

Gwydir Valley Irrigators
Associations Response to
Productivity Commission Draft
Research Report

*Market Mechanisms for
Recovering Water in the
Murray-Darling Basin*

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This submission contains no confidential material.

Introduction: The Gwydir Valley Irrigators Association (GVIA) is a voluntary organisation that represents the interests of irrigation entitlement holders in the Gwydir Valley of North-West NSW.

Membership of the organisation represents in excess of 90% of the privately owned (non-government) water entitlement in the valley, covering regulated, unregulated and groundwater sources.

The Association is a member of both the NSW Irrigators Council and the National Irrigators Council, but reserves the right to express views independently of these two bodies.

GVIA appreciates the opportunity to provide this response to the draft research report “Market Mechanisms for Recovering Water in the Murray-Darling Basin” inquiry.

GVIA will respond by addressing the specific draft findings and draft recommendations, and address the request for information.

Water use in the Murray-Darling Basin

Draft Finding 2.1

Current planning arrangements tend to assign a more than proportional cut to environmental water during dry periods. With climate change expected to increase the prevalence of dry conditions (particularly in the southern Basin), the environmental consequences of this could become increasingly significant. Accordingly, the prospect of climate change adds to the imperative to reconsider the balance between environmental and consumptive uses of water.

This finding runs the risk of being a dangerous generalisation that could lead to the wrong impression being given in public forums.

The Gwydir Valley Regulated River water sharing plan has been publicly acknowledged by both the CSIRO and the Murray-Darling Basin Authority, among others, of equitably sharing available water between extractive users and the environment, regardless of the level of available water resource.

This demonstrates that water sharing instruments can be designed in a manner that treats both the environment and extractors equitably. It is just about making sure the policy instruments are well designed.

G VIA requests that Productivity Commission amends this draft finding so that it clearly acknowledges that not all water sharing policy instruments favour extractors during drier periods.

Development of water markets

Draft Finding 3.1

Water markets are well developed and active in the southern-connected Basin, but not in parts of the northern Basin. This has implications for the buyback — market-based water recovery is more difficult where markets are not well developed.

Like the previous draft finding, this one also runs the risk of being a dangerous generalisation. In the Gwydir Valley, and the other regulated river valleys of northern NSW there is a well developed water market.

It would be true to say that the volumes of trade, both in terms of megalitres and transactions are not large, but that is more a reflection of the size of the available pool, and the limited physical connectivity across river systems.

Trade in unregulated entitlement and allocation is under-developed, but is underdeveloped in both the northern and southern parts of the Basin.

Groundwater trade in valleys with water sharing plans, including the Gwydir, is also well developed.

G VIA recommends that the report reflect that market underdevelopment be identified has primarily an issue associated with unregulated water, rather than a north-south issue.

Draft Finding 3.2

Market intermediaries, including brokers and exchanges, have developed alongside the market to facilitate increased trade, with lower transaction costs.

GVIA would agree with this finding, but suggests there is still further room for market intermediaries involvement, with the aim of making market transactions more efficient.

Allocating environmental water

Draft Finding 4.1

Water recovered in the northern Basin will usually result in limited environmental benefit for the southern parts of the Basin, given hydrological constraints. Water recovery within the northern catchments that are effectively disconnected should be driven primarily by environmental priorities within those catchments. Conversely, the southern Basin — including the Murrumbidgee, the Murray and the Goulburn rivers — is highly interconnected, allowing considerable flexibility in sourcing and delivering water for environmental purposes.

GVIA would agree with this position, but notes that considerable work needs to be done in identifying the true environmental water requirements of the northern catchments.

Draft Finding 4.2

Decisions on allocating water between competing uses in the Basin should be based on good science. But this is not a sufficient basis for achieving the best outcome for the community. Community preferences should be considered where tradeoffs are required between different environmental outcomes, and between environmental and consumptive outcomes.

GVIA agrees with this finding, and notes its great concern with the Federal Water Act which appears to place environmental outcomes above all social and economic considerations. GVIA would argue that this would have to be one of the first times in human history where a planning process has not allowed for trade-offs between environmental, social and economic needs.

