



National Irrigators' Council

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Public submission to water trading rules position paper by National Irrigators' Council

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Introduction

The National Irrigators' Council (NIC) is the peak body representing irrigators in Australia. The NIC's objective is to develop projects and policies to ensure the efficiency, viability and sustainability of Australian irrigated agriculture and the security and reliability of water entitlements. NIC currently has 21 member organisations covering a variety of states, regions and commodities.

While this document has been prepared by the NIC, each member reserves the right to independent policy on issues that directly relate to their areas of operation, or expertise, or any other issues that they may deem relevant.

NIC is pleased to be able to engage in the consultation process with the ACCC and has welcomed the opportunity to also have direct discussions with officers from the Commission. This is the first contact the NIC has had with the ACCC, however we would like it noted that some of our members have reported frustration with the ACCC's willingness to accept and act on their advice in past consultation processes. This has led to some members concluding that engaging in ACCC-style consultation is a waste of their time. This is an unfortunate situation and we hope and trust that the ACCC will give our submission and those of our members due consideration and that the views put forward will be reflected in the draft advice that is given to the Murray Darling Basin Authority.

Key issues

Coverage across all jurisdictions

The NIC has been formed as a peak body to represent the interests of all irrigators across the country, regardless of where they are located. One of our core policy positions is that irrigators should have access to a level playing field to the greatest extent possible.

As such, our most pressing concern with regard to the development of draft rules is that all jurisdictions within the Murray Darling Basin should be subject to the same rules, to the greatest extent possible.

At our July 2009 meeting, the NIC passed the following resolution:

“That NIC:

- (i) Reconfirm its commitment to equity across state borders in rules affecting water rights, use and trade;*
- (ii) Asks the Commonwealth to halt the development of any and all rule processes (including via ACCC) that cannot be enforced in all relevant jurisdictions: and*
- (iii) Asks the Council of Australian Governments to negotiate a position where sufficient jurisdiction is provided (howsoever that may be achieved) for rules to be made and enforced equally across all states.”*

Section 245(2) of the *Water Act 2007* provides that a transitional water resource plan containing trading rules will prevail over a Commonwealth rule, such as those being proposed by the ACCC, in the event of any inconsistency between the two.

The Act defines the transitional water resource plans for Queensland, New South Wales and South Australia in Schedule 4, yet notes that water resource plans for Victoria are to be “prescribed by the regulations”.

To some degree it is understood that Bulk Entitlements represent the Victorian water resource plans but this is by no means clear. NIC is aware of attempts to have either the Commonwealth or Victorian Governments identify exactly what constitutes the Victorian water resource plans but none of these attempts have been successful so far.

Given the lack of clarity surrounding the Victorian arrangements, it is possible that Victoria may end up with water trading rules (under whatever water resource plans it eventually submits) that are contradictory to the rules operating under the Basin plan. This could lead to rules being implemented in Victoria which are more favourable for Victorian market participants to the detriment of other states, or which are less favourable to Victorian irrigators – neither situation would be acceptable to the NIC.

Either way it would appear to be a fundamental flaw in the development of Basin wide trading rules if one jurisdiction is effectively excluded from the rules. NIC appreciates the rationale (put forward by ACCC officials in our discussions) that this is a policy matter that the ACCC cannot comment on, but we do not accept it. This is a significant structural design issue and in providing advice we believe it is something that the ACCC must address.

If the rules cannot be made to apply to all jurisdictions then they are meaningless. As per the resolution above, NIC calls for a halt to the development of all rules, including those that are the subject of this submission, until they can be enforced everywhere so that all irrigators have access to a level playing field. In this instance, we believe the identification of the Victorian water resource plans must be concluded prior to rules being further considered.

3.5 Stock and domestic water use

NIC is cautious about the trading of stock and domestic water. We contend that this water, along with that for critical human needs is provided for a specific purpose and should remain tied to land. Given the small volumes associated with stock and domestic entitlements, we find it hard to see what would be gained by making those entitlements tradeable.

3.6 Trade into and out of the MDB

NIC concurs with the ACCC that no specific rules need to be implemented to address trade into or out of the Basin. We submit that this is a political issue, not one for trade rules.

