

Institutional Options Hughenden Irrigation Project

Current as at 18 June 2021



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Institutional Options

Hughenden Irrigation Project

1. Executive Summary

1.1 Overview

Jacobs has been engaged to prepare a detailed business case (**business case**) for the development of:

- (a) a water storage in the Flinders River catchment on Saego station, 45km north-west of Hughenden (, and
- (b) an irrigation scheme on the southern side of the Flinders River.

The proponent of the project – Hughenden Irrigation Project Corporation Pty Ltd (**HiPCo**) – envisages the ultimate owner and operator of the Irrigation Scheme will be an entity owned by the customers of the Irrigation Scheme, that is a locally managed entity (**LME**). The ownership and operatorship of the Water Storage has not been determined.

This report sets out possible entity, institutional and governance arrangements and related strategic considerations for the project. The report considers:

- (c) ownership and operational options for the Water Storage
- (a) ownership, institutional and governance arrangements for the Irrigation Scheme
- (b) the options for 'ownership' of the water in the project, and
- (c) the possible contractual arrangements between the LME, customers and Water Storage owner/operator.

1.2 Raising funds from customers

The most likely funding model for the project is some funding from producers with a non-equity contribution from Government. This will require future customers to agree to commit funds to the project in return for equity (shares) in the LME and a right to receive water from the project and land in the Irrigation Scheme. The LME will use these funds to finance the project.

Under the Corporations Act, there are specific disclosure requirements which must be followed by a Company when it issues securities (shares)¹. In particular, unless a specific exemption applies a prospectus (or other disclosure document) must be prepared and lodged with ASIC. We anticipate that a disclosure document will be required as part of the capital raising process for the project.

The process of issuing a disclosure is significant and will require specialised legal and financial advice. The time and cost of this process should be considered as part of any feasibility study².

¹ Section 708 of the Corporations Act

² Our estimate is that the preparation and issue of the disclosure document could cost between \$500,000 and \$1million for legal, engineering and financial modelling.

1.3 Overview of key issues, considerations and recommendations

No	Issue	Options/requirements	Considerations	Recommendation
1.	Ownership of the irrigation scheme	<ul style="list-style-type: none"> Customer owned entity (LME) Government owned entity 	<ul style="list-style-type: none"> Strong evidence from other schemes that LMEs can operate on a substantially lower cost base than Sunwater and with services more attuned and responsive to local customer requirements. There is precedent for Government supporting LMEs to own and operate irrigation schemes. 	The irrigation scheme be owned and managed by an LME.
2.	Corporate structure of LME	<ul style="list-style-type: none"> Company limited by shares Company limited by guarantee Cooperative (single) Cooperative (dual) 	<ul style="list-style-type: none"> The five existing Queensland LMEs include examples of all four of the options listed, so all are feasible and have benefits from ownership/management perspective. A company limited by shares provides the most appropriate vehicle to accommodate the requirement to raise capital to construct the project. Will need to determine whether the objectives of the entity include making a profit, noting that any profit margin would increase prices for customers. 	<p>The LME be a company limited by shares, whose shareholders are customers.</p> <p>The company be a not-for-profit entity with all revenue to be re-invested into operation and maintenance of the Irrigation Scheme.</p>
3.	Board composition	<ul style="list-style-type: none"> Set total number of directors Prescribe number of independent and member directors 	<ul style="list-style-type: none"> Independent directors can be critical to bring both expertise and independence to the decision-making process. This is particularly important when setting prices. Need to strike balance between sufficient directors while not adding unduly to cost; also need to consider potential pool of member directors. Other Queensland LMEs have set the total number of board members at between three and seven, with five directors (two independent, three member) most common. 	The board include five directors, including two independent directors.

No	Issue	Options/requirements	Considerations	Recommendation
4.	Voting rights of shareholders	<ul style="list-style-type: none"> • One vote per customer • One vote per share (based on ML or \$) • Hybrid model (e.g. customers with <X shares receive 1 vote, customers with between X and Y shares receive 2 votes, etc) • Voting limited only to those who both own a water allocation and own / lease a property in the Scheme area 	<ul style="list-style-type: none"> • Through varying the constitution of a company limited by shares, there is the capacity to adjust the voting rights of shareholders (i.e. customers) to suit the situation. • Those customers who have invested more in the Irrigation Scheme and hold a greater delivery share and water share are likely to expect a greater say in the business. • Regardless, it will be necessary to ensure measures are in place to protect all customers, including those with small holdings. • As water allocations and land ownership in the Scheme may become separated overtime (e.g. if water traders own the water but do not operate a farm in the Scheme) consideration should be given to restricting voting rights to those who hold both water and operate a farm in the Scheme (i.e. active customers). 	The voting rights for shareholders to be determined in consultation with prospective customers.
5.	Ownership of the Water Storage	<ul style="list-style-type: none"> • Owned by Sunwater (or other government entity) • Owned by LME • Owned by Sunwater/government, but operated by LME • Commercial provider 	<ul style="list-style-type: none"> • Government is likely to be the major funder of the Water Storage and will have a major say in ownership. • There will be dam safety considerations and regulatory responsibilities associated with the Water Storage. Government has demonstrated reluctance for such significant infrastructure, funded by Government, to be held by private operators (or LMEs) and there is no current precedent in Queensland for such a storage being owned privately. • Any benefits from LME ownership and/or operation would primarily relate to reduced costs and greater flexibility in service standards. • However, there may be limited benefit to customers when balanced against the risks associated with such infrastructure being owned by a small standalone entity which has no operating or insurance history and may have limited resources to call on where major capital or refurbishment works are required or in response to a catastrophic event. 	<p>Water Storage be owned by Sunwater or another government entity.</p> <p>Careful consideration be given to setting the boundaries between the Water Storage and the Irrigation Scheme, to ensure risk and responsibilities are appropriately allocated.</p> <p>Explore options for LME to take operational responsibility for any water supply activities that would otherwise sit with the Water Storage owner.</p>

No	Issue	Options/requirements	Considerations	Recommendation
			<ul style="list-style-type: none"> Government/Sunwater are likely to be supportive of the LME undertaking certain operational functions related to water supply (e.g. diversions to the Irrigation Scheme) but less likely to support the LME having responsibility for maintenance of the dam wall and flood management/dam safety matters. Existing LMEs have worked successfully with Sunwater to carry out services for Sunwater. For example, in Emerald, the LME performs all the vegetation and slashing works within areas owned by Sunwater. In Theodore, a Sunwater employee co-locates within the LME office and where that person requires support, the LME staff work with them under a service arrangement. This has resulted in significant savings. 	
6.	Ownership of the water allocation	<ul style="list-style-type: none"> Customers own the water allocation LME owns the water allocation and supplies water under an agreement 	<ul style="list-style-type: none"> Policy approach nationally has been for individual water users to hold the water allocation where possible. Customers holding the water allocation would allow for it to be used as security and would enable water trading. No clear benefits from LME owning the water allocation. A separate water allocation will be required to account for water lost during the distribution process (seepage, evaporation). There are benefits from the Irrigation Scheme owner holding this allocation. This approach would be consistent with existing irrigation schemes. 	<p>Water allocations to be owned directly by customers.</p> <p>Water allocation associated with any distribution loss to be held by the LME. LME to have the flexibility to trade any of its volume for years where not all required.</p>
7.	Contractual arrangements	<ul style="list-style-type: none"> Customers have separate contracts with the LME and the Water Storage owner 	<ul style="list-style-type: none"> The Water Act requires a contract between the owner of a water storage and its customers.³ Customers within the existing Qld LMEs have two contracts – one with the LME, one with Sunwater – and customers receive 	<p>Customers have a single contract with the LME, with the LME to contract the Water Storage owner on their behalf</p>

³ Water Act 2000 (Qld), section 147 requires a supply contract between the allocation holder and the resource operations licence holder.