Recovering water through non-market means

Draft Finding 6.1

Under the Water Act 2007 (Cwlth), the Murray-Darling Basin Authority is required to determine environmental watering needs based on scientific information and to consider least cost ways of meeting these needs in setting sustainable diversion limits. This way of allocating water between environmental and consumptive uses does not take into account community preferences, the opportunity cost of water or the role of other inputs such as land management. As the sustainable diversion limits will be used to guide future water purchasing under Restoring the Balance, the effectiveness and efficiency of this program are likely to be compromised.

GVIA would agree with the finding, and is very concerned about the absolute focus on water volumes, rather than addressing environmental needs through a whole suite of mechanisms including improved land management.

GVIA argues that water volumes for environmental outcomes should be set based on the premise that best land and management practices are in place. For example, if poor land use is the cause of salinity problem, water volumes should not be set at a level that would effectively dilute the salinity; they should be set a level that would ensure suitable quality water, if land use practices were optimized.

Draft Finding 6.2

Considerable uncertainty exists about the application of the risk assignment provisions set out in the National Water Initiative, as amended by the Water Act 2007 (Cwlth), in respect of compensation that might be payable to irrigators upon the implementation of the Basin Plan. This is impeding the ability of irrigators to plan for the future and is affecting the efficient conduct of the buyback.

GVIA agrees that there is considerable uncertainty surrounding the application of the risk assignment provisions, and this does impact on the ability of water entitlement holders to make sound decisions in regards to planning for the future.

However, GVIA believes while the risk assignment provisions were relevant in the social and political environment of 2004, they should be deemed to be irrelevant today.

All Australian governments have now recognised the equity of paying for water entitlements, and that same recognition should apply when water entitlement holder's access is reduced by government policy change.

In summary, whether water is secured for the environment through entitlements purchase (currently fully compensated) or by policy induced adjustment to entitlement (currently subject to the risk assignment provisions), the entitlement holder should be fully compensated at the market rate.

Currently there is a real inequity where entitlement holders who choose to sell to the government are fully compensated (which is right), while those who maybe subjected to reliability changes face the uncertainty and inequity of the risk assignment provisions.

Draft Recommendation 6.1

All Basin jurisdictions should clarify how the risk assignment provisions set out in the National Water Initiative, as amended in the Water Act 2007 (Cwlth), will apply to the reductions in water availability that are likely under the Basin Plan. This should occur as soon as possible.

GVIA would recommend that the Commission change this recommendation, calling for a review of the risk assignment provisions, so that they fully compensate irrigation entitlement holders if their reliability is impacted by any policy change, regardless of the driver for the policy change.

Draft Finding 6.3

Purchasing water products from willing sellers is generally the most effective and efficient means of acquiring water, where governments are liable for the cost of recovering water for the environment.

GVIA strongly supports the right of the Commonwealth, and indeed anyone, to purchase water from willing sellers at the market price, and equally opposes any form of compulsory acquisition; including by way of loss of reliability as a result of policy and planning instrument changes. However, GVIA also see a role for a range of water efficiency programmes that share “savings” between entitlement holders and government.

Draft Finding 6.4

Funding infrastructure upgrades is generally not a cost-effective way for governments to recover water for the environment. It is also unlikely to be an effective or efficient means of sustaining irrigation communities.

As stated above GVIA does see a legitimate role for irrigation infrastructure upgrade programmes that recover water for the environment, as part of a suite of alternatives available to government.

GVIA concedes that if government was only interested in obtaining water entitlement at the lowest cost per megalitre, then upgrade programmes would not be desirable.

However, government needs to look at the total environmental, economic and social health of its communities, and then in some instances paying a higher price than the strict market price, would provide greater and ongoing returns into the future.

