

**QFF Submission to
Productivity Commission inquiry into
Market Mechanisms for Recovering Water in the
Murray-Darling Basin
SEPTEMBER 2009**

Queensland Farmers' Federation (QFF) is the peak body representing and uniting 16 of Queensland's rural industry organisations who work on behalf of primary producers across the state. QFF's mission is to secure a sustainable future for Queensland primary producers within a favourable social, economic and political environment by representing the common interests of its member organisations'. QFF's core business centres on resource security; water resources; environment and natural resources; industry development; economics; quarantine and trade.

Our goal is to secure a sustainable and profitable future for our members, as a core growth sector of the economy. Our members include:

- Australian Prawn Farmers' Association,
- CANEGROWERS,
- Cotton Australia,
- Growcom,
- Nursery and Garden Industry Queensland,
- Queensland Chicken Growers Association,
- Queensland Dairyfarmer's Organisation,
- Queensland Chicken Meat Council,
- Flower Association of Queensland Inc.,
- Pork Queensland Inc.,
- Biological Farmers of Australia
- Fitzroy Food and Fibre Association,
- Pioneer Valley Water Co-operative Limited,
- Central Downs Irrigators Limited, and
- Burdekin River Irrigators Association

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Submission Overview and recommendations

Irrigators in the Qld Murray Darling catchments support the concept of a buyback program to recover water for the environment. A workshop for Qld MDB irrigators conducted by QFF in October last year raised the following issues in regard to the implementation of the water purchasing program and other programs designed to implement 'Water for the Future':

1. It is expected that the Basin Plan will set environmental flow requirements for Basin catchments which are likely to reduce current entitlements when existing water resource plans are reviewed from 2014.
2. The focus of the proposed Commonwealth Water for the Future programs must be on achieving environmentally sustainable levels of take of water in the Qld catchments to give irrigators some certainty about farming for the review of water resource plans.
3. Environmental objectives to guide the development of the proposed programs must be clearly defined and justified for each Qld Murray Darling catchment.
4. Targets must be established for the buy-back program based on an assessment of ecological assets in the Northern Basin and their watering needs including management arrangements for the delivery of water. The environmental objectives and strategies of the current water resource plans for the Qld Murray Darling catchments must be accounted for in this assessment.
5. Water use efficiency programs on-farm must be fully investigated to assess whether these programs can achieve water savings that it is feasible to share between irrigators and the

environment. Investigations must be conducted to ensure that programs best suited to achieve objectives are selected for detailed design and implementation.

6. Irrigators and their communities must have a continuing opportunity to influence the development of these programs. They must be fully engaged in the investigations to select, design and implement programs particularly the buy-back program.
7. Irrigators in the Condamine Balonne could be disadvantaged in participating in the water buy-back if the resource operations plan is not finalised as soon as possible. Irrigators may not wish to enter into contracts for the sale of water without an approved ROP.
8. Programs must be able to address different water products and particularly unregulated water which comprises a significant component of water entitlements in the Qld Murray Darling catchments
9. There is a need for better information about the irrigation districts in the Qld Murray Darling catchments as an input to the planning, design and implementation of Water for the Future Programs. Information needs to be collated on issues such as water use, cropping, environmental and socio economic issues, water saving opportunities and vulnerability to the impacts of loss of irrigation entitlements.

QFF's approach to Commonwealth water recovery programs has sought to address these issues by advocating a planned approach to the Commonwealth buyback scheme and the State managed on-farm water use efficiency program because the outcomes of both programs are fundamental to the achievement of the following high level objectives:

- a. Increased provision of water for environmental flows to maintain or improve the health of riverine assets
- b. Reduction of consumptive water use in the Qld MDB
- c. Maintenance or improvement of community and industry resilience

We also strongly advocated the need for best practice engagement of irrigators and community stakeholders in the development, delivery and governance of the programs in delivering the outcomes sought.

Our proposal has been rejected with the Commonwealth managing the buyback program and the State Government having responsibility for the development and management of the on-farm water use efficiency program.