No	Issue	Options/requirements	Considerations	Recommendation
		<ul style="list-style-type: none"> Customers have a single contract with the LME, and the LME has a contract with the Water Storage owner on the customers' behalf 	<p>two invoices. However, arrangements are in place between Sunwater and all the LMEs which provide for the LME to be the first point of contact for all customer queries.</p> <ul style="list-style-type: none"> It may still be possible to avoid a contract directly between customers and the Water Storage owner, such as by having the LME contract as their agent. Irrespective of the contractual arrangements, it may be possible to simplify water ordering, billing and other customer interactions with the Water Storage owner by giving the LME responsibility for engaging with the Water Storage owner on behalf of customers. 	<p>LME to be the single point of contact with customers and appropriate contractual arrangements between the LME and Sunwater in place for this to occur.</p>
8.	Price setting	<ul style="list-style-type: none"> Mechanism for setting prices for Irrigation Scheme Mechanism for setting prices for Water Storage 	<ul style="list-style-type: none"> Contractual arrangements will need to provide sufficient flexibility for LME to set prices to recover costs and ensure financial viability. As a customer-owned and not-for-profit entity, customers are more likely to have confidence in the entity having discretion in setting prices. Prices for the Water Storage likely to be set based on recommendations by the Queensland Competition Authority (QCA), as for other Sunwater-owned irrigations schemes. 	<p>LME have flexibility to set water prices for the Irrigation Scheme, based on a Board-approved pricing policy.</p> <p>Water Storage prices be set based on QCA recommendations.</p>

2. Introductory matters

2.1 Overview

Jacobs has been engaged to prepare a detailed business case (**business case**) for the development of:

- (a) a water storage in the Flinders River catchment on Saego station, 45km north-west of Hughenden, and
- (b) an irrigation scheme on the southern side of the Flinders River

collectively, the “project”.

The proponent is Hughenden Irrigation Project Corporation Pty Ltd (**HiPCo**). HiPCo is a privately held company established by a group of land holders from the Hughenden area. The current Board of HiPCo includes members from Hughenden and other independent members who have experience with water projects.

It is envisaged that the project will have the capacity to supply a mixture of high reliability water (primarily to higher-value horticultural crops), and medium reliability water for lower-value crops, such as cereal grains, hay, and fodder crops.

The majority of the land that will form the Irrigation Scheme is presently part of a station called “Dunluce”, which is currently held by a single owner. The owner has indicated they are willing to sell the land for the project, but commercial terms have not been agreed. Similarly, the owners of the proposed site for the Water Storage have indicated a willingness to sell the land for the project but no agreement is in place.

Investigations are also underway into the potential for development of a number of ‘lifestyle’ blocks in the vicinity of the Irrigation Scheme.

Funding to support the capital investment in the project is expected to be sourced from a combination of:

- (a) Customers, and
- (b) Government (State and Commonwealth).

The business case being prepared by Jacobs is considering the potential capital costs of the project and the funds which may be available from future customers upfront to secure water in the project.

It is likely that the majority of funding for construction of the Irrigation Scheme will come from customers. Construction of the Water Storage will likely require the majority of costs to be met by Government. (To date the Commonwealth has indicated support for an investment of approximately \$180 million. It is highly likely a substantially greater Government contribution will be required for the project to be financially viable.)

The proponent envisages the ultimate owner and operator of the Irrigation Scheme will be an entity owned by the customers of the Irrigation Scheme (i.e. a locally owned and managed entity (**LME**)). The ownership and operatorship of the Water Storage has not been determined. Due to the size of the Water Storage, dam safety considerations and insurance and potential liability issues, the current expectation is that the likely owner will be a Queensland Government entity (e.g. Sunwater).

2.2 Assumptions regarding the objectives of the project

The structural arrangements need to:

- (a) be supported by investing customers (and their financiers), and
- (b) meet any funding conditions set by Government(s).

We have assumed that Government (Federal or State) will not hold equity in the Irrigation Scheme owned by the LME, given the entity will primarily be funded by customers. However, given the majority of capital investment for the Water Storage is expected to come from Government, together with public interest considerations related to dam safety, it seems likely that Government will seek to own this asset. It is understood that the investment itself by Government is unlikely to (and will not be required to) achieve a return on the investment given the required upfront capital investment, the number of customers and the price which can be paid by those customers for water.

All assumptions based on the information available to us at 18 June 2021.

Given the above, we assume that the more specific objectives for the institutional arrangements will include:

- (a) Customers, through the LME, own the Irrigation Scheme infrastructure (**Irrigation Scheme LME**)
- (b) The Irrigation Scheme LME will be not-for-profit with a primary focus on supplying low-cost water to customers, but also recognising the importance and value of the scheme in supporting broader community outcomes
- (c) The rights to water held by individual customers and their ownership interest in the Irrigation Scheme LME will be (broadly) proportionate to their level of capital investment and reflective of the volume of water available to them and their share of the delivery capacity of the scheme
- (d) The water rights and the ownership right in the Irrigation Scheme LME can be used as security by customers to assist with obtaining any credit required to buy into the project
- (e) The water rights can be sold for value
- (f) There are measures in place to protect the interests of all customers regardless of the size of their ownership interest in the Irrigation Scheme LME
- (g) The governance arrangements reflect best practice and support long term stability, financial viability and transparency in the operation of the Irrigation Scheme
- (h) The structure minimises costs, having regard to the size and nature of the business
- (i) There are mechanisms to ensure sufficient funds are retained for ongoing asset maintenance and renewal, and
- (j) The institutional arrangements will protect the owners of the Irrigation Scheme LME from any personal liability as a result of their investment in the project.

These assumptions should be agreed and finalised by the proponent.

2.3 Overview of customer investment

We have assumed potential customers seeking to invest in the project will ultimately be required to make a financial investment to secure land, water, and water delivery rights in the project. Any investment could only occur following confirmation from the Commonwealth of sufficient funds to construct the Water Storage. We anticipate that these funds would be directed to the Queensland Government to facilitate the construction of the Water Storage.

Customer investment for shares in the Irrigation Scheme will be subject to the disclosure requirements in the Corporations Act. We anticipate this would involve the issue of a prospectus which complies with

the Corporations Act. The prospectus will need to address all aspects of the project of relevance to the potential investor/customer, including matters related to the issue of shares in the Irrigation Scheme LME, the ownership/transfer of the water allocation, the transfer of land, and key contractual arrangements related to water supply.

Customer investment in the project is likely to be structured as follows:

Components of project package	Entity receiving funds	Customer receives	Entity obligation in return for funds
Land Parcel (Land parcel is likely to be allocated with a minimum water volume for land type / crop suitability)	Land owner ⁴	Land within the Irrigation Scheme	Transfer land to customer
Irrigation Scheme (Delivery)	Irrigation Scheme LME	Shares in Irrigation Scheme LME Ongoing contractual right for water delivery within the Irrigation Scheme	LME required to construct, operate and maintain the Irrigation Scheme.
Water	Queensland Government	Water allocation (or contractual/licence right) Ongoing contractual right for supply of water from the Water Storage.	Government (or Government entity) required to build water storage to facilitate the availability of water. Government to grant water allocation.

2.4 Scope and limitations

This report sets out possible entity, institutional and governance arrangements and related strategic considerations for the project, including addressing issues related to infrastructure ownership and a proposed contracting model for the irrigation users.

This paper primarily focuses on the institutional arrangements related to the Irrigation Scheme, including arrangements between the owners of the Irrigation Scheme and the owners of the Water Storage. The paper broadly considers the issues associated with the ownership of the Water Storage and whether ownership / operator models may be available for the Water Storage other than a government owned entity (see Part 3).

This report considers:

- (a) ownership and operational options for the Water Storage
- (b) ownership, institutional and governance arrangements for the Irrigation Scheme
- (c) the water framework relevant to the project, including the options for 'ownership' of the water in the project, and
- (d) the possible contractual arrangements between the LME, customers and the Water Storage owner/operator.

This report provides a high-level overview of the overall structure of a local management entity for the project and based on the information and assumptions set out in sections 2.1 and 2.2. The report is not intended to be definitive or final legal advice, nor does it address accounting, financial, insurance or tax

⁴ Further consideration as to the structure of the land sale contracts will be required, we would anticipate that the proponent or the Government entity enter option agreements with the existing land owner. Options would be exercised on conclusion of the investment process, with the proponent / Government entity nominating the successful bidder as the final purchaser on the exercise of the option.

matters (relevant to either the proponent, customers or others associated with the project). As the project progresses specialist advice should be sought on these components.