However NIC takes the opportunity to state that the MDB should not be seen as a solution to water woes outside of its boundaries. The system is already stressed and the current reform progress of which these rules are a part is designed to address that stress. Taking water out of the Basin is counter-productive to the aims of the reform program which irrigators support.

3.11 Metering

The NIC strongly supports metering of water extraction where practical. At its last meeting, the Council passed the following resolution:

“That the NIC fully supports accurate water metering and the full use of the law to investigate and prosecute water theft.”

However we are perplexed at the inclusion of this issue in discussion about the trading rules given that metering relates to extraction, not trade. Throughout the position paper, the ACCC discusses the involvement of non-landholder buyers and sellers of water who will clearly not need to have meters. It would seem that including metering in trade rules would discriminate between different market participants based on the intended use of water. As such, this position would appear to be at odds with the ACCC’s position at 3.4 that:

(1) There should be no restrictions on trade due to the purpose for which the water has, is currently, or will be used

Metering is an issue that should be properly dealt with by the relevant state authorities, not through trading rules.

4.1 The 4 per cent limit

As mentioned at the outset, NIC would like to see a level playing field for all irrigators when it comes to trade. The 4 per cent limit as it applies in Victoria is a barrier to trade. Unfortunately it prompted the NSW embargo which has now been lifted via an agreement between the Commonwealth and NSW that also restricts trade. In our view, two wrongs do not make a right.

NIC is also concerned that the 4 per cent limit is, perversely, harming the irrigators and communities that it is designed to protect, as the ACCC has pointed out. Not only are distressed sellers being prevented from liquidating an asset during the difficulties of the drought and low commodity prices (dairy in particular), but they are also potentially facing a greater disadvantage when new sustainable diversion limits (SDLs) are introduced. The Commonwealth and MDBA have stated that all water purchased by the Commonwealth will go towards “offsetting” reductions under any new SDLs (and inevitably it will be reductions). By being restricted in the amount of water they can sell to the Commonwealth because of the 4 per cent rule, Victorian irrigators are reducing the size of the “offset” and face the risk they will eventually face a far more significant cut – and all at once – than they would otherwise.

NIC supports the ACCC’s position that the 4 per cent limit – and any other barriers to trade, including the volumetric limit now in place in NSW - be removed across the basin immediately. NIC has made further comments in relation to the removal of barriers to trade and development of a mature water market in its submission to the Productivity Commission study into market mechanisms for recovering water – a copy is attached.

5.5 The role of water market intermediaries

A number of NIC members have raised concerns about behaviour, or potential behaviour, of water market intermediaries (brokers, water exchanges etc.). While, as a general rule, NIC would prefer to see a “light-touch” when it comes to regulation in the water industry, there is support for better regulation of the broking sector.

It may be true that the Basin Plan trading rules are not the correct forum for this discussion, but NIC believes the ACCC has some role in overseeing this sector and that the implementation of minimum standards – similar to those applicable to real estate agents and accountants etc should be pursued.

6.2 Trade in unregulated systems

NIC notes that trade in unregulated systems is an extremely complex matter that requires further investigation and discussion. We also note that the recent MoU between the Commonwealth and NSW contains a proposal to establish a taskforce to develop shepherding rules in that state. This may be a useful forum for further development of ideas for trading in unregulated systems.

On this point, NIC registers its strong position that water entitlements held by environmental agencies (including the Commonwealth Environmental Water Holder) should be treated no differently than any other entitlements. That is, any rules developed for environmental water use, including shepherding, should also be available to other participants in the market.

END OF SUBMISSION

ATTACHMENT 1

Productivity Commission study into Mechanisms for Recovering Water

Introduction and overview

The National Irrigators' Council (NIC) is the peak body representing irrigators in Australia. The NIC's objective is to develop projects and policies to ensure the efficiency, viability and sustainability of Australian irrigated agriculture and the security and reliability of water entitlements. NIC currently has 21 member organisations covering a variety of states, regions and commodities.

Irrigators have for many years sought recognition of their water entitlements as a property right and it is in this context that the NIC does not oppose government purchases in the market. The Restoring the Balance program (RTB) is an implicit recognition that water entitlements are indeed a property right and any change to them should be compensable. The NIC supports the right of "willing sellers" to sell their entitlements to whomever they please.

