



Australian
Competition &
Consumer
Commission

Water market rules issues paper

April 2008



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Submissions should be provided to the ACCC by no later than **Friday, 9 May 2008**.

Although every submission is welcome, multiple identical submissions do not carry any more weight than the merits of an argument in a single submission.

When making a submission, please title your document, 'Public submission to water market rules issues paper by [INSERT NAME] on [INSERT DATE]'.

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Water Branch
Water market rules—issues paper
Australian Competition and Consumer Commission
GPO Box 520
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General inquiries may be directed to the ACCC Infocentre on 1300 302 502 or to water@acc.gov.au.

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Abbreviations

ACCC	Australian Competition and Consumer Commission
ACT	Australian Capital Territory
ATO	Australian Taxation Office
COAG	Council of Australian Governments
DWLBC	Department of Water Land and Biodiversity Conservation (SA)
DWE	Department of Water and Energy (NSW)
MDB	Murray-Darling Basin
MDBA	Murray-Darling Basin Agreement
MDB Authority	Murray-Darling Basin Authority
NICWER	National Irrigation Corporations Water Entitlement Register
NRMA	<i>Natural Resources Management Act 2004 (SA)</i>
NRW	Natural Resources and Water, Department of (Qld)
NSW	New South Wales
NWI	National Water Initiative
Qld	Queensland
ROP	Resource Operations Plan
SA	South Australia
the Act	<i>Water Act 2007 (Cwlth)</i>
Vic	Victoria
WAR	water allocations register
WAL	water access licence
WIRO	Water Industry Regulatory Order

Glossary

This glossary endeavours to provide practical meanings of terms; however, readers may need to consider the legal meaning of some terms under the *Water Act 2007* (Cwlth) and obtain legal advice on these definitions, if required.

externality	an externality is the effect of a purchase or use decision by one party that imposes costs or benefits on another party that are not reflected in the market price
exit fee	a fee levied by an irrigation infrastructure operator on the transfer of a water entitlement out of the operator's network or irrigation district (excluding any fee associated with the costs of processing that transfer)
irrigator	a person who receives water delivery services from an irrigation infrastructure operator. This may include a person who receives water for any purpose, such as for stock and domestic
irrigation right	a right that a person has against an irrigation infrastructure operator to receive water, that is not a water access right or a water delivery right
irrigation infrastructure operator	any person or entity who owns or operates infrastructure for the purpose of delivering irrigation water to another person (e.g. an irrigator)
irrigation district	an area or district that is supplied with water via an infrastructure supply network, (channels, pipes and other structures) operated and maintained primarily to supply water for use within that district
regulated water charge	charge to which the water charge rules (Division 1 of Part 4 of the <i>Water Act 2007</i>) apply. This includes fees and charges payable to an irrigation infrastructure operator for access to, or terminating access to, the operator's network
transformation arrangement	process by which an irrigator permanently transforms their entitlement to water under an irrigation right against an irrigation infrastructure operator into a water access entitlement held by the irrigator (or anybody else), thereby reducing the share component of the operator's water access entitlement
water access right	any right conferred by or under a law of a state to hold water from a water resource or to take water from a water resource. This includes stock and domestic rights, riparian rights, a water access entitlement, a water allocation and any other

	right relating to the taking or use of water
water access entitlement	open-ended or perpetual access to a share of the water resource that is available for consumption as specified in a water plan
water allocation	the specific volume of water allocated to a water access entitlement in a given season, defined according to rules established in the relevant water plan
water delivery right	a right to have water delivered by an infrastructure operator

1 Introduction

The Murray-Darling Basin (MDB) extends across five states and territories and is Australia's most important agricultural region (see appendix A).

The *Water Act 2007* creates new institutional and governance arrangements to address the sustainability and management of water resources in the MDB. The Act builds on earlier reform initiatives, including the National Water Initiative (NWI)¹ and the Murray-Darling Basin Agreement (MDBA).

The Act, which came into effect on 3 March 2008, creates new functions for the Australian Competition and Consumer Commission (ACCC). These include developing draft water market rules and water charge rules for consideration by the relevant Minister, and advising the new MDB Authority on water trading rules (see appendix B). The Act also requires the ACCC to monitor compliance with, and enforce², the water market rules and water charge rules.

The Minister for Climate Change and Water, Senator Penny Wong, has written to the ACCC requesting advice on water market rules by August 2008.