As each stage of the project is progressed, specific legal, financial, insurance and taxation advice should be sought by the proponent. It is not intended to be, nor should be relied upon as an exhaustive list of matters associated with the structure, governance or corporate form.

As HiPCo has been incorporated we have not considered any of the governance or structural issues for HiPCo prior to the funding stage for this project.

We have been instructed by Jacobs to prepare this Report which is to be made available to the HiPCo. The Report has not been prepared with refinements or clarifications to specifically assist individual stakeholders.

3. Water Storage Ownership and Operation Considerations

3.1 Overview and dam safety issues

We understand that the Queensland Government has indicated that the water storage should be owned by a government entity. (At the time this paper was prepared a firm decision had not been made). In Queensland, major water storage facilities (dams) outside Southeast Queensland are owned and operated by Sunwater, a Queensland Government Owned Corporation (GOC).

The operation of a dam in Queensland is subject to specific regulatory requirements associated with 'referrable dams'⁵. In addition, events over the past decade, including the flood in Townsville in February 2019, the Brisbane Floods of 2011 (and the subsequent class action litigation) and the issues associated with Paradise Dam near Bundaberg have resulted in an increased focus on the risks and potential liability associated with the operation and maintenance of major dams. This is particularly the case if those dams are used as a flood mitigation tool (which we understand is not the case for this dam).

We expect the Queensland Government will be concerned to ensure:

- (a) The dam wall, is constructed to the highest standards (refer to Jacob's business case for further information on these)
- (b) Is appropriately maintained and operated to required regulated safety standards, and
- (c) During any flood event is managed in accordance with dam safety protocols.

In addition, a major consideration for a dam owner is the ability to meet any potential liability arising from the ownership and operation of the dam. This includes obtaining sufficient insurance to meet any potential liability arising from the operation, including a catastrophic event which results in the destruction of the dam, property, livestock, and life.

Meeting insurance costs on an ongoing basis may also be a major concern for Government noting insurance premiums are on an upward trend which commenced in 2015 ([Global Insurance Market Index - 2020 Q4 \(marsh.com\)](#)) and there is expected ongoing volatility given the potential impacts of climate change.

⁵ See Chapter 4, Water Supply (Safety and Reliability) Act 2008 (Qld)

3.2 Options

In relation to ownership and operation of the Water Storage, we see the following potential options:

No	Option	Detail	Construction Phase	Practical Completion	Barriers / Disadvantages	Advantages
1.	Water Storage owned and operated by Sunwater (or other Queensland Government GOC)	Water Storage owned and operated by Sunwater. Pricing recommended by QCA and determined by Minister.	Owned by GOC	Owned by GOC	<p>Significant distance from Brisbane and other Sunwater infrastructure.</p> <p>Lack of flexibility to meet local needs / changes.</p> <p>May result in higher design standards and hence higher construction costs due to low-risk appetite.</p> <p>Prices under Sunwater ownership has historically increased above CPI overtime.</p>	<p>Entity is best placed to manage risk associated with dam safety and insurance. Risk remains with Government.</p> <p>Potentially provides greater confidence for Government to invest.</p>
2.	Water Storage owned and operated by the LME <i>[An owner of a dam is the owner of land on which the dam is constructed or is to be constructed. The 'owner' includes the lessee / licensee</i>	An entity owned by customers would own the Water Storage (either the same entity as the Irrigation Scheme or a separate entity).	Owned by GOC, constructed by private contractor under appropriate delivery model.	Land transferred (or leased under the Land Act) to LME.	<p>Given significant financial investment by Government it is difficult to justify transfer of ownership for no financial return.</p> <p>LME responsible for all risk associated with dam including regulatory compliance under the</p>	<p>LME is able to manage all costs associated with the operation of the Water Storage together with the Irrigation Scheme.</p> <p>Small operation provides more nimble and flexible decision making to meet changing local needs.</p>

No	Option	Detail	Construction Phase	Practical Completion	Barriers / Disadvantages	Advantages
	<i>under the Land Act 1994 (i.e. a state lease)</i> ⁶				Water Supply Act. We don't see this on its own as insurmountable however, LME would need to hold appropriate insurance for Water Storage. ⁷ Government concern regarding solvency risk.	LME sets prices which may be done without QCA oversight and may be able to operate with lower overheads.
3.	Water Storage owned by Sunwater with long term operation and maintenance contract to LME	Under long term operation and maintenance contract: (a) LME to set and collect fees from customers sufficient to cover the full cost of operation and maintenance. (b) No fee paid by Sunwater to LME. (c) LME responsible for compliance with regulatory requirements (noting that owner remains responsible for referable dam requirements under the Water Supply Act).	Owned by GOC, constructed by private contractor under appropriate delivery model.	Owned by GOC; long term operation and maintenance contract with LME commences.	LME will have limited ability to control Sunwater costs associated with the contract management and the dam safety component (including costs associated with maintenance of the dam wall) that cannot be devolved (contract will need to build in appropriate audit / information and dispute mechanisms). Sunwater contract practice would be to require full indemnities from LME and LME likely to be required to hold full insurance (see	Enables the LME to manage the on-ground operations costs associated with the Water Storage and Irrigation Scheme locally and under the same system. Flexibility with respect to employment (i.e. not bound by Sunwater Enterprise Agreement) and procurement (i.e. no bound by Sunwater corporate policies). LME sets prices which may be done without QCA oversight.

⁶ See definition of 'owner' in Schedule 3, Water Supply Act

⁷ We recommend insurance costs and the ability to obtain insurance for the Water Storage is sought as part of the DBC. Noting for example, Sunwater is experiencing difficulties with respect to insurance associated with Paradise Dam see page 85 of [Sunwater Annual Report 30 June 2020](#) which provides: "Sunwater's insurers have declined to provide insurance policy coverage for the period 1 July 2020 to 30 June 2021 in respect of some elements of Paradise Dam in light of the structural issues currently being addressed at that site. Specifically, Sunwater has been unable to obtain insurance policies relating to property damage to the dam and associated Sunwater assets, and for Directors and Officers Liability coverage for claims relating to Paradise Dam."

No	Option	Detail	Construction Phase	Practical Completion	Barriers / Disadvantages	Advantages
		(d) LME required to pay Sunwater a fee to cover costs associated with management of contract, dam safety obligations which cannot be devolved to the LME, and insurance costs allocated to the Water Storage.			comments about insurance). Sunwater/Government concern regarding solvency risk.	
4.	Owned by a special purpose company owned by Government	Similar to option 1 above	As above	As above	SPV would need to be established, board engaged and likely would use Sunwater or Seqwater to support the operation. Likely to result in higher overhead costs.	As above.
5.	Private Third-Party Owner	Third Party acquires dam on understanding it can obtain a return on investment.			Water prices likely to be higher prices to achieve a profit for private owner. Government concerns with making a major investment in an asset that will be owned by a private, for-profit entity.	Commercial provider may operate under a lower cost-base than a government owned entity.

3.3 Preferred approach

Based on the above analysis, we consider that the only viable options are option 1 (Sunwater ownership) or option 3 (Sunwater option with long-term operation by LME). We also note:

- Sunwater (or other government entity) would be best placed to manage risks associated with the Water Storage (primarily related to flood risk/dam failure)
- An LME would be best placed to manage costs associated with water delivery, while an LME may be less well suited to activities related to major dam operation and maintenance where more sophisticated management systems and engineering can be required, and
- An LME would likely have the maximum drivers to ensure security of water supply from the Water Storage.

On this basis, the benefits of option 3 (LME operation) will be constrained by the extent to which there are operations and maintenance activities that can reasonably be undertaken by the LME, and not the Water Storage owner. This is likely to be limited to activities related to water diversion/supply. Any activities related to maintaining the integrity of the dam wall and major releases will likely need to be undertaken by Sunwater, or in any case to the same standard, in which case any benefits of LME involvement are likely to be minimal and outweighed by the additional risks.