Irrigators are increasingly concerned that the lack of progress with purchasing in the Qld MDB under a no regrets approach may reflect underlying impediments to the purchasing of water in these catchments. It is being questioned whether the Commonwealth has an interest in purchasing unsupplemented entitlements which account for over 70% of allocations in these catchments. There is also concern that governments are yet to resolve how to achieve improved environmental outcomes from Qld MDB water entitlements including how to shepherd purchased water. The problem of implementing a closed reverse tender process in the absence of a functioning water market is also a significant limitation on purchasing of water from willing sellers. The lack of feedback to entitlement holders in regard to unsuccessful bids is adding to the level of uncertainty and concern that Qld irrigators are not being given an even chance with southern irrigators to soften the blow of future entitlement reductions. The level of engagement with irrigators has been very limited which has increased the level of uncertainty and negative response to the buyback program.

To address these problems the following actions are recommended:

1. The Commonwealth Environmental Water Holder (CEWH) must take greater responsibility for working with jurisdictions and industry as a matter of urgency to develop a more sophisticated set of market based instruments to facilitate the delivery of improved environmental flows. The CEWH should also be permitted to broaden its approach rather

than having to rely on purchasing of tradeable water entitlements to achieve environmental watering plan outcomes.

2. The Commonwealth should engage irrigators in the Qld MDB in regard to conditions for the conduct of further purchasing under a no regrets approach. Engagement should seek to improve information on the program and provide for irrigators in priority areas to submit coordinated bids to sell a package of water entitlements for an agreed value.
3. The release of the draft Basin Plan in mid 2010 with the environmentally sustainable levels of take of water in the Qld catchments should allow a more planned approach to the implementation of buyback in the Qld MDB to be adopted. Again there is a need for an enhanced level of engagement with irrigators and groups of irrigators to develop effective ways to implement water purchasing.
4. The Commonwealth must ensure that the buyback program is implemented in a fair and just way across the Basin and must ensure that the program continues until this outcome is achieved.
5. The coordinated implementation of the buyback and water use efficiency programs is required to achieve increased environmental water provisions and reduced consumptive water use of water for environmental flows while supporting the maintenance or improvement of community and industry resilience. Groups of irrigators in the Qld MDB should have the option of submitting business cases to DEWHA for the coordinated sale of a grouping of water entitlements and the implementation of water use efficiency measures on farm to recover water and deliver productivity improvements.
6. Arrangements are required to reconcile water recovery outcomes with NWI risk assignment implications. Reliability reductions as a result of the implementation of catchment water resource plans from 2014 will also need to be taken into account.

Response to specific issues raised by the Commission

1. Objectives of the Restoring the Balance Program

- a. *Is the focus on acquiring entitlements the best way of achieving the environment's needs?*

A well developed and transparent program for the purchase of water entitlements from willing sellers is an important mechanism to have available to recover water for environmental flows. However it is difficult to assess whether this would be the best tool to achieve environmental needs without an environmental water plan to define what water is required and when and how it should be delivered. Irrigators support the concept of the Commonwealth holding entitlements which can be managed to deliver environmental outcomes in accordance with a defined plan.

However, with a well planned approach to recovering water for the environment, a 'buyback' program should have a suite of mechanisms available to deliver required outcomes. Given the national funding commitment and the significant impact buyback will have in water markets, the Commonwealth has a responsibility to ensure that the best range of market based instruments is available to recover water for the environment in different parts of the Basin. Accordingly, it is recommended that CEWH work with jurisdictions and industry, as a matter of urgency, to develop a more sophisticated set of market based instruments to facilitate the delivery of improved environmental flows in catchments in accordance with an environmental watering plan that has been developed with the full engagement of water users.

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

A no regrets approach is an acceptable way to initiate the purchasing of entitlements in defined priority areas given the time lags involved in taking a planned approach. However, it is assumed that prior to implementing 'no regret' water purchasing, the Commonwealth has determined what purchased water is required for and how it can be delivered. These issues do not appear to be adequately addressed in the Qld MDB.

It is essential that a planned approach is adopted as soon as possible to achieve value for tax dollars based on defined environmental objectives and water purchasing targets. The release of the draft Basin Plan in 2010 with defined sustainable development limits for catchments and the basin as a whole should provide the basis to implement a planned approach which coordinates buyback and water use efficiency programs with full and effective community and industry engagement to achieve successful delivery of programs.