The ACCC has also been requested to provide advice relating to water charge rules by January 2009. The development of rules relating to bulk water charges, charges of irrigation infrastructure operators and charges levied to recover the costs of water planning and management will be managed through separate consultation processes and are not the subject of this issues paper.

One of the main objectives of the NWI and the Act is to facilitate the operation of efficient water markets and the opportunities for water trading. The water market rules will contribute to this objective by ensuring that the policies and administrative requirements of operators of irrigation infrastructure do not represent a barrier to trade (see Chapter 2). In other words, the water market rules will ensure that the water rights of irrigators are, in fact, tradeable.

The water market rules must contribute to achieving the Basin water market and trading objectives and principles (see Chapter 3).

In developing its advice, the ACCC will consider what restrictions imposed by operators should be permitted (see Chapter 4) and whether operators should be required to undertake certain actions (see Chapter 5).

¹ The Intergovernmental Agreement on the National Water Initiative between the Commonwealth of Australia and the Governments of New South Wales, Victoria, Queensland, South Australia, Western Australia, the Australian Capital Territory, and the Northern Territory (as amended from time to time). The NWI (2004) built on the 'Water Reform Framework' agreed by the Council of Australian Governments in 1994, which was incorporated within the National Competition Policy Agreement in 1995.

² Part 8 of the Act provides the ACCC with a suite of mechanisms to enforce water market rules and water charge rules.

The financial implications of water market rules (see Chapter 6) and other matters associated with the application and implementation of these rules will also be considered (see Chapter 7).

1.1 Consultation process

Consultation with stakeholders is an important part of the ACCC's process in developing its advice to the Minister. This issues paper begins that consultation process by seeking submissions from stakeholders, including:

- MDB jurisdictional governments
- irrigation infrastructure operators
- irrigators and other water users
- water market intermediaries
- other interested parties.

The ACCC welcomes submissions on issues raised in this paper as well as any other relevant information that could assist and inform its advice to the Minister. Where submissions address one or more of the specific questions in this paper, the relevant question number(s) should be noted.

Given the timeframe for the ACCC to develop its advice on water market rules, submissions need to be provided to the ACCC no later than **Friday 9 May 2008**.

There will be further opportunities to inform the ACCC's development of water market rules before the preparation of final advice to the Minister. Specifically, the ACCC proposes to release a draft of its advice in mid-2008 for further consultation.

1.2 Treatment of confidential information

The ACCC prefers that all written submissions be publicly available to foster an informed, robust and consultative process. Accordingly, submissions will be considered to be public and will be posted on the ACCC's website unless confidentiality is sought and obtained from the ACCC.

Any information that parties would like to request the ACCC not make publicly available should be provided in a separate document and clearly marked 'Confidential' on every page. Reasons must be provided to support the request for confidentiality.

The ACCC will only accept a claim of confidentiality if the information is truly confidential in nature. Grounds on which confidentiality could be claimed include that the information disclosed is commercial in confidence and/or is non-public information.

The ACCC will not accede to a request for confidentiality if it would not be in the public interest to do so. If the ACCC considers the information should be disclosed (either because it is not confidential or because it would not be in the public interest to receive the information without public disclosure), the ACCC will provide the parties with an opportunity to withdraw the submission (or part of the submission) containing the information. If the submission (or part of the submission) is withdrawn, the ACCC may not take it into account. If a party elects not to withdraw the submission (or part of the submission) the ACCC may disclose the information publicly.

Any information accepted as confidential by the ACCC will not be publicly released by the ACCC, except where required as part of the provision of advice to the Minister or where required by law (e.g. in response to a request under the *Freedom of Information Act 1982* or a subpoena regarding proceedings between third parties).

2 Water market rules

2.1 What is the purpose of water market rules?

The Water Bill 2007 Explanatory Memorandum states that the purpose of the water market rules is to:

free up the trade of water access rights within the Murray-Darling Basin by ensuring that the policies or administrative requirements of [irrigation] infrastructure operators do not represent a barrier to trade.³

Broadly speaking, an **irrigation infrastructure operator** ('operator') is any person⁴ who owns or operates infrastructure for the purpose of delivering irrigation water to another person (i.e. an irrigator or other water user).⁵ The Act does not distinguish between operators on the basis of the size of the irrigation network, the number of irrigators serviced⁶, or the volume of water rights held by the operator or their customers. Similarly, the definition of an irrigation infrastructure operator is not related to the operator's governance structure.