For example a government may purchase 1000 megalitres on the open market, and this water is no longer available for productive extractive use. The seller has been fully compensated by the market price, but in the past that 1000 megalitres has supported two on farm jobs, and six more jobs in town, and result in five children attending the local school, and the hospital having a big enough patient base to support a full time surgeon. With the 1000 megalitres sold, that productive flow-on is lost, and government will have to increase its support for that community, or allow it to suffer uncompensated.

However, if government invested in an infrastructure programme that created 1000 megalitres of savings (at lets say twice the market price), and dedicated those savings to the environment, a true win-win situation exists, with the environment receiving its water with no net cost to the community.

GVIA does believe that financial discipline must be applied to these sorts of projects, but in making a decision governments must account not just for the straight financial cost per megalitre of securing entitlement, but also the ongoing social and economic costs to a community of transferring water from extractive use to environmental use.

Draft Recommendation 6.2

Rigorous approval processes should be applied to all projects under the Sustainable Rural Water Use and Infrastructure program. In particular, projects should generally only be approved where the cost per megalitre for water entitlements recovered is similar to the market price. Premiums above this price should only be paid in exceptional circumstances.

Irrigators in the Gwydir Valley are able to access on-farm irrigation efficiency funding through the federally funded NSW Priority Project – NSW Sustaining the Basin – Gwydir Valley Project.

GVIA is supportive of a rigorous assessment and approval process, but as discussed in the previous response strongly argues that there is justification for approving projects that do have costs-per-megalitre higher than the market price.

GVIA believes project application should be competitive in nature, and that government will naturally favour those applications with lower per megalitre costs, but it also must be recognised that on-farm irrigation efficiency projects have to offer a premium if they are to have any attraction to irrigators.

It is clear that a price equal or less than the market price will attract no takers. Efficiency programmes will only be attractive if there is a market premium, but that “premium” is not a windfall to the irrigator, as he/she must undertake works; it is in effect an investment in the regional economy.

Portfolio of water products

Draft Finding 7.1

Purchasing unregulated water entitlements can provide environmental managers with different environmental watering possibilities to holding storage-backed entitlements. Although less reliable, holding unregulated entitlements can help managers to restore natural flows in river systems. However, their effectiveness and efficiency can be compromised by complexities involved in shepherding environmental water downstream. These third-party effects may need to be addressed through negotiating with groups of irrigators, or through administrative changes to environmental flow rules.

GVIA supports the finding.

Draft Recommendation 7.1

The Australian Government should adopt a portfolio approach to purchasing water products, and not focus solely on water entitlements. Other products, such as seasonal allocations, leases on entitlements, options contracts and contracts for environmental services, have advantages in specific contexts and should be considered.

GVIA supports this recommendation, and adds that the NSW Supplementary Water entitlement product is an ideal product for environmental managers looking to restore the natural pattern of river flow events.

Mechanics of the buyback

Draft Finding 8.1

Where active markets for water entitlements exist, acquiring water entitlements directly from those markets is likely to be more efficient than utilising alternative purchase mechanisms.

GVIA would be supportive of the government operating directly in the market, provided there was timely disclosure of market price. GVIA is very concerned that at the moment public reporting of price only occurs when the dealing is shown on the NSW Water Register, which often can be many months after the sale is agreed on.

Timely price disclosure is absolutely critical when there is a dominant buyer operating.

GVIA would be supportive of a low-cost mechanism that ensured price reporting within 72 hours of contract exchange.

Draft Finding 8.2

Allowing irrigators to bid several combinations of entitlements and prices as part of a single bid could improve the efficiency of the tender.

GVIA is supportive of this finding.

Draft Finding 8.3

The effectiveness and efficiency of the tender process would be improved by making the offers to sell binding on potential sellers.

GVIA believes there are some advantages to having non-binding offers. It allows a degree of negotiation to occur between buyers and sellers. This can in fact lead to some time saving and efficiency if there is only limited gap between buyer and seller price expectations.