However, there remains concern among irrigators at the impact of the RTB. Some of these concerns include:

- Reduction of productive capacity in irrigation communities – loss of water = loss of wealth
- Impact on economy of local towns and regions
- Potential implications for major processors of food and fibre reliant on irrigation production – concern that buyback may take production levels in some areas to below critical mass resulting in the exit of processors with flow on effects to jobs and local towns
- "Swiss cheese" effect whereby the purchase of water entitlements and exit of irrigators leads to stranded or under-utilised assets, adding cost burdens to remaining irrigators and infrastructure operators
- Impact of a single large buyer (government) in the water market driving up prices, and subsequent "clifftop" effect when the government exits the market.

Irrigators' other main concern about the buyback is the illogical nature of the process as it stands – the government is buying water without a clear understanding of what the needs of the environment are and before a clear plan for the use of the water has been produced.

Nonetheless there is also support from many in the irrigation community for the buyback. Some certainly see the RTB program as an opportunity, rather than a threat, including for the following reasons:

- Allows some irrigators to sell part or all of their water with a view to either exiting the industry with dignity or to reinvest in efficiencies on-farm
- Has allowed some significantly distressed sellers to realise cash from their capital (water entitlement) to enable them to reduce debt or survive through the drought
- Provides the opportunity for a "smoothed" adjustment to likely reduced diversions under the proposed Murray Darling Basin Plan and future climate change and variability.

As mentioned above, the NIC is not opposed to the RTB program but it is concerned that the government has been too focussed on buybacks, and has not done enough to get infrastructure projects rolling, including on-farm efficiency programs. The NIC believes investing in efficiencies in

water use and delivery creates a win-win for all Australians. It reduces water use, provides water for the environment and helps maintain productivity in agriculture to the benefit of the wider economy.

It should be noted that this document is the first submission prepared by the NIC and each member reserves the right to independent policy on issues that directly relate to their areas of operation, or expertise, or any other issues that they may deem relevant.

Responses to specific questions

What are the objectives of the Restoring the Balance program?

Is the focus on acquiring entitlements the best way of achieving the environment's needs?

The NIC is not opposed to the acquisition of entitlements but believes the government is too focussed on buyback at the expense of investment in infrastructure to create efficiencies and provide water for the environment. We are also concerned that the program puts the cart before the horse – purchases are being made before environmental assets and the amount of water (and the timing and reliability of its delivery) they need are identified and before the Basin plan has even been drafted. We are also concerned at the lack of attention paid to the third party social and economic impacts of the program.

The government has so far spent \$840 million on RTB, but very little has yet been spent on infrastructure programs (the NIC notes that program guidelines for the On-Farm Irrigation Efficiency program are due for release shortly and accepts that much of the infrastructure programs are reliant on state plans being presented). Irrigators have expressed frustration that the roll-out of infrastructure programs has progressed at a glacial pace.

The NIC contends that there are alternative approaches to straight out purchase of entitlement that may better balance the needs of the environment with those of irrigators and irrigation communities, including leasing and derivative products (more detail later in this submission).

Is a 'no regrets' presumption a reasonable basis for purchasing entitlements, and at what point does this cease to be the case?

Irrigators are very concerned at the impact of a “no regrets” policy and the fact that the government has set no volumetric target for its buyback other than a dollar figure (\$3.1 billion). It would appear that the government has not identified exactly what the environmental needs are, what volume or water product it therefore needs to purchase, and what the likely impact of those purchases might be on remaining irrigators and irrigation communities.

It appears unusual to say the least that in this day and age a government program is proceeding spending hundreds of millions of dollars with no identified target, performance outcomes or measures of success.

The NIC sees significant risk to the Commonwealth and to irrigators in the “no regrets” policy through the potential to “overshoot” purchases, particularly in individual valleys, if not across the entire basin. For example, the Gwydir Valley Irrigators Association estimates that Commonwealth and NSW Government purchases of water in the Gwydir of some 86,000 ML equates to almost 20

per cent of entitlements in the Valley – yet the government has not indicated what its volumetric target (or environmental need) for that valley is (bearing in mind that the Gwydir ends in terminal wetlands and only in very wet years does it contribute to the rest of the basin – to a large degree it is a closed system). This potentially creates inefficiencies in the purchasing program, could lead to areas of more significant environmental need being short-changed, and may lead to a greater reduction in the social and economic base of the region than is necessary.