Although many operators, particularly in South Australia and New South Wales, are owned by member irrigators, the operators have a separate legal status to their members. Water market rules are likely to apply to operators regardless of their governance arrangements (i.e. whether they are established as trusts, corporations, associations or cooperatives).

In most cases, these operators own a 'group' **water access entitlement**⁷ and the member irrigators have a right to a share of water under an **irrigation right**⁸ against the operator (as conferred through their supply agreement). Further details of the governance arrangements of operators in the MDB and their arrangements with their customers and members are contained in appendix C.

Transformation arrangements are those that allow a member irrigator to permanently transform their entitlement to water under an irrigation right against an operator into an independently held water access entitlement, thereby reducing the share component of the operator's water access entitlement (see figure1).

³ Explanatory memorandum to the Water Bill 2007, clause 97, paragraph 190, p. 28.

⁴ 'Person' includes a body politic or corporate as well as an individual.

⁵ Water Act, s. 7(4).

⁶ For the purposes of this paper, an irrigator includes any person who receives water delivery services from an irrigation infrastructure operator. This may include a person who receives water for any purpose, such as for stock and domestic.

⁷ For example, a 'water share' in Victoria, a 'water access licence' in New South Wales, a 'water taking/holding allocation' in South Australia, and a 'water allocation' in Queensland.

⁸ Water Act, s. 7(4).

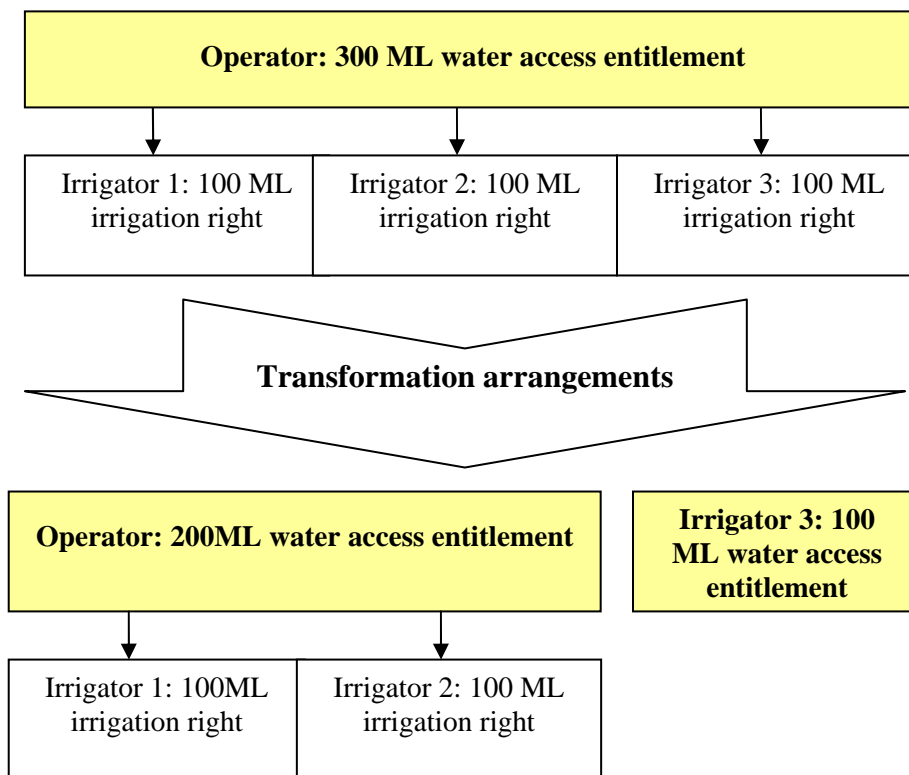
Such a transformation arrangement is a necessary first step if an individual wishes to permanently trade their share of a group entitlement to anybody other than another group member. However, they may also simply prefer to hold an individual water access entitlement because they consider that it is of greater value than an entitlement to water under an irrigation right. For example, an individual entitlement may provide greater access to finance (see section 6.1).

In the absence of a legal requirement to act otherwise, an operator, as the owner of the group water access entitlement, can unilaterally prevent or delay any member from transforming their ‘share’ of the group entitlement into a separate water access entitlement.

Figure 1: transformation arrangements

Suppose that an operator owns a water access entitlement of 300ML and that the operator supplies three member irrigators who each have an irrigation right of 100ML.