- c. *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?*

Water recovery programs will not have confirmed targets until the Basin Plan, including the environmental watering plan, is approved in 2011. State catchment water resource plans will give effect to the Basin Plan from 2014 but there is still provision in the Commonwealth Water Act 2007, for a transition period of up to 5 years to achieve sustainable diversion limits defined in the Plan. The approved Basin Plan will also address the allocation of risks in relation to reductions in water availability and changes in water reliability as a result of the Plan. A process must be put in place for the implementation of the Basin Plan which reconciles water recovered through buyback and other programs with risk allocation under the Act. This will be needed to guide further purchasing and if necessary to implement arrangements for compensation payments that entitlement holders may claim under the provisions of the Water Act 2007.

Consideration must also be given to the slow progress being made in the Qld catchments with the implementation of no regrets water purchasing. The lack of progress may reflect the need to take time to address a range of potential impediments to the implementation of the buyback program. For example, DEWHA has indicated that the delay in the ROP in the Lower Balonne is an impediment to the implementation of water purchasing. In addition, shepherding rules for purchased water in NSW will have to be put in place before enhanced environmental flows can be delivered. It is also expected that a lag in the response to matters addressed in items 1 d. and e. below could also delay the implementation of buyback in the Qld MDB. Importantly, the Commonwealth must ensure that buyback program is implemented in a fair and just way across the Basin and ensure the program continues until this outcome is achieved.

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

Water resource plans for the Qld Murray Darling catchments define environmental flow objectives to meet assessed environmental needs. To achieve these objectives, the plans impose flow based rules to provide for the passing or release of environmental flows from storages and to restrict the take of water from streams (unsupplemented water) in different flow conditions. The 'Framework for Determining Commonwealth Environmental Watering Actions Discussion Paper – May 2009' indicates that 'the CEWH has been established as a holder and manager of tradeable water entitlements, rather than as a manager of a water reserve with

specific environmental characteristics or as a manager of environmental flow rules.’ It will be a matter for the Basin Plan and particularly the environmental watering plan to address how these two approaches will be combined to achieve environmental outcomes in the Qld MDB. However, it is recommended that CEWH be permitted to broaden its approach rather than having to rely on the purchasing of tradeable water entitlements. It is also important that the CEWH initiate investigations into the targeting of purchases and mechanisms and instruments that could be ideally used in this part of the Basin. These investigations must involve jurisdictions, industry and irrigator groups. It is imperative that environmental demands are defined to ensure that purchases of entitlements and mechanisms and instruments used are well targeted to facilitate a planned and managed approach.

e. How should environmental water be allocated across competing projects and sites?

It is also pointed out in the CEWH framework that the exact combination of water entitlements purchased will have a ‘significant impact on the approach to environmental watering that is possible across the Basin.’ In addition, it is recognised that the decision framework will require significant amount of information and data to effectively conduct the four step process proposed to prioritise environmental watering actions and match these priorities with available water. It will be difficult to address the above issues unless the purchasing program is developed to address defined environmental objectives. In implementing this proposed framework in the Qld MDB, the characteristics and deliverability of entitlements particularly unsupplemented entitlements will need specific consideration together with the adequacy of information (current or planned) to support the approach. It is imperative that a very transparent purchasing process is implemented that can account for the type of entitlements held and how these entitlements can be best used in addressing environmental needs. A robust monitoring and evaluation program must also be implemented to ensure that the community is well informed about decisions made and results achieved.

f. 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?

The buyback program must be well targeted to address recovery of environmental water. This will make the task of achieving sustainable diversion limits with the implementation of the Basin Plan less onerous. The sale of water will also provide irrigators with the opportunity to invest to improve productivity and gear farms to use water more efficiently. The benefits of a planned approach which coordinates buyback and water use efficiency programs is addressed later in the submission. However, the buyback program must be implemented in a way that maintains or improves community and industry resilience. QFF is concerned that while a number of studies are to be conducted into economic and community issues they will not be effective in benchmarking current socio-economic performance at a regional level as a basis for progressively evaluating the impact of the implementation of buyback program and the Basin Plan. An investigation of this nature is required in the Northern Basin which is specifically designed to take into account local and regional issues such the impact of purchasing in small irrigation communities which are widely dispersed.