Having regard to the above options and considerations, we are of the view that the preferred model is as follows:

- The Water Storage to be owned by Sunwater (or another Queensland Government entity)
- Dam safety obligations, maintenance of the dam wall, and flood management be the responsibility of the Water Storage owner
- Consideration be given to the LME taking responsibility for the remaining operational activities related to the Water Storage, including potentially water accounting and the diversion of water to the Irrigation Scheme under a long-term operating agreement with the Water Storage owner,⁸ and
- The boundaries between the Water Storage and the Irrigation Scheme be defined such that the water delivery infrastructure and related responsibility sits within the Irrigation Scheme to that extent feasible.

In setting the boundaries between the Water Storage and the Irrigation Scheme, it is worth noting that under the LME process, the Queensland Government has supported the transfer of major pump stations, channels, pipelines, drainage networks, the distribution loss water allocation, and balancing storages to the relevant LME. In no cases have major water storages or weirs been transferred to an LME. (For some of the irrigation schemes that remain with Sunwater, it was contemplated that one or more of the weirs within the scheme may have transferred, where they were integral to the distribution network, but a final decision was not made by Government).

It is also worth noting that for the current Queensland LME's there are services and tasks performed by the LMEs for Sunwater which has led to not only cost saving but other efficiencies and the ability to be more responsive to the local requirements. This includes:

- (a) First contact point for customers to the LME's (we see significant potential to improve this in a greenfield scheme where customer relationship management systems (CRMs) are set up at commencement rather than in the existing LME's where those systems sit in Sunwater),

⁸ While it may be feasible for these tasks to be undertaken by the LME, we note that (i) the actual release of water from Water Storages is not a task carried out by any of the existing LMEs, and (ii) water accounting, particularly where capacity sharing arrangements are in place (which is under consideration for the project) requires significant expert resourcing. The St George water supply scheme currently operates under capacity sharing arrangements which are managed by Sunwater. The St George LME has indicated it would not have the capability to undertake the water accounting for the water supply scheme.

- (b) LME employees carrying out vegetation management within Sunwater owned areas (this has occurred in Emerald where the LME performs vegetation management for Sunwater over a large drain – significant cost savings have resulted from this arrangement), and
- (c) The co-location of Sunwater employee in Theodore and arrangements for the LME employees to support that single employee where required, particularly where higher risk activities require two people.

4. Locally managed irrigation schemes in Australia

To assist with considering the issues for a locally managed irrigation scheme it is worth reviewing current structures in Australia. The Schedule includes a table setting out details for existing local management entities, including the various corporate forms and the governance structures.

A brief overview is provided below.

4.1 Queensland

In Queensland, there are five locally managed irrigation schemes (St George, Theodore, Emerald, Pioneer Valley and Eton). Each of these schemes were previously owned by Sunwater and all but Pioneer Valley have recently been transferred to not for profit, customer owned entities (i.e. an LME).

Under each of these schemes, customers hold a water allocation and are parties to the following contracts:

- (a) Distribution contract with the LME for the distribution of their water allocation from the bulk water source to their property (i.e. a contractual delivery right). Customers pay the LME:
 - (i) a fixed fee annually based on the nominal volume of their water allocation, and
 - (ii) a consumption fee based on their actual usage recorded at the meter⁹, and
- (b) Supply contract with Sunwater for the supply of their allocation from the bulk water source owned by Sunwater. Under this contract, customers pay Sunwater a fixed fee and a consumption fee.

The five LME's all have different corporate structures as follows:

- (a) Eton – Non trading cooperative without shares – regulated under the Queensland Cooperatives Act
- (b) St George – Company Limited by Guarantee
- (c) Emerald – A large company limited by shares
- (d) Theodore – A small proprietary company limited by shares
- (e) Pioneer Valley – A dual cooperative – meaning two cooperatives have been established one to operate the scheme and the second to own the infrastructure.

When considering the existing LMEs in Queensland, they are distinguished from this project:

- (a) each scheme was funded, built and owned by Government before they were transferred as existing operations to the LME,
- (b) customers owned land within the irrigation area at the time of the transfer to an LME, and
- (c) customers had the option to become members of the LME at the time of the transfer so not all customers are members of the LME (we assume that all initial investors will require shares).

⁹ Currently in Queensland, there is no differentiation given in the contracting or pricing as to the maximum share / capacity a customer has in the Scheme.

(Note, for the recent transfers Government required that a significant percentage of support by water volume in each Scheme both supported the transfer (70% threshold) and elected to become members (50% threshold in St George and Theodore and 70% in Emerald and Eton).

4.2 Other States

The move from Government ownership to local management for irrigation schemes has been occurring in Australia since the mid-1990s. In all cases, the assets were originally constructed and operated by a Government entity and so on the move to local management the business and assets were already in operation.

Key characteristics of these entities (as for the Queensland LMEs) are:

- Not for profit – no dividends are paid back to owners
- Members must be customers
- Boards of governance are made up of both customers and independent directors
- Members either have:
 - 1 vote, or
 - their voting power reflects the volume of water they hold in the particular scheme.

The entity structure adopted generally falls into one of two categories:

- (a) Corporations Act companies limited by shares. Under this model, irrigators/customers hold shares in the company, typically in proportion to the volume of water rights allocated to them. Due to the number of customers/shareholders (greater than 50) these are generally public companies.
- (b) Dual-structure co-operatives. Under this model, two cooperative entities are established:
 - (i) The asset entity which owns the infrastructure, and
 - (ii) An operating entity which holds the customer contracts.

Members (i.e. customers) are members of both entities. The use of this structure allows the assets (and any sinking fund) to be quarantined from an insolvency event in the operating company. This structure also sets up some unique tax consequences which treats member levies to the asset entity as non-assessable income for tax purposes – however the asset entity is then not able to claim deductions for depreciation. The corporate form relies upon the Cooperative Legislation in each State rather than the Commonwealth Corporations Act (although Queensland has recently adopted the Cooperatives National Law so the law is the same as other States operating under that model but the regulator remains a State regulator).

4.3 Potential cost savings of local management.

Currently, in Queensland, irrigation customers sourcing water from the water storages owned by Sunwater:

- (a) Own (hold) a water allocation in the relevant area
- (b) Hold a supply contract with Sunwater for the release of their water allocation from the water storage, and
- (c) A distribution contract with the owner of the irrigation scheme (either an LMA or Sunwater) for the delivery of that water from the water storage.

Under the supply contracts, customers pay Sunwater a fixed charge per annum based on the nominal volume of their water allocation (Part A) and a consumption charge for the water taken (Part B). These prices are determined by the Queensland Treasurer following irrigation pricing recommendations made by the Queensland Competition Authority (**QCA**). The QCA has recently released its [recommendations](#) for irrigation prices for 2020-2024.

As a general comment:

- (a) irrigation schemes under Sunwater management run at a loss, that is the prices charged do not reflect the costs Sunwater allocates to the operating, maintenance and running the schemes and the associate water storage infrastructure
- (b) the Sunwater costs generally rise year on year and historically have increased above inflation and above the projected costs determined by the QCA, and
- (c) prices are informed by the Sunwater costs and increase year on year.

Each of the LMEs that transitioned from Sunwater since 1 July 2018 (starting with St George) have indicated that the costs to operate the irrigation scheme within the local management structure have resulted in significant cost saving for the schemes which have or are resulting in prices being set below prices that would have applied if Sunwater continued to operate those schemes.

Some of the advantages we have observed have been the ability of the LME to:

- (a) trade unused volumes of their distribution loss
- (b) carry out capital works:
 - (i) at lower cost than similar work was carried out by Sunwater, and
 - (ii) more work than that Sunwater had previous performed in similar periods and at time more appropriate to the local operation and needs of the scheme
- (c) set up scheme specific trading platforms to support the temporary trading for the local area
- (d) sell or decommission assets no longer required by the Scheme
- (e) use local suppliers, where possible (e.g. accountants and auditors).