The effect of one irrigator (Irrigator 3) choosing to transform their irrigation right into an individual water access entitlement is illustrated below.*



* This example does not account for any conversion factors or other adjustments that may be applied to the transformation of an irrigation right into a water access entitlement.

2.2 What can water market rules cover?

Water market rules may relate to an act that an operator does, or fails to do, in a way that prevents or unreasonably delays transformation arrangements being made.⁹

This includes the restrictions that an operator may, or may not, impose in relation to the trading or transferring (by a person who had an irrigation right against the operator) of a water access entitlement obtained as a result of transformation arrangements.¹⁰

For simplicity, this paper will refer to conduct by operators of the type discussed above as restrictions on ‘transformation and/or trade’.

The types of restrictions on transformation and/or trade that the water market rules may deal with include restrictions imposed by the inclusion of provisions in a contract, arrangement or understanding between an operator and a person who has:

- an irrigation right against that operator; or
- a water access entitlement obtained from transforming an irrigation right that the person had against the operator.

The Act specifically identifies two actions of an operator that the water market rules **cannot** prohibit. These are where the operator:

- imposes, or requires the payment of, a **regulated water charge**¹¹; or
- requires the approval of a person who holds a legal or equitable interest in an irrigation right that a person has against the operator before allowing transformation arrangements in relation to that irrigation right.¹²

The Act also identifies that the water market rules may permit an operator to require security before allowing:

- a person who holds an irrigation right against an operator to obtain a water access entitlement through transformation arrangements; or
- a person who has obtained a water access entitlement as a result of a transformation arrangement to trade or transfer that entitlement.¹³

In developing the market rules, the ACCC will consider the extent to which the rules should allow operators to require security in these circumstances.

⁹ Water Act, s. 97(1).

¹⁰ Water Act, s. 97(3)(b).

¹¹ Water Act, s. 91.

¹² Water Act, s. 97(6).

¹³ Water Act, s. 97(5)(a).

The water market rules may also provide for transitional arrangements relating to contracts entered into between an operator and another person before water market rules are made or amended.¹⁴

In developing advice on water market rules, the ACCC intends to consider:

- What actions undertaken by an operator that prevent or delay transformation and/or trade should be permitted under the water market rules?
- What actions should an operator be required to undertake so as to not prevent or unreasonably delay transformation and/or trade?

The legislative arrangements that exist in each MDB jurisdiction may be relevant to the policies, rules and actions of operators; in particular, arrangements that relate to water trading processes, approvals and administration.

The legislative nature of water rights and extent to which these rights are unbundled may also affect the market arrangements of operators. For example, the Murray-Darling Basin Agreement—*Schedule E Protocol, access, exit and termination fees* requires that water rights are to be unbundled from delivery rights by 30 June 2010.

The current legislative arrangements of the different jurisdictions are discussed further in appendix D.

¹⁴ Water Act, s. 97(5)(b).

3 Water market and trading objectives

The water market rules must contribute to achieving the *Basin water market and trading objectives and principles* as set out in Schedule 3 to the Act. These objectives are:

- (a) to facilitate the operation of efficient water markets and the opportunities for trading, within and between Basin States, where water resources are physically shared or hydrological connections and water supply considerations will permit water trading; and
- (b) to minimise transaction cost on water trades, including through good information flows in the market and compatible entitlement, registry, regulatory and other arrangements across jurisdictions; and
- (c) to enable the appropriate mix of water products to develop based on water access entitlements which can be traded either in whole or part, and either temporarily or permanently, or through lease arrangements or other trading options that may evolve over time; and
- (d) to recognise and protect the needs of the environment; and
- (e) to provide appropriate protection of third-party interests.

This chapter discusses these objectives in greater detail. The principles are contained in appendix E.

3.1 Facilitate efficient water markets

An efficient, well functioning water market can reveal the value of water to existing and potential users. Water trade creates incentives for users to seek improved technical productivity, innovate and improve water use efficiency. This leads to more productive and efficient use of water resources over time.¹⁵

Markets are quicker in reallocating water in response to changes in the availability and demand for water than the traditional methods of allocation. Removing impediments and restrictions that may be imposed by operators helps to ensure that this reallocation occurs at a lower cost.