Draft Finding 8.4

The efficiency of the conveyancing process could be improved by:

- *exchanging the contracts of sale before the due diligence process commences*
- *assessing the current due diligence process for potential duplication with current state approval processes and removing the sources of duplication*
- *introducing a formal requirement on the Department of the Environment, Water, Heritage and the Arts to notify tender participants of any delays in the process and the reasons for the delays.*

GVIA is supportive of this finding.

Draft Finding 8.5

Using the buyback to address indirect objectives, such as achieving distributional goals, system rationalisation, and reducing the salinity impacts of water use is likely to compromise its effectiveness and efficiency. Other more direct instruments would generally achieve those objectives at lower cost.

GVIA is strongly supportive of this position, but this does not extend to being supportive of “buyback”, instead of irrigation efficiency infrastructure upgrade, when it is clear that pursuit of “buyback” will result in significant economic and social consequences to a community.

Governance and institutional issues

Draft Finding 9.1

Transparency in environmental water recovery by the Commonwealth would be improved by providing clear and public information summarising the existing and planned holdings of environmental water across the Basin, and explicitly explaining how Commonwealth water recovery is being coordinated between the two Commonwealth water recovery programs (Restoring the Balance and Sustainable Rural Water Use and Infrastructure), and with other environmental water holdings.

One of the great frustrations of the environmental water recovery programme is the lack of any real information on water requirements, and therefore recovery targets. While GVIA has some sympathy for the government's "no-regrets" approach, it does believe that government should be prepared to publish its "no-regrets" targets and the reasoning behind their establishment.

GVIA is very concerned that government will "over-acquire" water entitlement, and this may in effect result in "environmental water requirements" being set at an unnecessary high level, rather than have government admit that it had over acquired.

GVIA believes it is essential that the Commonwealth Environmental Water Holder immediately releases its current environmental water targets, and that the Murray-Darling Basin Authority release its list of environmental sites and water requirements as-soon-as-possible, and certainly prior to the development of the proposed basin plan.

Draft Finding 9.2

Current governance arrangements for the management of environmental water in the Basin are fragmented between various state and local environmental water managers and the Commonwealth Environmental Water Holder. Governance arrangements for coordinating environmental watering activities are unclear.

GVIA strongly endorses this finding, and is very concerned that the current management arrangements are inefficient and will not lead to the best environmental outcomes. As a case in point, in the Gwydir Valley there is a 45,000 megalitre Environmental Contingency Allowance (ECA), approximately 17,000 megalitres of adaptive environmental water controlled by the NSW Department of Environment, Climate Change and Water (DECC&W), and approximately 90,000 megalitres (general security & supplementary) of Commonwealth owned adaptive environmental water entitlement.

The Gwydir has a long established ECA Advisory Committee, that makes recommendations on the management of the ECA and DECC&W water, while the Commonwealth is developing a parallel system.

The Commonwealth does have observer status on the ECA committee, and has indicated a willingness to work with the committee, but at the same time is maintaining its independence, but it does not possess the on-ground local management expertise that the ECA committee has.

GVIA would recommend that the CEWH assign the management of its Gwydir environmental water to the ECA committee. The ECA committee would have to produce an annual plan (which it does) and the CEWH could then assess that plan, and if consistent with the aims of the CEWH, then the sensible and efficient thing to do, would be to hand over the management of the Commonwealth water to the ECA committee. The committee could then report back the outcomes to the CEWH, and provided the results were consistent with the annual plan expectations, the arrangement could continue.

Draft Finding 9.3

Recovering water is necessary in most cases, but is not always sufficient to achieve desired environmental outcomes in the Basin. Other inputs, such as capital works to manage and direct environmental flows, and changes to land management practices, may also be required. Yet the focus of the Basin Plan, and the Australian

Government's buyback and infrastructure programs is solely on recovering water, without regard for the role of these other inputs. Better systems are needed to coordinate the mix of water purchases with other actions and inputs to achieve the desired environmental results.

GVIA strongly supports this finding, and is very frustrated by the almost total focus on water volumes. For example, it is well known, that if a desired environmental outcome is increased fish numbers, increased flow in the absence of habitat restoration eg re-snagging, or effective management of cold-water pollution risks will achieve little or nothing.

