundaberg Irrigation Scheme flow to the entire region, it is unrealistic to expect irrigators alone to pay cost reflective prices. The Scheme effectively needs a CSO to realise its full potential. For regional economic benefits to be achieved it is necessary for water to be affordable to all Sunwater customers.

Moderating bill impacts effectively translates to capacity to pay. The work, associated report and tool undertaken by our irrigation consultant Daley Water Services has demonstrated that irrigators ***do not*** have the current or future capacity to absorb any more price increases for water. In the short term it is also not possible to transition to other crops or more efficient irrigation systems to offset rising prices in water – refer Attachment 1a and b. As highlighted in this report, there a number of critical factors constraining irrigators in this region

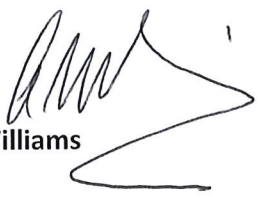
- capacity to convert water to crop yield to buffer rising costs
- the delivery system itself being able to deliver allocated water;
- Increased costs and decreasing crop value; and
- Growers being unable to afford to transition to other crops

We also strongly urge Sunwater and QCA to focus on ensuring the correct price for electricity is used which includes defining the cost as fixed or variable. As stated it is our view that fixed charges should be treated as a fixed cost eg electricity should be treated like any other expense with fixed and variable components.

Any costs associated with Inspector General Emergency Management and Damn Safety should be recovered by the community beneficiaries (the government) not irrigators.

We look forward to your response.

Sincerely,



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