Many restrictions imposed by operators could constitute trade barriers. Barriers to water trade can result in a thinner market than might otherwise exist, distort the decisions of market participants, dampen signals for necessary investment and long-term structural adjustment and result in a reduction in the gains from trade (that may otherwise have been realised).

¹⁵ National Water Commission, *2005 NCP Assessment follow-up assessment of water reform progress*, p. 1.2, 2006.

Efficient markets are characterised by, among other things:

- a multitude of buyers and sellers
- well informed decision making on the part of market participants
- market participants taking account of all the costs and benefits generated by their actions (i.e. any externalities are internalised)
- low barriers to entry
- low transaction costs
- few impediments to trade
- well defined property rights.

These characteristics help to ensure that any opportunities for beneficial trades are fully realised, thereby facilitating the optimal allocation of resources. Facilitating the operation of efficient water markets involves ensuring that the elements that characterise efficient markets are present.

3.2 Minimise transaction costs

High transaction costs can act as an impediment to a well functioning water market by discouraging otherwise beneficial trades from occurring.

Some typical transaction costs in water markets include costs associated with obtaining market information, seeking and obtaining transformation and/or trade approval, and negotiating and enforcing contracts.

It is important that market participants have timely and relevant information on prices, the availability of water and market processes. Where the cost of obtaining such information is excessive, this can hinder the efficient operation of the market.

However, to encourage appropriate market behaviour and limit market failures, it may be necessary to impose transaction costs on market participants. These may relate to costs associated with the implementation and operation of trade approval processes and water accounting systems. While these processes may be necessary and even desirable features of the market's operation, these mechanisms should be designed with regard to minimising the costs of implementation, to minimise any associated transaction costs.

Institutional features of the market's design may also reduce transaction costs. For example, an adequate and accessible register of titles and record of transfers helps to reduce transaction costs by facilitating the enforcement of property rights and informing market participants.

3.3 Enable a mix of water products to develop

An increase in the choice of water products available can deepen the water market by generating more buyers and sellers; it can also provide increased flexibility to water users. Water products could include water access entitlements, water allocations, leases and option contracts.¹⁶

For example, given the variability in water availability in Australia and that some irrigators need long-term access to secure supplies of water because of their cropping choices, these irrigators may wish to own water entitlements rather than rely on trading in allocations. On the other hand, some irrigators with annual crops may prefer to trade allocations, taking advantage of times when water is less expensive and more readily available.

3.4 Recognise and protect the needs of the environment

Where environmental externalities are present, water markets may not result in the most efficient outcomes. Externalities occur where a market decision by one party imposes costs or benefits on another party that are not reflected in the market price.

Water provided for the environment is a public good¹⁷. As a result, the benefits generated cannot be confined to those willing to pay for its provision, which can lead to the under-provision of water for the environment (i.e. too much water is allocated to consumptive uses and too little to the environment).

To increase the efficiency of water markets, these issues (associated with externalities and the public good characteristics of water) need to be addressed. A possible solution is for trading to be restricted in situations where it may result in negative environmental outcomes or for governments to secure and manage water access entitlements for environmental purposes. Alternatively, it may be possible for property right regimes to be specified more precisely to manage these externalities.

3.5 Provide appropriate protection of third parties

While water trading can increase net social benefits, there may be parties within irrigation communities who may be negatively impacted. For example, irrigation networks typically involve large initial capital outlays and predominantly fixed recurrent operating and maintenance costs. For the most part these costs are common to all network users. As a result, when an irrigator reduces their use of the network (possibly in association with the trade of their water right), there may be little, if any,

¹⁶ An options contract is a contract that gives the right, but not the obligation, to purchase or sell a product at a specified price within a period of time.

¹⁷ A good that is non-rival and non-excludable, such that the consumption of the good by one individual does not reduce the amount of the good available for consumption by others and the benefits generated from the good cannot be confined to those who are willing to pay for the provision of this good.

avoided cost from the perspective of the operator and therefore these fixed, common costs must be shared by the remaining network users.

Water trading can also lead to structural adjustments such as contraction in the demand for complementary agricultural services and output from districts. This may result in changes to the demographics and population of some communities.

A range of tools and policies can be used to provide appropriate protection of third party interests.

Question 3:	Are there any other factors that the ACCC should consider when interpreting the water market and trading objectives?
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4 Restrictions that should be permitted

Currently a range of practices are carried out by operators that prevent or delay transformation and/or trade. These restrictions may be contained in the constitutions or operating charters of operators, supply contracts with irrigators, or they may not be documented. Any restriction imposed by operators is likely to reduce trade, and may lead to inefficient market outcomes. However, in some cases, these restrictions might be imposed for operational reasons or to comply with state legislative requirements if the operator is also an approval authority.