GVIA believes it is essential that environmental water requirements are assessed on the basis of other best management practices being in place.

For example, GVIA would be completely opposed to salinity dilution flows being set at a level to mitigate salinity issues in an environment where there had been large scale and inappropriate land clearing, which has caused the high levels of salinity.

If required at all, dilution flows should be at a level to manage background salinity levels, and other environmental remediation works need to be put in place to rectify the high salinity inflows into the system.

Request for Information

Based on good governance principles, what do you think are the appropriate institutional structures for:

- conducting the purchase of entitlements under the Restoring the Balance program*
- purchasing the suite of water products that the Commonwealth Environmental Water Holder will need, to meet varying environmental demands in the interim before the Basin Plan takes effect*
- purchasing environmental outcomes through new programs aimed separately at private providers and public environmental managers?*

What do you think the role of the Commonwealth Environmental Water Holder should be in holding and trading in water products once the Basin Plan has been fully implemented?

GVIA is not opposed to the CEWH being the primary manager of sourcing and utilising the Commonwealth's environmental water holdings.

However, where there are mature and efficient environmental water managers in place (such as the Gwydir ECA Advisory Committee, then the CEWH should delegate the management of its water resources to that committee, rather than trying to replicate a management system.

It is clear from the Gwydir experience that effective management requires local management, back by local knowledge and experience. It will be impossible to effectively managed environmental water for the Gwydir, from Canberra. As one GVIA member likes to say – “Centralised economies have failed, and so will centralised ecologies.”

GVIA does not understand why there is, or needs to be a separation, between the Commonwealth Water Purchasing group and the CEWH, and suggests there may be efficiencies in merging these two entities. However, GVIA has observed a high level of co-operation between these two bodies.

GVIA believes there may be some merit of bringing the work of the CEWHA into the Murray-Darling Basin Authority to assist with better integration of environmental watering, with the basin plan.

Overcoming impediments

Draft Finding 10.1

Restrictions on water trade in Victoria and New South Wales have the potential to impair the effectiveness and efficiency of the buyback

- Victoria's agreement to allow some exemptions to a 4 per cent limit on out-of-area trade of water entitlements is an improvement but because the extra purchases can only occur from specified areas, the constraints are still distortionary and decrease the cost effectiveness of the buyback*
- New South Wales' agreement to lift a blanket embargo on sales to the Commonwealth and replace this with annual volumetric caps is less distortionary than the Victorian restrictions, but it does limit options for conducting a faster buyback should this be deemed necessary.*

While the issues raised in the above draft findings are not major issues for Gwydir Valley irrigators, GVIA is supportive of a much more level playing field when it comes to interstate trading.

Draft Recommendation 10.1

The 4 per cent limit on out-of-area trade of water entitlements should be eliminated as soon as possible, rather than phased out by 2014 as currently scheduled. Limits on the amount of entitlements that can be sold to the Commonwealth through the buyback should also be eliminated.

GVIA is supportive of this recommendation.

Draft Finding 10.2

Moving to cost-reflective pricing for water delivery is likely to improve the efficiency of water trading. Irrigation infrastructure operators that implement this reform will reduce the risk that geographically dispersed sales into the buyback could harm the competitiveness of their irrigation area.

GVIA is not convinced that cost reflective pricing will have any significant impact on water trade, one way or the other. However, GVIA is very concerned that the wholesale pursuit of "full-cost recovery" by some jurisdictions is significantly eroding the profitability and therefore sustainability of irrigation farming.

Draft Recommendation 10.2

The Murray-Darling Basin Authority should commission an independent study into ways of expanding the ability of water users to carry over water, while adequately managing third-party impacts. This study should consider options that treat environmental entitlements and consumptive use entitlements the same and options that treat them differently.

GVIA would support the first part of the recommendation, and suggests the study looks at the continuous accounting system that operates in NSW as a positive model.

GVIA would be opposed to any move that changes the characteristic of water entitlements that were purchased for environmental use.

Submission ends