Irrigators have received assurances that the government buyback will help soften the blow of anticipated reductions in diversion limits under the new Basin plan, but are concerned that this is not being completed in a strategic or coordinated manner. For example while the Gwydir Valley has provided rich pickings for the buyback, at the other end of the scale no purchases have been made from the mid and upper Condamine region in Queensland and very few entitlements have been purchased from the Border Rivers area. This leads to concern that those areas may be disadvantaged if their new Sustainable Diversion Limit (SDL) is cut significantly under the Basin plan.

Most particularly, the lack of an identified, publicly available set of environmental aims means the program cannot possibly be operating at the most economically and environmentally efficient level.

What are the arguments for continuing the buyback after the new Basin Plan is implemented in 2011, and associated state water sharing plans start to be implemented in 2014?

It is the NIC's view that the emphasis should be firmly on gaining water through infrastructure programs, rather than buyback in the first instance.

A coordinated approach will be needed between the MDBA and the Commonwealth to ensure the SDLs in the Basin plan are set in a manner that considers the prospect of further purchases for the environment. Similarly, the Commonwealth will need to consider an approach for the wind-down of the RTB that ensures the environment's needs are adequately met without unnecessarily "over-shooting" the mark to the detriment of irrigators and irrigation communities.

The NIC sees the buyback as implicit recognition that water entitlements are a property right. If governments wish to provide water for the environment in the future, including after the Basin plan and associated Water Sharing Plans are implemented, then they should invest in infrastructure upgrades first before continuing to purchase water from willing sellers. However irrigators would like to see far greater transparency in the purchasing program than they are currently getting. As mentioned above, the NIC is supportive of the RTB program as a means of assisting the adjustment to lower SDLs in the future.

What implications do environmental demands across the Basin have on the targeting of purchases and the mechanisms and instruments that should ideally be used?

It is obvious that purchases (in most cases) should be made geographically so as to maximise the positive impact on the environmental assets that are being targeted. There is no point buying water for the Chowilla floodplain from the Upper Condamine. The question again highlights a key concern of irrigators relating to the buyback, in that the environmental demands were not clearly identified before the purchase program began.

NIC supports the notion that the government should consider innovative products to deliver the environmental outcomes it desires. Leasing, options and derivative solutions such as RiverReach (details described below) can provide environmental benefits by mimicking the natural flooding and

drying cycles of the MDB. In short, the Commonwealth gets access to water once certain thresholds are met in allocations, allowing the Commonwealth to top up or prolong natural flood events.

Should the buybacks be designed so as to reduce structural adjustment costs or should adjustment be addressed separately? If the former, are there particular buyback mechanisms that should be used to do this? If the latter, what approach should be used?

Structural adjustment is a term that can be difficult to define and means different things to different people. The NIC has been assured by government and the MDBA that the buyback will assist with the “adjustment” to a new future with less water. Separately there is the flow-on impact of the buyback in terms of reduced water and therefore economic activity in irrigation communities. NIC contends that “structural adjustment” in this sense has not been addressed by the government. As an example, it is understood that at least one cotton gin employing 30 people (FTE) has closed as a result of the government’s purchase of water from the Twynam Agricultural Company.

NIC re-affirms its view that the need for this type of structural adjustment would be negligible had the government placed more emphasis on infrastructure spending that actually helps stimulate economic activity in irrigation areas. If the buyback was better balanced with a suite of measures for returning water to the environment, structural adjustment needs would be lower. The buyback should be seen for what it is meant to be – a component of the overall package to realign water use in the MDB. It must be part of a coordinated approach that includes infrastructure investment, community support and investment in irrigation R&D. NIC is concerned that these elements have been left far behind in comparison to the buyback.

NIC believes there may be a case for separate structural adjustment support but is currently formulating that policy and this would be outside the scope of this study.

NIC has outlined alternative mechanisms elsewhere in this paper.

Does the exit grant package for small block irrigators play a useful role in the overall buyback scheme? Should it be offered again?

NIC members have suggested that the criteria for EC packages (and the small block irrigators exit package in particular) is too focussed on traditional dryland conditions, too rigid and has led to sub-optimal outcomes. Both the assets and off-farm income tests have excluded many small irrigators who would like to access the package. By definition, small block irrigators are often those who supplement their income with off-farm employment; or are those who are reaching the end of their working lives and have invested off-farm (as an alternative to superannuation funds, for example) for their retirement. In addition, in some irrigation industries (eg horticulture), the intensive nature of the production technology has in the past supported multiple-farming families in the same enterprise. This has meant that there are often multiple family dwellings on the one ‘block’; the value of these should be removed from the ‘farm assets’ test, and be returned to the ‘personal assets’ category.