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

This program has not been implemented in the Qld MDB and its relevance in this part of the Basin is questionable.

2. Market for water

- a. 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?*

Only 425ML of supplemented medium security water has been purchased by the Commonwealth in the Qld Border Rivers catchment as reported at the end of August 2009. 3,195 ML of supplemented water in total has been permanently traded in the Border Rivers since the resource operations plan was approved in March 2008. This represents 1.41% of the total volume of supplemented allocations.

SunWater report that there have been no temporary transfers in the Macintyre Brook scheme. Department of Environment and Resource Management report that there have been some limited temporary transfers of unsupplemented water in the Border Rivers groundwater.

There is insufficient information available from only 15 months of water trading in the Border Rivers to provide any response to this question. The resource operations plan for the Condamine has only recently been approved. However, if the Commonwealth proceeds with significant purchasing in the Border Rivers and Condamine at this very early stage of the development of water markets in these catchments, the program could have a significant influence on setting the initial market price of water.

- b. DEWHA is now publishing average prices paid for entitlements. What impact is this likely to have on bids in subsequent tenders or one-off purchases?*

The provision of average price paid is of limited value for purchases of supplemented water. The Department also points out on its website reporting on progress with water purchasing that average prices are not an indicator of the current price the Commonwealth is willing to pay as this is effected by 'factors such as market price movements, reliability of entitlements, expected environmental benefits and the cumulative volume of purchases that have been made in each catchment.' Average prices are also only provided where there have been five or more sales and no details are provided on the location of the purchase other than the reference to the broader catchment.

There is very limited market information to help irrigators to determine a value for their licences to inform their expressions of interest to sell entitlements to the Commonwealth. Irrigators that depend on access to river flows (unsupplemented entitlements) are particularly concerned about their ability to achieve a market based return for the investments they have made on farm to store and use their water supplies. These issues must be better addressed if irrigators in these northern catchments are to participate willingly in the buyback program.

It is important also that DEWHA provide as much information as possible about progress with purchasing in catchments. Irrigators in the Qld MDB are seeking updated information on a range of issues concerning the program in the Northern Basin including:

- i. How many offers have been received, accepted, rejected or remain unassessed?
- ii. Where have they come from?

- iii. What water products feature in the mix?
- iv. When can irrigators with unassessed tenders expect to receive a response? What is the response process?
- v. What are the environmental objectives for the Qld MDB purchase rounds?
- vi. Putting price to one side what sort of water where and why is proving the most attractive to you
- vii. When, how and in what detail will the results of the round be made public?
- viii. What is the schedule for future southern and northern purchase rounds?

DEWHA could also provide more advice on funding limits for each program round and progress reports re the likely availability of funding as the round progresses. For example, irrigators in the Lower Balonne were advised in early September by DEWHA that their offers could not be pursued as the Program was fully subscribed before the assessment round for their applications had commenced.

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

As outlined above, the Commonwealth purchasing via a tender process will have a significant impact on catchment water markets. It is difficult to answer this question given the limited market development in the Qld MDB and the slow progress in purchasing. However, the Commonwealth is likely to find that they cannot simply rely on the RTB process to recover water to meet environmental requirements. As outlined above, the Commonwealth needs to be able to choose from a suite of mechanisms to successfully complete the buyback program.

- d. *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?*

Again there has been insufficient purchasing to provide a response to this question. DERM trading reports show that in addition to 3,195ML of supplemented water traded, there has been 1,267ML of unsupplemented water purchased in the Border Rivers catchments. 5.5ML of unsupplemented water has been traded in the Condamine since the ROP was approved earlier this year. The Commonwealth is yet to purchase unsupplemented water in these catchments. There has been some trading of supplemented water (720ML) and unsupplemented water (1,325ML) in the Warrego catchment but this is a low priority catchment for Commonwealth water purchasing.

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

Irrigators in the Qld MDB are concerned about the slow pace of water purchasing in the Qld catchments. Their concerns reflect a high degree uncertainty about the conduct of the Commonwealth's water purchasing program and the problems many face coping with farm financing following the drought.