These advantages, are starting to be reflected in the Queensland LME prices since transition which can be summarised as:

	2017/2018	2018/2019	2019/2020	2020/21	2021/2022
St George	Sunwater	Transferred 1 July 2018	Mallawa	Mallawa	Mallawa
Fixed (Part C) per ML	\$35.41	\$35.41	\$35.41	\$29	\$29
Consumption (Part D) per ML	\$5.75	\$5.75	\$5.75	\$4.70	\$4.70
Drainage	\$27.15 (per hec)	\$27.15 per ML	\$27.15 per ML	\$11.13 per ML	\$11.13 per ML
Theodore	Sunwater	Transferred 1 October 2018	Theodore	Theodore	Theodore
Fixed (Part C) per ML	\$48.41	\$55.90	\$55.90	\$55.90	\$55.90
Consumption (Part D) per ML	\$32.17	\$32.97	\$32.97	\$32.97	\$32.97
Drainage	\$28.10 per hectare				

	2017/2018	2018/2019	2019/2020	2020/21	2021/2022
Emerald	Sunwater	Sunwater	Transferred 1 July 2019	FIN	FIN
Fixed (Part C) (MP) per ML	\$22.73	\$26.60	\$25.00	\$25.00	\$20.00
Consumption (Part D) (MP) per ML	\$6.55	\$6.71	\$6.71	\$6.71	\$6.71
Drainage		\$28.10 / \$6.85	\$28.10 / \$6.85	\$28.10 / \$6.85	\$22.50 / \$5.50
Eton	Sunwater	Sunwater	Transferred 1 April 2020	Eton	Eton
Fixed (Part C) per ML		\$35.20	\$38.40	\$40.55	\$42.83
Consumption (Part D) per ML		\$32.81	\$33.63	\$10.09	\$14.33

5. Irrigation Scheme Corporate Form

5.1 Overview

There are four corporate structures for the Irrigation Scheme which could be considered:

- (a) a company limited by shares
- (b) a company limited by guarantee
- (c) a cooperative, or
- (d) a dual cooperative.

Other business structures, for example a unit trust or partnership would not be suitable, and we have not considered them as they would not support the objectives set out in paragraph 2.2.

5.2 Preferred corporate form

The dominant consideration in selecting the corporate form for the Irrigation Scheme entity is its capacity to support raising funds for the capital cost of the Irrigation Scheme. Given this consideration, in our view a company limited by shares is the most suitable. This structure would enable customers to:

- (a) Own an equity interest in the Irrigation Scheme entity proportionate to their investment
- (b) Sell their shares in the Irrigation Scheme, and
- (c) Use their shares as security.

The structure is also commonly understood, governed by the Corporations Act, widely used and allows for significant flexibility in the governance documents.

If there are more than 50 customers (and therefore shareholders) the entity would be a large proprietary company limited by shares. A large company is subject to additional regulatory oversight under the Corporations Act, including for example the takeover provisions.

A company limited by shares is governed by a constitution and the Corporations Act. The constitution can establish the entity as a not-for-profit business, by specifically preventing the return of profit (e.g. through dividends) to shareholders under the constitution and requiring all funds received by the LME to be used to operate and maintain the Irrigation Scheme.

The constitution will also address:

- (a) The board make up
- (b) The qualification of directors
- (c) The qualification requirements to become a shareholder, and
- (d) Voting thresholds for key business decisions.

A company limited by shares may establish a subsidiary company to hold the assets (or the customer contracts) should that be considered necessary to quarantine the Irrigation Scheme assets from any liability related to the customer contracts or more generally the operation of the scheme.

5.3 Vehicle HiPCo or a new entity

As detailed considerations with respect to the investment model are considered, either HiPCo or a new company limited by shares could be used as the LME Irrigation Scheme entity. There may be benefits is using HiPCo as it already holds a significant component of the 'project' intellectual property and confidential information.

5.4 Dual cooperative model

Given that a number of irrigation schemes have adopted the dual cooperative model it is worth noting that this model:

- (a) has not been used for a new project where upfront capital investment is required,
- (b) is regulated in Queensland by the Office of Fair Trading in Queensland under the Queensland Cooperative Act rather than the Australian Securities and Investment Commission (ASIC) under the Corporation Act. The rules and legislation applying to cooperatives are generally less flexible and more prescriptive than requirements in the Corporations Act. In addition, given that there will be a large upfront capital cost in constructing the project, it may be that the depreciation of those assets may be more beneficial than the benefit derived from collecting levies which are not treated as assessable income (further tax analysis would be required to assess any tax benefits of this model for a greenfield water project), and
- (c) requires two Boards (one for each entity) and a different set of cooperative rules for each entity which could create an additional administrative burden.

We also note that the members of the Coleambally Irrigation Scheme, which has operated as a dual-cooperative, recently resolved to wind up the mutual and revert to a single entity structure.

6. Governance considerations – Irrigation Scheme LME

In developing the governance structure for the Irrigation Scheme LME, key considerations include:

- (a) Facilitating appropriate and transparent governance and accountability
- (b) Providing for a mix of skill representation on the Board and include both member directors and independent directors
- (c) The voting power of shareholders
- (d) Mechanisms to ensure funds are retained for renewals and upgrades, and
- (e) Management of conflict of interest particularly in relation to price setting.

Set out below are key considerations for the constitution / rules of the Irrigation Scheme LME:

Issue	Proposal / Options
<p>Objects</p>	<p>To include constructing the Irrigation Scheme, and operating and maintaining the Irrigation Scheme for the customers.</p>
<p>Profit / Not for Profit</p>	<p>Not for Profit.</p> <p>No return to shareholders and all funds to be used in the operation and maintenance of the Scheme (and to paydown any funding loans).</p> <p>(Note, should private investors be sought a process for a return to investors would need to be built into the constitution.)</p>
<p>Shareholder</p> <p>The constitution will need to determine (i) who can be a shareholder of the entity and (ii) the rights (including voting rights) of shareholders.</p> <p>The shareholders of a corporate entity generally have the power to:</p> <ul style="list-style-type: none"> - Appoint the directors by a simple majority - Change the constitution by a special resolution of 75% - Wind up the entity by a special resolution of 75%. <p>In privately held companies it is common for the shareholders to agree additional restrictions related to decision making and who can be appointed as a director.</p> <p>Consideration also to be given to whether eligibility to hold shares and/or vote should be limited to active irrigators within the scheme, to prevent water speculators from influencing business decisions.</p>	<p>Shareholding to be limited to those who hold a water allocation in the Scheme.</p> <p>Shares transferable (i.e. could be sold for value) only where transferred with water rights and delivery rights the project, and have taken on the associated contractual obligations to pay annual fees etc.)</p> <p>LME to consider whether the shares and governance arrangements are designed to achieve:</p> <ul style="list-style-type: none"> - a weighted vote reflective of their equity interest and water rights (i.e. one vote per ML) - one vote per shareholder, or - something in between. <p>It is possible to establish different classes of shares (including voting and non-voting shares) to strike a balance between the one vote per member and one vote per ML.</p> <p>Limit eligibility to those that own/manage land within the Irrigation Scheme.</p>
<p>Board – Make Up</p> <p>The constitution should determine the total number of directors, as well as any requirements on the number of Member Directors and Independent Directors.</p> <p>Member Directors are directors who are themselves a shareholder or are nominated by a shareholder.</p> <p>Independent Directors are appointed solely based on their skills/expertise and usually must not be a shareholder.</p> <p>Existing LMEs typically have between 3 and 6 directors, with at least 2 Independent Directors.</p>	<p>We recommend the Board should have 5 Board members, with at least 2 directors that are Independent Directors.</p> <p>Given the price setting power the Board will have it is important that the independent directors have the skills and experience to lead this process. Whilst Member Directors will necessarily be part of the decision, if there is any dispute in relation to price setting it is necessary to ensure Independent Directors are able to navigate these issues with the Member Directors.</p>
<p>Board – Term</p>	<p>Post funding, the rules need to provide for stability and consistency but ensure that the Board does not become entrenched with limited opportunity for new directors to be appointed.</p>

