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Mr E J Hall
Chief Executive
Queensland Competition Authority
GPO Box 2257
BRISBANE QLD 4001

Dear Mr Hall

SUBMISSION TO FINAL CONSULTATION: BURDEKIN HAUGHTON WATER SUPPLY SCHEME

The Authority's assessment of pricing matters in the Burdekin Haughton Water Supply Scheme has dealt with a wide range of issues. SunWater and other stakeholders have put forward their views prior to the Authority reaching a position and after its draft report through this current third round of submissions.

There are various issues in SunWater's submission on the draft report where the Authority has maintained its original position, most notably that payments for land and water allocation should be considered capital contributions with associated pricing benefits, and other matters of detail such as optimisation. SunWater has no additional comments to those contained in its submission to the draft report.

However, it appears from this latest round of documentation that the Authority may have changed its position in respect to the treatment of capital contributions for pricing purposes. The draft report stated[1]:

> *Where a capital contribution is established, there is an issue of whether irrigators have already received offsetting price benefits through lower than efficient historical prices.*
>
> *For example, if it could be established that price for 2000-01 within the price path (for which the Authority has calculated the efficient capital base) lay below the efficient cost-based price, then irrigators may have been compensated to some extent through lower than efficient historical prices.*

[1] Draft Report for Consultation, Burdekin Haughton Water Supply Scheme: Assessment of Certain Pricing Matters relating to the Burdekin River Irrigation Area. Page 31/32.

> *Determining whether irrigators have previously received offsetting price benefits, to the extent that no further compensation for the capital contribution is necessary, is difficult to establish as:*
>
> - *The historical accounting data ... is not available ...; and*
> - *it is not clear that the Burdekin Scheme was optimally staged ...*

SunWater's submission to the draft report set out a robust (and conservative) methodology for determining the extent of the offsetting price benefits, demonstrating that these benefits were consumed well within the period of development of the scheme (ie 1993). The Authority accepted this approach as representing a reasonable approximation of the past benefits of lower prices in its response to the SunWater submission, but also stated[2]:

> *The Authority also notes that the policy of less than commercial prices was designed to promote economic growth. The question then arises as to whether it is legitimate to offset the capital contributions by the benefits of past price concessions when the past concessions were part of a conscious government policy. To do so would be to negate the intended benefit. Further there is no evidence of an intention to recoup the benefits of past lower than commercial prices.*

This implies that the approach adopted in the draft report as a proxy measure to assess any excessive return on capital should be adopted as the optimal treatment, resulting in the asset base for the scheme permanently being reduced by the amount of past "capital contributions". This is at odds with the Authority's statements in various position papers and responses to submissions, including:

> *The Authority has concluded that while there was no clear statement from government that a rate of return would be charged, it was evident that governments were changing their direction in respect to pricing towards more commercial pricing practices. Initially such statements related to the Queensland Government seeking in excess of local costs of operation and maintenance, and more recently took the form of national agreements under COAG to include a rate of return, where practicable. Grower representatives were advised of these changes in December 1987 and again in October 1988*[3].

and;

> *Since the Scheme was developed, in the interests of more efficient resource allocation, the State has moved to more cost reflective and commercial pricing, including water pricing. This commenced before COAG but was reinforced by COAG and national competition policy reform. ...the Authority notes that all jurisdictions have committed to the achievement of a positive real rate of return on the written down replacement cost of rural water assets, where practicable. There is no suggestion that pre-1994 assets should be valued at zero for pricing purposes regardless of the circumstances*[4].

and;

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[2] Response to SunWater Submission. Page 2.
[3] Draft Position Paper Number 2. Page 6.
[4] Draft Position Paper Number 1. Page 4/5.

The Authority accepts that, in the past, the State Government accepted less than full commercial returns as part of a strategy to promote economic growth. That does not, however, mean that government intended those benefits to be maintained in perpetuity[5].

SunWater strongly submits that the "capital contributions" must be dealt with in terms of consumption through past pricing benefits (as originally proposed in the Draft Report) rather than by a permanent reduction from the asset base as implied in the response to SunWater's submission.

Government policy in relation to water pricing was clearly articulated through commitment to the COAG and NCP reform. At various points through the past 15 years (ie before and after COAG) the State Government signalled it was reviewing pricing policies to be more cost reflective. SunWater is not aware of any evidence that this maintenance of prices in line with inflation since the larger Burdekin development was done for regional development reasons. In fact, prices were maintained in real terms (at subsidised levels) due to Government's review of water pricing during the 1990s and its desire to maintain the status quo until implementation of the COAG reforms was complete.

In summary, the Authority appears to suggest (in its response to SunWater's submission) that prices should be constrained in perpetuity by deducing the contribution from the asset base due to in interpretation of a past Government policy. This is inconsistent with the Authority's substantive position (as set out in Position Papers Numbers 1 and 2), which indicates that it is not appropriate to unduly constraining future prices due to a past Government policy.

Proposed Approach

As discussed above, SunWater believes there is ample evidence that Government's policy was more aligned with cost recovery during the late 1980s and 1990s than regional development.

SunWater submits that the policy of regional development was extinguished at various points in history:

1980 Report to Parliament

This report, which addresses water prices from the scheme, makes no mention of setting prices to achieve regional development outcomes. While the development of the scheme *per se* was made on the basis of facilitating regional economic growth (as was the development of electricity transmission lines, ports, power stations, and rail networks) the report does not state that water prices would be the stimuli for economic growth – this development would occur due to the increased availability of water and development of new land for irrigation.

[5] Response to Submission on Draft Report: BRIAC. Page 15.

1994 COAG Reforms

The State Government's commitment to COAG reforms clearly signalled a policy commitment towards the COAG water pricing principles as articulated in the Authority's position papers. The relevant dates for consideration include:

- The 1995 commitment to National Competition Policy; and
- The 1996 Rural Water Pricing and Management framework released by Government.

The Queensland Commission of Audit Report (June 1996) further demonstrates Government's commitment to implementing COAG reforms. For example, the Committee's Terms of Reference were clearly focussed on improving the financial performance of state-owned assets such as bulk water supply to irrigators. Furthermore, the Committee's recommendation were a detailed exploration of the benefits of the implementation of COAG-type reforms in industries including water and many of these recommendations were later manifest in the *Water Act 2000*, price paths and corporation of SunWater.

2000 Corporatisation Charter

In May 1999, the Queensland Government agreed to consider the corporatisation of State Water Projects (SWP).

SWP was corporatised on 1 October 2000 in accordance with a regulation made under the *Government Owned Corporations Act 1993* on 20 June 2000. This was further evidence of the Government's commitment to implementing COAG reforms, with SunWater's charter established under that Act setting out a clearly commercial focus. Specifically, the charter provided the corporatised entity with the autonomy to set prices, subject to price paths set by Government or directives by Shareholding Ministers.

October 2000 also saw the establishment of price paths for rural irrigation water following the Water Reform Unit's process.

SunWater submits that whilst any of these three dates could be suggested as the relevant in determining the start date for past pricing benefits consuming the capital contribution, the Authority should adopt, at the latest, the COAG agreement. The methodology proposed by SunWater and accepted by the Authority can then be used to determine the date at which price benefits would extinguish.

This discussion is not to say what prices should be, but rather to determine any constraints on Government or others setting future prices.

Yours sincerely

Peter Noonan
CHIEF EXECUTIVE