While the NIC understands the government’s intention was to allow farmers to exit irrigation while staying in their own home, the criteria that irrigation infrastructure on these farms should be removed and the land not used for irrigation for at least five years is counterproductive and detrimental to irrigation regions. Should an irrigator wish to sell his water to the government and exit, he or she may also wish to sell their land to a neighbour who could expand, become more efficient and make productive use of the land. They could do this by purchasing extra water on the open market, investing in efficiencies to yield water savings to use on the new block, or using

“excess” water on their existing farm to irrigate on the new block. The restriction on further irrigation use of the land would appear pointless and destructive – remaining irrigators who may wish to use the block would not be using more water overall, indeed they would likely be making more efficient use of the water on the market given economies of scale, productive use of existing resources and (generally) good quality, irrigation-suitable soils.

Removing irrigation could also lead to problems for infrastructure operators, landscape and environmental management, and potential inefficiencies related to stock and domestic supply to relatively isolated homes.

It is unclear if the program was fully subscribed at its close or not, but if the true aim of the program is to remove a quantum of small irrigators and the water they use from the market, the criteria need to be revised should the program be re-opened.

The market for water

What impact has the Restoring the Balance program had on the price of water entitlements to date? What, if any, impact has this had on the market for seasonal allocations?

Anecdotally, and as basic economic theory would dictate, the RTB program has had the effect of increasing the price of water. This is an issue for the government to carefully consider – does it get the most efficient outcomes via its current purchasing approach? From an irrigators’ perspective, the current record low allocations mean that there is very little yield on entitlements and subsequently – again anecdotal only – there are few other productive purchasers in the market. It appears at this point that the government *is* the market. While this is positive for those irrigators selling their entitlement, it makes life difficult for any others wishing to purchase entitlement to plan for the future.

NIC is not aware that the RTB is having any significant impact on temporary trade.

How much influence would the choice of market mechanism used to purchase entitlements for environmental purposes have on the market for water?

Until environmental objectives and water requirements are defined, it is very difficult to say what the impact of other mechanisms might be.

Given the points made above, it is clear that the sheer size of the government relative to the market makes it likely that the government will impact on price, regardless of the mechanisms it might use. However the NIC contends that the use of derivatives and options may be a more strategic way for the government to achieve the environmental objectives it desires, without the need to necessarily purchase entitlements outright.

What impact has the entrance of the Commonwealth (and other governments) into the market for water had on background trade in water between third parties?

The Commission may wish to look at various water trading exchanges for information on trades such as at Murray Irrigation (<http://www.murrayirrigation.com.au/watexch>) or Waterfind (<http://www.waterfind.com.au>).

It is difficult to qualify an answer to this question given the lack of reliable data, but as mentioned above, anecdotal evidence suggests that the few other potential purchasers of entitlement have been squeezed out by the government’s involvement and subsequent increase in prices. Available

yield in this low-allocation environment and the impact of drought on the liquidity of other potential purchasers, suggests that they are less active in the market than may otherwise be the case.

How would speeding up or slowing down the Australian Government's water purchases influence the effects on trade between irrigators?

The major impact would be on price however this is also determined by the number of willing sellers on the market. Should there be a return to more "normal" allocations the government would likely find fewer sellers on the market.

What market mechanisms should be considered?

What are the advantages and disadvantages of the different market mechanisms that could be used to obtain water for the environment? In particular, how do they compare in terms of compliance and transactions costs and the ability to meet the different watering needs of environmental assets?

The NIC is supportive of innovative market products that meet the needs of both the irrigator and the environment.

This could include options such as leasing, forward contracts and derivatives such as the RiverReach program which has been trialled in the Murrumbidgee irrigation area and is referred to in the issues paper.

