Submission to the Delivery Share review team

1.0 BACKGROUND.

Delivery Shares were "created" in 2009 as part of the unbundling exercise in which I was involved. .

The initial assumptions were:

- Delivery Shares would become an asset because it provides access to channels which have a finite capacity.
- 80% of the cost of running GMW was fixed and the infrastructure access fee reflected this break down.
- Water trading and climate change would have a modest impact on the annual volumes of water delivered.

2.0 WERE OUR ASSUMPTIONS CORRECT?

2.1 Delivery Share is an Asset

There has been no positive sales of Delivery Share to date. Any sale has been in the form of compensation for the person who takes on the Delivery Share. The selling price for land also reflects DS is not an asset. When irrigation properties are sold, the DS either has no impact on the price of the farm or has a negative impact.

There is no shortage of channel capacity in the GMID. In fact water use has declined from an annual average of 2100GL to around 1100GL. Also, system efficiency will improve by 15% which creates additional channel capacity.

The policy of allowing water use of 270ML/DS was outrageous and meant that almost every irrigator had excess DS.

2.1.1 Delivery share detracts from the value of most farms because it is the single biggest determinate of water charges. The higher the ratio of water used per DS, the lower the cost/ML used. The optimum ratio of DS to water use is 270:1. This is demonstrated in table 1.

Table 1

Relationship between ML/DS and price paid for water[1]

Use ML/DS	Service	Service point	Infrastructure access	Infrastructure use $5.93/ML	Bulk Water $8.25	$/ML used
29.4	$110.00	$ 575.00	$ 2,896.00	$174.34	$242.55	$135.98
42	$110.00	$ 575.00	$ 2,896.00	$249.06	$347	$99.44
100	$110.00	$ 575.00	$ 2,896.00	$593.00	$825	$49.99
270	$110.00	$575.00	$2,896.00	$ 1,601.10	$2227.5	$27.44

2.1.2 It is a good investment to reduce DS. Some landholders have actually reduced their DS by paying a Termination Fee of 10 times the Infrastructure Access fee. This generates a 10% reduction in their Infrastructure Access charges. If they borrow money at 5%, this gives them a positive net return of 5% - a very attractive investment in today's low interest rate environment.

2.2 80% of GMWs costs are fixed

This is difficult to ascertain from GMWs annual reports. The largest expenditure type is salaries and associated costs. The allocation of staff costs to fixed and variable is likely to be arbitrary.

However, as the volume of water delivered reduces, the percentage of revenue recovered from the Infrastructure Access fees decreases. Consequently, infrastructure use fees are now significantly less than at unbundling.

2.3 Impact of Water Trading to be modest

The impact of water trading and climate change has been massive – a reduction of water used in the GMID of almost 50%. This had not been envisaged at the time of unbundling and it is my view there would have been a much different policy setting if it had.

3.0 NEW ISSUES

The unsuccessful attempts of the connections project to right size the project should be identified and incorporated into our thinking on DS.

3.1 Stock & Domestic

The cost of supplying domestic water to rural residences in rural Victoria is high. Stock and domestic schemes like the Tungamah S&D have high capital and operating costs yet a similar service is provided in the GMID virtually free. The cost of providing D&S across Victoria should not be discounted because individuals happen to live in an irrigation area. Progressive tariffs for Infrastructure Access charges and Infrastructure Use charges should be

[1] 20015-16 GMW charges

introduced so that people who live in the GMID pay a similar tariff to those that are serviced by D&S schemes.

3.2 Cost of servicing small irrigators vs large irrigators

Intuitively, the cost of servicing a large irrigator should be cheaper than a small irrigator. However, the cost of water used is largely determined by ML used/DS. If the goal is full cost recovery, a tariff policy which reflects the cost of the service being provided is warranted.

3.3 Exiting Irrigation

Since unbundling many irrigators have either sold all their water and stopped farming or scaled back the intensity of their irrigation enterprise. It is difficult to calculate the HRWS sold out of the GMID because water is no longer connected to land but most people in the industry believe the number of HRWS has reduced from 1600GL at unbundling to around a 1000GL now.

However, what is clear that properties with excess DS (water use less than 150ML per DS) are being discounted when they are sold. A recent sale in Kialla saw a discount of $300K applied to a property with 13 DS[2].

The view at the time of unbundling was that landholders who sell their water entitlements should sell their DS, or continue to pay for the running of the system y by paying an annual fee or a termination fee. This was not thought to be a big issue because nobody thought:

- DS would become an impost on a property;
- the ratio of HRWS:DS would drop from 100:1 to 60:1; and
- sales allocations would drop from 30% of HRWS to 0%

The equity of the current DS policy framework must be reviewed given the changes that have occurred since unbundling.

4.0 SUGGESTIONS FOR THE FUTURE

4.1 Right Sizing maximum water use

When unbundling occurred, the maximum water use was 200% of water right. At about this time the “20% sales deal” was done, effectively reducing maximum water use to 180% or 180ML/DS. The decision to have a maximum based on the number of days in the irrigation season was foolish and should be “fixed”. I think a maximum water use of 130ML/DS is appropriate.

The limit of 270ML water use/DS must be reduced to at worst 180ML/DS and preferably 130ML/DS.

4.2 Right Sizing the GMID

[2] Personal Communication David McKenzie Optium

GMW has missed an opportunity to right size the GMID distribution assets to match the available water resource through the Connections Program. Right sizing would have allowed the termination of DS as infrastructure was decommissioned.

Connections may have been a missed opportunity but right sizing must still be achieved. If it is not, the negative spiral of water leaving the GMID will continue because the real cost of water will go up compounding an already parlous situation.

3.2 Right sizing GMID Enterprises

Not only does the GMID infrastructure need to be right sized, the enterprises it supports must also adjust to the economic realities of farming. The number of residences and hobby farms being serviced in the GMID is increasing and the number of commercial farms is decreasing. However, the burden of maintaining the system falls largely on the people who had large water rights at the time of unbundling.

4.3 Infrastructure Access Fee vs Service Point Fees

The question of how to recover fixed costs is interesting. GMW policy of phasing in full cost recovery for service point fees over a long period was irresponsible because it did not give irrigators the appropriate signals during Connection negotiations on service points. In spite of this missed opportunity, ***GMW should immediately adopt full cost recovery for service points.***

An increase in Service Point charges will be accompanied by a reduction in Infrastructure Access fees.

Perhaps the minimum DS per serviced property should be increased from the nominal .02DS to .5DS or even 1DS to spread the load more fairly.

4.4 Stock and Domestic

Residences on serviced properties in the GMID should pay an equivalent tariff to those in schemes like the Tungamah Scheme. This can be done by implementing a minimum DS for a serviced property and a variable infrastructure use tariff.

4.5 Variable Cost Recovery to Reflect the Cost of Service Provision

A charge per ML water used is an appropriate way to recover variable costs. However, large irrigators are cheaper to service than hobby farmers and this is not currently reflected in the current Tariff. Murray irrigation has a sliding infrastructure. However, as mentioned above, a sliding scale of charges

5.0 RECOMMENDATIONS

5.1 Immediately reduce the max water use per DS to 130ML/DS.

5.2 Fully implement the service point charging policy immediately.

5.3 Develop a program using termination of DS and service points as well as other levers to right size the GMID footprint.

5.4 Increase the minimum DS for a serviced property to .5DS.

5.5 Implement a sliding scale of volumetric charges similar to Murray Irrigation to reflect the cost of delivering water to small users.