Issue	Proposal / Options
	<p>Changes to the Board should occur by rotation to maintain stability and ensure corporate memory is retained.</p> <p>None of the new Queensland LME's have limited the reappointment of directors. However, some of the irrigation entities in other States have specified a limit on the number of re-appointments (e.g. only one reappointment and therefore limiting the maximum term to 6 years).</p> <p>It is also possible to impose time limits that only apply to the Independent Directors or only to the Member Directors if preferred.</p>
<p>Board decision making</p> <p>The standard position is that Board decisions are made by simple majority.</p>	<p>This may be an issue to consider further and particularly whether for key decisions where the Member Directors will have a personal financial interest (e.g. price setting) whether such decisions require support of an Independent Director.</p>
<p>Price setting</p> <p>Water prices and other charges will likely be set by the Board in accordance with the requirements of the distribution contract. Prices should be set to (i) recover operating and maintenance costs and (ii) build sufficient reserves to meet long-term capital renewal costs.</p> <p>The principles required to inform the setting of prices can be described in the LME constitution. Such an approach would provide greater certainty to customers but would limit the flexibility of the Board.</p> <p>Alternatively, the principles can be defined in a pricing policy to be prepared by the Board. This option is considered preferable given the nature of the entity, as a not-for-profit member-based entity.</p>	<p>That the constitution requires the Board to prepare a pricing policy, setting out the approach to determining water prices and other charges to be paid by customers.</p> <p>Prices be determined in accordance with the pricing policy by a sub-committee of the Board made up of the Independent Directors, in accordance with the pricing policy set by the Board.</p>
<p>Protection of minority shareholders</p> <p>Depending on the final make up of customer in the scheme and the water rights held by those customers, there may be a small number of customers/ shareholders able to have effective control of the LME. It is important that other customers/shareholders have sufficient confidence that their interests will be adequately protected.</p>	<p>Practical control of a company may be achieved at shareholdings significantly less than 50% as in practice not all shareholders attend and vote on resolutions. Shareholders primary power is to appoint directors to the Board. Therefore, depending on circumstances, control could potentially be achieved at between 25%-35% of the shareholding.</p> <p>We recommend that the constitution includes mechanisms to prevent a single shareholder or closed related group of shareholders from having effective control of the Irrigation Scheme LME. This can be achieved through the use of one or more of the following mechanisms:</p> <ul style="list-style-type: none"> • including a cap on voting power for example, no single shareholder or related group of shareholders can vote on more than [5/10/20%] of shares in the LME • reserving a role on the Board for smaller shareholders (none of the current Queensland LMEs adopted this mechanism • requiring the establishment of an advisory committee for smaller shareholders. <p>We consider the actual mechanism will need to be considered as part of the consultation process with the potential customers for the scheme.</p>

Issue	Proposal / Options
	<p>Some mechanisms adopted in other schemes to protect minority interests include placing a cap on voting power (for example Emerald has a 25% cap and Murray Irrigation has a 5% cap).</p> <p>If the takeover provisions of the Corporations Act apply to the entity (i.e. if it has more than 50 shareholders), then changes which result in a shareholder increasing their interest to above 20% will trigger those provisions (specific advice on the impact of these provisions and how to manage them will be required by the LME).</p> <p>In establishing protections, it is important to ensure that the entity is not unduly restrained from making business decisions by a small group of minority owners.</p>
Quorum (Board and Shareholder Meetings)	<p>Needs to be a practical number reflecting realistic attendance at AGMs.</p> <p>Attendance via electronic means at AGMs should also be considered.</p>
Annual General Meeting	<p>The Corporations Act requires a public company limited by shares to hold an AGM within 4 months of the end of the company's financial year.</p> <p>Attendance via electronic means should also be considered.</p>

7. Water framework

7.1 Water for the project

Water resource management in Queensland is regulated under the *Water Act 2000* (Qld) (**Water Act**) and the *Water Regulation 2016* (Qld) (**Water Regulation**) (collectively, **Water Legislation**). The Water Act establishes a system for sustainable planning, allocation and use of water. Under the Water Legislation a process for creating water planning instruments has been established.

The existing instrument relevant to the project area is the [Water Plan \(Gulf\) 2007](#) (Water Plan). The area is within the Flinders River Catchment. The Plan is due to expire on 1 November 2027.

Under the Water Plan in the Flinders River catchment area there is:

- (a) 8,500 ML of indigenous unallocated water¹⁰
- (b) 17,850 ML state purpose strategic unallocated water¹¹
- (c) 239,650 ML general unallocated water¹².

The project will apply for part of the unallocated water set out above. This will need to be granted in accordance with processes required under the Water Plan (Gulf) 2007 and Water Regulation. This process is considered by Jacobs elsewhere in the business case and we have assumed this granting can occur either through the regulatory framework or via an amendment to the Plan. We understand consideration is also being given to purchasing some of the existing water allocations under the plan.

¹⁰ Schedule 6A of the Water Plan (Gulf) 2007

¹¹ Schedule 7, Part 2 of the Water Plan (Gulf) 2007

¹² Schedule 8 of the Water Plan (Gulf) 2007

7.2 Water allocations and water licences under the Water Act

In Queensland, under the Water Act all rights to water vest in the State and in order for a person to take water they must be authorised via a mechanism in the Water Act or via some other legislation or statutory instrument.¹³ For individuals, under the Water Act these authorisations are primarily via a water allocation, a water licence or a general authorisation.¹⁴ The primary difference between a water licence and a water allocation is its relationship with land.

Water allocations are registered on the Water Register. The water allocations do not attach to specific parcels of land and can be bought and sold independently of the land on which they may be used. They are subject to conditions regarding the locations at which they can be taken, and these locations are referenced in the relevant water plans. All water rights in irrigation schemes in Queensland are water allocations.

Water licences on the other hand are limited licences and are generally linked to the land on which they can be used. They cannot be sold separately to the land. As they cannot be traded independently of the land, we do not believe they are appropriate for the project.

7.3 Water allocations held by customer or LME

In Queensland, generally, customers own a water allocation and their ownership is registered on the Water Register. It is possible for the LME to hold the water allocation and then give customers a 'contractual right' to a portion of the LME's water allocation.

An example where this has occurred previously is in St George, unsupplemented water allocations were owned by Sunwater for the benefit of customers. However, these allocations have since been 'transformed', that is registered separately and to the actual beneficiaries rather than Sunwater. This was done as part of a requirement under the Commonwealth Water reforms.

It is our view, the preferred approach is that customers (and not the LME) hold the water allocations, on the basis that:

- (a) customers (and their financiers) will require ownership of a water allocation (rather than a contractual right) as these can be used as collateral and generally will provide greater security to the customer
- (b) it would provide greatest flexibility for temporary trading of water
- (c) such an approach would be consistent with past practice of the State and Commonwealth regarding ownership of water allocations, and
- (d) there are not significant benefits from the entity holding the allocation.

7.4 Distribution operations licence and resource operations licence

The Water Act provides for the following licences associated with the operation of water infrastructure:

- (a) Distribution Operations Licence, and
- (b) Resource Operations Licence.

Under the Water Act, a resource operations licence (ROL) authorises its holder to interfere with the flow of water to construct or operate water infrastructure or to take water to distribute the water under water allocations¹⁵. The ROL must be held by the owner (or a parent company or subsidiary of the owner) of the Water Storage.

As it is likely that the Irrigation Scheme will be owned by a different entity to the Water Storage holder, the Irrigation Scheme LME will be required to hold a distribution operation licence (DOL) under the

¹³ Sections 26 and 27 of the Water Act.

¹⁴ See section 93 for the General Authorisations.

¹⁵ Section 176 of the Water Act

Water Act. A distribution operations licence authorises its holder to take water or interfere with the flow of water to distribute water under water allocations.

7.5 Distribution loss water allocation

Operation of the Irrigation Scheme will inevitably involve system 'losses', where water is 'lost' prior to delivery to the customer, for example due to evaporation or seepage. Typically, a separate water allocation is granted to allow for such losses. This distribution loss allocation could be held:

- (a) By the Irrigation Scheme owner (i.e. the LME), or
- (b) By individual customers, proportionate to their primary water allocation.