RiverReach, and products like it, aim to find market mechanisms to provide water for the environment while underpinning the security of access to water for irrigators. To illustrate the concept, consider a water entitlement is a "tank" that fills progressively throughout the year as water becomes available ("allocation" in regulated systems). Irrigators may wish to sell a part of that entitlement as water fills up the tank. For example, an irrigator may choose to sell to the government any water in their "tank" above a certain allocation, say 70 per cent. Once their allocation reaches 70 per cent, the government gets all of the "surplus" to use for the environment. This will be particularly useful for the environment when in wetter years more water is needed to create or prolong flood conditions, for instance.

There are a number of trigger points or other arrangements that could be put in place. Products that are new to the water market including futures, options and sale and lease back contracts could also be part of RiverReach.

Innovative market products can align the needs of both irrigators and the environment and in most cases will be preferable to the blunt instrument of direct entitlement purchases.

Of the other market mechanisms mentioned in the issues paper, the NIC does not oppose the **purchasing of entitlements in the market place**, **leasing of entitlements** and the **purchasing of environmental services** (although we would require further detail on the latter were it to be considered).

Purchasing of entitlements in the market place would be a preferable approach to the current tender proposal given the likelihood it would be more transparent and would help develop water markets to a more mature level. The government could actually assist in the development of a more mature market by stimulating the necessary exchange of information as the largest player in the market.

The NIC is uncomfortable with the current **tender** process given its lack of openness and transparency and the lack of timely information provided about sales, volume and prices.

NIC does not oppose the **purchasing of land and water** entitlements in the market place, but submits that it is sub-optimal and has so far been notable for a lack of clear strategy and measurable outcomes.

In relation to the involvement of governments in **purchasing water on the temporary market**, NIC understands that this has been ruled out by the government and submits that it is not an appropriate avenue for a permanent solution to the Basin's woes. More generally, we would not be opposed to the Commonwealth Environmental Water Holder trading in the temporary market post-buyback but would expect it should only be for specific, clearly articulated environmental needs at a given time and not a permanent activity. The government would need to be alert to the potential impact of government activity in the temporary market on irrigators, food production, local communities and the wider economy.

We have commented elsewhere on the efficacy of **subsidies** to leave irrigation. We are unconvinced on the merits of **covenants** – irrigators would be opposed if the characteristics of entitlements purchased for the environment were to change. It is irrigators' understanding and position that entitlements purchased by the Commonwealth will be treated the same as any other entitlement.

With the benefit of the experience gained from three tenders under the RTB program:

- *What are the advantages and disadvantages of the chosen rolling tender process?*
- *How could the tender process be improved?*
- *How do you think an open market process would have fared instead?*

Irrigators are very frustrated that the current tender process has not provided timely, useful and accurate market data. For the process to work effectively it is critically important that the market is informed immediately of all transaction information as soon as practical after a contract is signed. The provision of historical, averaged and delayed information on trades has little or no value and puts potential sellers at a disadvantage.

The department seems concerned about privacy considerations in providing this information but it should at least be able to provide the same sort of market information that is easily accessible in the real estate or share markets.

Irrigators have also reported frustration with the unwieldy nature of the tender process and long delays in processing. This has made it difficult for them to plan their business activity.

Similarly, there have recently been reports of some irrigators being told either verbally or by email that their tender has been accepted, only to be informed weeks or months later by letter that they have missed out. Potentially this has calamitous implications for their businesses and families, but presumably is a function of human error, rather than a flaw in the process itself.

Do we need a portfolio of mechanisms and water products?

What mix of market mechanisms and water products should the Australian Government be using to achieve its environmental objectives?

As already stated, the NIC would prefer to see greater emphasis on infrastructure spending to achieve water savings.

It is appropriate that a mix of options is used by the government and these should include (and be weighted towards) infrastructure investment and mutually beneficial market products to provide flexibility and certainty for irrigators and environmental purchasers, maintain the productive capacity of our irrigation regions and ensure a sustainable future for rural Australia.

NIC would support the government's involvement as a player in the open market for water, noting its involvement would likely help to bring that market toward greater maturity, and foster the development of innovative water market products.

Upgrading infrastructure

Should water purchasing and infrastructure upgrades be coordinated and, if so, how?

This question gets to the heart of much of the concern among NIC members about the current approach of the buyback. In an ideal world, the answer is yes, but the "how" is much more difficult to describe. Firstly, the question highlights the major fault with the program – that is, that the government is seeking to buy water for the environment without first considering exactly what (and how much) the environment's needs are.