3. What market mechanisms should be considered

- a. *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?*

Irrigators do not consider that the current buyback process is sufficiently transparent particularly in catchment areas where there is a lack of market information. Irrigators would favour the environmental manager purchasing entitlements in the

open market place. The RTB expression of interest approach provides no direct feedback on price and is raising uncertainty regarding Commonwealth purchasing intentions in the Qld MDB. If a tender or auction process is required to meet Commonwealth purchasing requirements then variations to the RTB process warrant investigation and must allow for bidding on both supplemented and unsupplemented water entitlements.

Other mechanisms warrant investigation in delivering defined environmental outcomes. The option of purchasing seasonal allocations would be a useful mechanism which has already been applied in the Lower Balonne to support bird breeding event. Covenants are also worthy of investigation. They could be applied statutorily to bind an entitlement holder to comply with obligations not to take water during certain flow events or to release water from on farm storage at particular times. Covenants may be particularly valuable in managing water that can be made available from water harvesting licences. As proposed above, the CEWH is best suited to investigate the mechanisms for recovering water to accommodate the environmental watering plan.

- b. *Are there other market mechanisms, not listed above, that the Commission should be considering?*

No further comments.

- c. *With the benefit of the experience gained from three tenders under the RTB program:*
i. *What are the advantages and disadvantages of the chosen rolling tender process?*
ii. *How could the tender process be improved?*

Qld MDB has limited experience with the implementation of the RTB program. Refer to comments in 3a

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

Apart from comments made in 3a, irrigators in high priority areas in the Qld MDB have an interest in investigating with the Commonwealth how market value could be established for the purchase of a group of entitlements to deliver defined environmental flows. Other options worthy of investigation are contracts with individual irrigators or groups of irrigators to provide access to substantial water supplies on a seasonal basis to achieve defined environmental flow outcomes.

- e. *Should water purchasing and infrastructure upgrades be coordinated and, if so, how?*

The outcomes of both the Commonwealth buyback program and the Qld Healthy Headwaters project are fundamental to achieving increased environmental water provisions and reduced consumptive water use of water for environmental flows while supporting the maintenance or improvement of community and industry resilience.

It is difficult to see how these objectives can be efficiently and effectively addressed while the buyback program is run on a standalone basis with little relationship with or connection to infrastructure upgrades and basin planning to address environmental and community needs. Irrigators in the Qld MDB would welcome a more coordinated approach to implementation of the buyback and water use efficiency programs. They advise that as a result of significant recent drought periods that many will have difficulty justifying on farm water use efficiency investments unless they have the opportunity to sell water to reduce debt levels and fund expected costs of implementing on farm infrastructure improvements.

Governments and stakeholders must work to achieve a more harmonized approach. This could involve cooperative planning at a regional irrigation scale to help irrigators examine their options for water purchasing and water use efficiency and then a call for those interested to submit their propositions from which an aggregated outcome could be developed for government investment decision. Such an approach will engage affected regional irrigation communities and make it easier to justify purchasing decisions in terms of value for money, meeting environmental priorities and resilience of the communities.

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

The next price paths for schemes in the Qld MDB have to be in place by July 2011. These prices only affect about 15% of water allocations in this part of the basin.

- g. *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?*

Irrigators in the Qld MDB are interested in submitting business cases to DEWHA for a coordinated sale and infrastructure upgrade. They are of the view that cases can be developed to address environmental needs in areas such as the Lower Balonne by providing a selection of water entitlements which are capable of providing water from a range of flow thresholds across the floodplain at an assessed value together with a coordinated program for on farm water use efficiency measures to achieve targeted productivity outcomes including a share of savings. They would like to initially put forward a proposal for the next round of no regrets purchasing.

- h. *Impediments to market mechanisms*

It is not considered that termination fees or transaction costs will present significant impediments to trading however these issues warrant monitoring together with other issues as trading markets develop. The QFF submission to the ACCC Issues Paper on water trading rules addressed a range of issues. A copy of this submission could be made available to the Commission if so requested.

- i. *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?

These issues need to be answered by DEWHA particularly as part of the investigations the CEWH needs to undertake into varied mechanisms to recover environmental flows.