Across all Queensland LMEs, the distribution loss allocation is held by the LME. This has provided maximum security and flexibility for the LMEs in operating the schemes. It has also provided the opportunity for the LMEs to release surplus distribution water allocation on the temporary market (either at no cost or to generate an income).

On this basis, we recommend that the distribution loss allocation be held by the LME and that the allocation (and the Water Plan) permits the LME the flexibility to trade that water, where appropriate for the operation of the Scheme.

8. Customer Contracts water supply and delivery

8.1 Contract structure

As part of the initial investment package, customers will be required to enter long term contract(s) for the supply and distribution of the water from the Water Storage and through the Irrigation Scheme. The contract structure will ultimately depend on: (i) the final relationship between the Irrigation Scheme LME and the Water Storage owner; and (ii) the final decision with respect to whether customers hold individual water allocations or whether the water allocation is held by the LME.

Secure, enforceable contract(s) are critically important to secure the long-term financial viability for the infrastructure and the scheme.

The two options with respect to contracts are:

- (a) Customer has two contracts:
 - (i) With the Irrigation Scheme for the **delivery** of water from the Water Storage to the customer, and
 - (ii) With the Water Storage owner for the **supply** of water from the Water Storage, or
- (b) Customer has a contract for both the supply and delivery with the LME and the LME has a contract with the Water Storage owner.

The Water Act requires that where an allocation is managed under a resource operations licence (which will apply to the Water Storage), that there must be a supply contract between the allocation holder (i.e. the customer) and the resource operations licence holder (i.e. the owner of the Water Storage).¹⁶

While this suggests that separate contracts will be required, it may still be possible to operate under a single customer contract model (or to the customer the appearance of a single contract). This would require the LME to act as agent on behalf of its customers/members in entering a single contract with the Water Storage owner.

Historical arrangements have meant that to date all Queensland LMEs operate under a model of two customer contracts. However, a greenfield site offers the opportunity for a single customer contract model which has the potential to simplify administration for all parties, and potentially reduce costs.

¹⁶ Section 47(4) of the Water Act 2000

Should, a two-contract model be required due to the regulatory restraints or the ability to negotiate terms between Sunwater and the LME we would anticipate that once established the contracts for the Scheme would be in a standard form, available on the LME websites. On the transfers of any water allocations (and if separately accounted for the delivery right) acceptance of these terms would be conditional on the approval by the ROL holder (Sunwater to the transfer). We would expect the LME to be the customer contact point for all these matters, regardless of whether there was a single or dual contract with the customer.

8.2 Contract content

Importantly, the contract(s) should be standardised for the Scheme so that all customers are on the same terms and conditions and published on the Scheme website (as is currently the case for the Queensland LMEs).

Key matters to cover in the contract(s) include:

- (a) The contract must be ongoing and fix to the water right and have a link to the shareholding. There should be no ability for a customer to terminate the contract, and on any transfer of the water right within the Scheme the new owner of that water would be bound by the standard contract.
- (b) The contract should define the right of the customer to a share of the delivery capacity of the Irrigation Scheme, i.e. the delivery right.
- (c) Provide for price setting including the basis on which the Irrigation Scheme LME and the Water Storage entity can set prices.
- (d) A mechanism to change contract terms should circumstances require.
- (e) The ability to require security from customers should that be deemed necessary by the entity.
- (f) The ability to buy or sell water from or to other water allocation holders, as well as to buy or sell additional delivery capacity.
- (g) A mechanism to set rules for the operation of the scheme to provide for water ordering and delivery (noting that other LMEs have identified that further potential operational savings can be achieved in irrigation schemes by providing for optimal delivery processes).
- (h) Default mechanisms, including an obligation to pay an exit fee (termination fee) should water be taken out of the scheme permanently (whether this can occur will depend on the final regulatory arrangements).
- (i) An ability to seasonally assign part or all of their water right within a water year (this may enable customer to bring in water from outside the Scheme).

9. Pricing

There are two components to pricing:

- (a) The mechanisms for the Irrigation Scheme LME to set prices, and
- (b) The mechanisms for the Water Storage owner to set prices.

9.2 Price setting – Irrigation Scheme

For the Irrigation Scheme, the contract would provide for the price setting mechanism and the LME Board would set the prices. We would anticipate the contract including the following:

- (a) whether the annual charges (fixed and variable) are locked in for an extended period and for how long (e.g. with only CPI adjustments) (noting Queensland LME's can set prices annually on the giving of 6 months notice),

- (b) any changes to the charges including the introduction of new charges.

To the extent that the Irrigation Scheme entity is wholly owned by customers, and all customers are shareholders, this may provide comfort that prices will be set to reflect underlying costs, and that it would be reasonable to allow flexibility for the entity to adjust prices unilaterally provided sufficient notice is provided to customers. (Note further discussion on the price setting mechanism in section 6).

Under the Queensland local management process, the standard contract allows the LME to adjust prices annually provided the entity:

- (a) acts reasonably
- (b) has regard to the pricing principles which would be taken into account under any statutory regime for prices oversight from time to time applying in Queensland, and
- (c) gives customer's six-month's notice of a price change.

There is the potential that once operating, that the Irrigation Scheme could be declared a monopoly business and subject to pricing regulation by the QCA. However, current Government policy on local management is not to subject the LMEs to pricing regulation and therefore at this stage it seems unlikely that prices would be regulated by the QCA unless at a future time there was discontent on the part of customers.

9.3 Price setting – Water Storage

For the Water Storage, the pricing mechanism, depends significantly on ownership / operatorship discussed at section 3. For each option:

Option	Who sets prices	Comments
Option 1 (Sunwater)	Prices recommended by the QCA and determined by Minister.	This is the same process currently applied to set rural irrigation prices throughout Queensland. Prices are set every 5 years following a price review process conducted by the QCA.
Option 2 (LME)	LME sets prices.	LMEs in Queensland currently set their own prices. For the Water Storage, Government will be concerned to ensure that LMEs maintain and retain sufficient cash reserves to cover maintenance and major upgrades and renewals. We would anticipate if this option applied, further consideration would be required to provide a mechanism to require the establishment of a renewal fund and some further regulatory oversight.
Option 3 (LME Operator)	LME sets prices Sunwater passes its cost through on a cost recovery basis.	Under this mechanism the LME would set prices to cover all costs including major upgrades and renewals and to cover the Sunwater costs charged to the LME for its contract management role. We would anticipate that under this model, Sunwater would require the establishment of a renewal fund by the LME.

Option	Who sets prices	Comments
		The contract would also need to provide a mechanism for the LME to have the Sunwater costs reviewed/audited by a third-party expert.
Option 4 (GOC / SPV)	Same as option 3	Same as option 3
Option 5 (Private owner)	Private owner	For reasons set out elsewhere we do not see that this will be an option. In addition to concerns regarding renewals, customers will need a mechanism to ensure prices are reasonable given that the asset is a monopoly business.

Based on the recommendations in section 3.3 that the Water Storage be owned by Sunwater, with consideration to some limited operational role for the LME with respect to water delivery functions, we assume that bulk water prices related to the Water Storage will be determined via the existing QCA process (i.e. option 1 above).

10. Process for raising funds from customers

10.1 Requirement for disclosure document

The institutional arrangements for the project will likely require future customers to agree to commit funds to the project in return for equity (shares) in the LME and a right to receive water from the project. The LME will use these funds to finance the project.

Under the Corporations Act, there are specific disclosure requirements which must be followed by a Company when it issues securities (shares).¹⁷

In particular, unless a specific exemption applies a prospectus or information statement (disclosure document) must be prepared and lodged with ASIC. Where the disclosure document provisions apply there will be prescribed content required by the regulatory regime. The intent of these provisions is to ensure that investors can make informed decisions about whether to accept the offer to invest.