NIC is concerned at the potential that infrastructure programs may be under-subscribed as many irrigators may be reluctant to invest (even jointly) because of uncertainty surrounding the future reliability of their entitlement (ie the new SDLs under the Basin plan). To quote one irrigator in the Murrumbidgee area: *"I am scared to do anything on my farm because of the uncertainty"*. It is also true that some irrigators (and operators) may prefer not to take up government funds and share the water with the environment, and will instead fund their own infrastructure works to recover more water for their farms to boost their productivity. Reluctance may also stem from the complexity and cost associated with putting together proposals that meet the government requirements. Nonetheless, NIC is encouraging all parties to take advantage of the opportunity provided by government infrastructure programs.

Infrastructure operators are also facing difficulty in how to modernise their systems when they cannot possibly know the likely future shape of their customer base. To give an example, an operator manages a channel that currently serves 10 irrigators, but it requires an upgrade or reconfiguration. Two have sold their water to the Commonwealth and exited irrigation. How can the operator possibly plan for investment in that channel if they don't know if any of the remaining irrigators will sell out in the coming years or what the likely new SDL for their region will be?

If the program was rolled out in a more logical fashion, many of these issues would not exist or would be significantly lesser concerns.

Nonetheless, NIC acknowledges that we now have what we have and will need to work within the current parameters.

NIC, governments and irrigators are all struggling with how to achieve the integration of the two programs or what could more generally be termed "adjustment".

In an ideal world, irrigation communities would themselves identify those areas that need rationalisation, upgrading or even closing down. It is better this comes from the ground up than top

down. However to achieve community consensus is extremely difficult – some NIC members have tried, but failed to win the level of support necessary for a wholesale re-configuration of certain districts. We are dealing not only with people’s businesses that they have worked on for many years and often many generations, but also family homes, lifestyles and communities. This makes it impossible to divorce these sorts of decisions from emotion and renders a strictly economic approach to the problem flawed.

It is almost certain though that if wholesale changes are considered (ie a whole district opting to sell their water and exit irrigation or move elsewhere) then the government will need to be prepared to pay a premium to aid and stimulate the adjustment.

NIC is working with infrastructure operators on how best it might help communities to further examine the options for an integrated approach to infrastructure and buybacks and is keen to work with the government on possible solutions. In areas without infrastructure providers it will be very difficult to provide any coordination.

What potential is there for a more cost-reflective approach to pricing of water delivery to obviate the need for targeting purchases of water?

As water is only one component of irrigation businesses it would be difficult to see how “pricing-out” some irrigators (as the question seems to imply) would be effective or efficient. Irrigators already operate in a full cost recovery environment and the government would still need to carefully target water purchases to meet its environmental targets, howsoever defined.

How well has the irrigator-led group proposal component of Restoring the Balance addressed the possibilities for taking group action that coordinates infrastructure upgrades and water sales? How could it be improved?

See answer two questions above for a description of why this has been a difficult element of the program. NIC has had informal discussions with government about the possibility of engaging community facilitators to help drive some of these proposals, but this is in the very early stages.

Feedback from our members suggests that this part of the program would work better if the infrastructure operators were more fully engaged by the department in negotiations.

Impediments to the use of particular market mechanisms

What impact is the 4 per cent limit having on the market for water entitlements?

What impact is it having on the effectiveness and efficiency of the Australian Government’s purchasing programs (both under the RTB program and under The Living Murray)?

To what extent are irrigators who wish to sell their entitlement being disadvantaged by the limit?

Is a limit on outwards trade the best way to address concerns over possible socio-economic impacts on particular irrigation areas?

Is the Commonwealth–Victorian agreement on the 4 per cent limit a satisfactory way to allow a greater quantity of entitlements to be purchased in Victoria?

What impact is the NSW Government’s ban on sales of NSW entitlements to the Commonwealth for environmental purposes likely to have on the ability of the buyback to obtain water efficiently and effectively?

The 4 per cent cap being imposed in Victoria, and the retaliatory embargo currently imposed by the NSW Government, mean there is not a level playing field for irrigators across the country in terms of

the buyback. Prior to the embargo being implemented, it was clear that NSW was the main source of purchases by the Commonwealth due to the operation of Victoria's 4 per cent cap.