The process of issuing a disclosure document is significant and will require specialised legal and financial advice. The time and cost of this process should be included in any feasibility process. We estimate that between \$500,000 and \$1 million would be required for the process for preparing the prospectus and verifying the legal, financial modelling and engineering aspects of the project. At least 6-12 months should be allowed for this process¹⁸.

The disclosure process does also expose directors of the company to potential civil liability under the Corporations Act including for example in the event of misleading and deceptive conduct. To limit these risks, when developing a disclosure document, a careful due diligence process should be established to ensure that all statements of fact, opinion or belief can be justified and verified. The due diligence process generally would include the establishment of a due diligence committee made up of key legal and accounting advisors and board representatives. All statements of fact, opinion and assumption will need to be carefully checked and verified through this process.

(Examples of the documents produced by the LMEs can be provided on request. The LMEs were not required to comply with the prospectus provisions in the Corporations Act, however, a similar approach was adopted as best practice).

¹⁷ Section 708 of the Corporations Act

¹⁸ If an information statement rather than a full prospectus is issued financial reports for the prior 12 months are generally required by ASIC

10.2 Exception to disclosure requirements in the Corporation Act

Under the Corporations Act there are exceptions to the disclosure document requirements. A key exception applies where offers of shares are made (and accepted), in a 12-month period:

- (a) by no more than 20 investors, and
- (b) the amount raised does not exceed \$2,000,000 per annum. This would include an offer that provided for payment to be made in stages.

However, investors and the amounts they invest are excluded from the above thresholds if they hold a certificate from a qualified accountant to show that they either have:

- (c) a gross income of \$250,000 or more per annum in each of the previous two years, or
- (d) net assets of at least \$2.5 million¹⁹.

Given the expected number of shareholders and the amounts being raised it seems unlikely that an exemption from the disclosure requirements in the Corporations Act could be achieved.

10.3 Staged funding

As part of the capital raising, the investment may be staged through the construction so that money is only received by the LME on achieving key milestones. This could involve funds being placed in a trust account upfront to ensure the LME can access those funds when required but similarly protect those funds for return to investors should the project fail to move past an early stage.

10.4 Tax advice and financial structuring options

Tax advice on the funding model will ultimately be required from both the investor / producer perspective and the LME perspective. Investment by producers could be structured purely as an equity investment attaching to shares in the company and a related supply contract for a specific volume of water. However, as a 'not-for-profit' there is no dividend paid to equity holders and their investment is effectively given in return for a water delivery right (noting that this will also attract ongoing fees).

Alternatively, there may be merit in considering the investment by producers as a combination of a loan and equity. The loan would carry with it a right to be repaid over the life of the loan, with repayments only made when certain triggers are met within the LME. This would enable investing producers to have their initial contribution returned overtime. It would likely result in the annual water charges being higher, as prices would need to recover sufficient revenue to allow for loan repayments. Such an approach could have the added benefit of encouraging trading of shares (and associated water rights) to non-equity customers, where the initial investor keeps their rights under the loan.

11. Definitions

Definition	Meaning
ASIC	Australian Securities and Investment Commission
Cooperative Act	Cooperative Act 1997 (Qld)
Corporations Act	Corporations Act 2001 (Cth)
LME	Local Management Entity (Queensland)

¹⁹ Corporations Regulations 2001 (Cth) Reg 6D.2.03

Definition	Meaning
project	As set out in paragraph 2.1.
QCA	Queensland Competition Authority
Water Act	Water Act 2000 (Qld)
Water Supply Act	Water Supply (Safety and Reliability) Act 2008 (Qld)

Schedule: Details of existing locally managed irrigation entities in Australia

1.1 Recent Queensland Local Management Entities

Entity	Corporate structure	Approximate number of customers	Board	Voting rights of members	Other matters of interest
Mallawa Irrigation Limited (St George)	Company Limited by Guarantee	50	5 Directors - 3 Member Directors and 2 Independent Directors	Members holding more than 50 ML of water in the Scheme 1 vote at general meetings. Members with less than 50 ML can attend meetings and speak but unable to vote.	-
Theodore Water Pty Ltd	Small Private Company Limited by Shares	45	Minimum of 3 and maximum of 6 (with at least 1 independent and 2 member directors)	Shareholders are eligible for 1 share per ML owned in the Scheme. Each share is equal to 1 vote at general meetings.	75% support required for certain changes to the asset management plan.
Fairbairn Irrigation Network Limited (FIN) (Located in Emerald)	Large Company Limited by Shares	190	Minimum of 5 and a maximum of 7 with at least 2 member directors and 2 independent directors	Shareholders are eligible for 1 share per ML owned in the Scheme. Each share is equal to 1 vote at general meetings.	As a large company it is subject to the takeover provisions in the Corporations Act (which can be triggered in a number of circumstances, including where one shareholder's holding increases above 20%). The FIN constitution includes a restriction on any one customer (or their associates holding more than 25% of the

Entity	Corporate structure	Approximate number of customers	Board	Voting rights of members	Other matters of interest
					shares in the Company). Resolutions proposed by members at a meeting requisitioned by members must achieve 75%.
Eton Irrigation Cooperative	Non-Trading Cooperative without shares	330	5 which must include 3 Member Directors and 2 Independent Directors)	Members each have 1 vote regardless of their water entitlement	-

1.2 Other examples of customer owned irrigation Schemes

Entity	Start of local management	Model	Board	Other matters	Comments
Coleambally Irrigation Coop Ltd (NSW)	2000	Dual Cooperative (However has commenced winding up the mutual and will revert to being a single Cooperative)	4 Member Directors and 2 Independent Directors.	Members must hold a minimum of 10 ML in the Scheme.	CICL is situated in the Murrumbidgee valley in the NSW Riverina.
Coleambally Irrigation Mutual Co-operative Limited	1999		4 Member Directors and 1 Independent Director.	Membership gives a member 1 vote. Special resolution required for a number of key decisions including entering into a loan valued at 5% of the net assets of \$1.5 million whichever is the greater.	It provides irrigation and drainage services to nearly 500 farms owned by 350 businesses and has 295 members. The average size of an irrigated farm is 220 ha.
Pioneer Valley (Qld)	2005	Dual Cooperative	Asset Operator	(Rules not available on website)	Located near Mackay. Has over 300 customers.

Entity	Start of local management	Model	Board	Other matters	Comments
Harvey Water (WA) South West Irrigation Asset Cooperative South West Irrigation Management Cooperative	1996	Dual Cooperative	Current Asset – 3 directors, 2 member directors and 1 non-member director Operator – 6 directors, 5 members and 1 non-member director	(Rules not available on website)	Located in South West Australia. It has approximately 720 irrigator members and 350 non-member customers
Ord Irrigation Co-operation Ltd	1996	Dual Cooperative	(Rules not available on website)	(Rules not available on website)	Manages Stage 1 of the Ord River Irrigation Project
Murray Irrigation Limited	1995	Limited by Shares Unlisted Public Company	Btw 6 and 9 Directors permitted. No more than 3 non-member directors and no more than 6 member directors.	No member permitted to hold more than 5 % of the voting rights	Largest private irrigation water supplier in Australia with 2200
Western Murray Irrigation Ltd (NSW)	1995	Unlisted Public Company Limited by Shares	7 directors – 3 non-members and 4 members (one for each area and a general member director)	(Rules not available on website)	Western Murray Irrigation maintains 3 pump stations; 2 re-lift stations and 184 km of pipelines which supply and service over 4,100ha of irrigated land in Curlwaa, Coomealla and Buronga.
Murrumbidgee Irrigation Ltd (NSW)	1999	Unlisted Public Company Limited by Shares	No more than 8 directors. 2 are Class A directors, 2 are Class B directors, no more than three independent directors and the final may be	A and B Class shares issued. Holders get 1 vote per landholding in the irrigation area.	Serving over 3,260 landholdings owned by over 2,300 shareholder customers within an area of 378,911 hectares.

Entity	Start of local management	Model	Board	Other matters	Comments
			the Managing Director.	Must hold water entitlements to hold shares.	
Jemmalong Irrigation Ltd (NSW)	1995	Unlisted Public Company Limited by Shares	Not available on website	Not available on website	Distributes approximately 100,000ML