At its July meeting, the NIC unanimously passed the following resolution which is pertinent to this issue:

"That NIC:

- (iv) Reconfirm its commitment to equity across state borders in rules affecting water rights, use and trade;
- (v) Asks the Commonwealth to halt the development of any and all rule processes (including via ACCC) that cannot be enforced in all relevant jurisdictions; and
- (vi) Asks the Council of Australian Governments to negotiate a position where sufficient jurisdiction is provided (howsoever that may be achieved) for rules to be made and enforced equally across all states."

The 4 per cent cap was designed to slow the rate of change in irrigation areas subject to trade. Perversely the NIC contends that the cap (and the NSW embargo) is impacting negatively on irrigators who want to - or are desperate to - sell their water. NIC is concerned that there may be significant numbers of irrigators forced into bankruptcy if they cannot sell their water because of these trade restraints.

In addition, the cap in Victoria may also be more problematic for Victorian irrigators in future in that less water may be purchased from that state by the government and subsequent reduction in SDLs under the Basin plan may therefore be much higher. So far from slowing the rate of change, it may in fact lead to a much more dramatic change down the track.

The NIC understands the rationale behind both barriers to trade, but would like to see a level playing field, as much as possible, across all jurisdictions.

Termination fees

How substantial are the impediments to trade in entitlements created by the imposition of termination fees?

Any fee involved in a transaction can be an impediment to trade, but termination fees are now a regulated, accepted part of the water market and the level of impediment to trade is no different than any other fees relating to general transactions – be they stamp duties on property, GST or real estate agent's fees. Termination fees are designed to protect third parties (specifically, remaining irrigators) not involved in the transaction.

Is the potential for irrigation assets to be stranded a relevant concern? Should some buyback mechanisms be preferred over others because they have a lower propensity to lead to stranded assets?

Yes. Although in principle the costs of stranded assets to an infrastructure operator can be covered for 10 years by termination fees, the reality is that the infrastructure that is being "protected" by that fee will have a substantially longer life – usually decades longer. In addition, the non-strategic nature of the current approach to buyback makes it extremely difficult for operators to plan for upgrades in the future and longer term planning of delivery infrastructure is also affected by the uncertainty (alluded to earlier in this submission).

Stranded assets are also an issue on-farm. Irrigation infrastructure on-farm (channels, pipes, drip systems) is worthless without water and the value of the land is considerably less once water is removed.

Are termination fees likely to help or hinder the efficient use of, and investment in, irrigation infrastructure during the buybacks?

NIC submits that they are unlikely to be a problem and in any event their role in enabling remaining irrigators and operators to service infrastructure costs far outweighs any negative impacts.

How can the right incentives for investment in irrigation infrastructure be achieved during the buyback program?

Government must ensure that the guidelines and criteria surrounding infrastructure programs are sufficiently flexible and not overly bureaucratic so that farmers and operators will be willing to go through the “pain” of dealing with government. Programs where water is sold to government at a premium in return for certain standards of work appear to be preferable as they allow the farmer/operator to make decisions about how to invest and what yield they are likely to achieve from various investments. The risk is in the hands of the farmer/operator and administration costs are reduced by not having government checking and re-checking the level of savings from the investment time and again.

What impact are termination fees likely to have on an irrigator’s willingness to sell and the cost of the buyback?

They do represent a cost, but as mentioned above, we do not believe they have any greater impact than other transaction costs in other industries.

Transaction costs

Are the costs associated with trading water entitlements (including those associated with delays and lack of market information) higher than they should be?

Are these costs a significant impediment to the efficient operation of government water buybacks and the water market more generally?

How might these costs be reduced?

As stated earlier, NIC does not believe transaction costs represent a significant deterrent to trade. NIC members have consistently reported frustration with delays in processing trades and this is a matter that needs to be taken up with state governments.

Government Procurement Guidelines

To what extent have the CPGs restricted or limited the design of current DEWHA purchasing mechanisms and the decision to buy only water entitlements?

What impact might the CPGs have on the Commonwealth’s ability to use alternative purchasing mechanisms to buy water products other than water entitlements?

It would appear that CPGs have limited the flexibility that government might have in approaching its buyback program, particularly in relation to participating in the open market. This is a matter for

government but to find the most efficient method of operating the buyback it may need to investigate how “flexible” the guidelines can be.

END OF SUBMISSION

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