Some common restrictions that may prevent or unreasonably delay transformation and/or trade include:

- constraints on the parties to whom water can be sold
- constraints on water exports
- other constraints on trade and transformation
- security requirements for future fee payments
- administration fees and charges
- cut-off dates and trading seasons.

In developing the water market rules, the ACCC will consider what restrictions imposed by operators that may prevent or delay transformation and/or trade should be permitted.¹⁸

4.1 Constraints on the parties to whom water can be sold

Restrictions imposed by operators on the parties to whom water can be sold predominantly relate to the following:

- restrictions based on the possible use of traded water (e.g. land use assessment requirements)
- restrictions on water sales to non-landholders/non-water users (e.g. landholder requirements or restrictions on sales to an environmental water purchaser).

Restrictions on the basis of the possible use of water can take the form of specified water-holding limits or requirements for land use assessments as part of an application to trade.

The exact form and wording of these restrictions varies. One form of restriction is the assessment of trade applications against the possible adverse impacts associated with

¹⁸ As discussed in chapter 2, the Act specifically identifies two actions of an operator that the water market rules cannot prohibit.

the use of the water resulting from the trade. Another restriction may take the form of placing the onus of proof on the trade applicant to assess the impacts, through preparation of various assessments.

The rationale behind land use assessment requirements may relate to managing the on-site impacts of irrigation, such as salinity, by preventing unsustainable irrigation techniques. These arrangements may be associated with the jurisdictional government's policies or the licence conditions imposed on the operator. In many cases operators may undertake these actions as part of their role as the designated trade approval authority.

In jurisdictions where there is no process to approve water use separate to trade, consent for use of water on land is often triggered upon application for the transfer of a water entitlement. Where these assessments are completed as part of an application to transform and/or trade, they would present a barrier to water trade. Clause 30 of the NWI notes that regulatory approvals enabling water use at a particular site, for a particular purpose should be specified separately to the water access entitlement, consistent with the principles set out in Schedule D of the NWI.

This approach recognises that linking water use approvals with the ownership of water access entitlements may not be the most appropriate mechanism for dealing with concerns surrounding water use. While rules and restrictions on water use assessments may achieve the goal of impact mitigation, they do so in a way that is inefficient for water market operations, as they impose time and cost burdens on processing applications to trade water entitlements.

Restrictions on the sale of water to non-landholders/non-water users often take the form of clauses within an operator's supply agreement/constitution that specify that only landholders can hold water shares in the operator's water entitlement. In some cases these restrictions may be a feature of jurisdictional water policy.

The rationale for restrictions on the sale of water to non-landholders and non-water users appear to relate to concerns about speculative behaviour in water markets (i.e. water 'hoarding' and manipulation of water markets) and concerns relating to water exports from a district (see section 4.2).

- Question 4.1: To what extent, and in what circumstances, is it appropriate for an operator to be able to impose restrictions on the parties to whom water can be sold? More specifically:
- a) What are the specific forms of these restrictions, and their implications?
 - b) To what extent are these restrictions imposed to comply with or reflect jurisdictional requirements? What is the specific jurisdictional requirement and what is the specific restriction imposed?
 - c) What are the impacts and significance of these types of restrictions in terms of achieving the water market and trading objectives and principles?

4.2 Constraints on water exports

One of the key objectives of the NWI is the commitment to reduce barriers to trade.¹⁹ However, the majority of operators in the MDB place some form of restriction on water sales to areas outside their areas of operations. These restrictions may take the form of:

- specified limits on the volume/percentages that can be traded out
- requirements for minimum water holdings to be retained
- exit fees, or
- other rules/penalties to discourage water leaving an area.

New South Wales legislation provides for the Minister to impose civil penalties on some specific operators²⁰ if they prevent arrangements being made to permanently transfer a member's irrigation right outside their area of operations, up to an annual threshold of 4 per cent of the operators' water entitlement (in order to comply with obligations agreed under the NWI).²¹ However, many operators are not currently subject to this or other equivalent legislative provisions. Therefore, specified limits on the volumes or percentages of outward water trade may still exist.

In some cases, operators' require minimum water holdings to be retained by the seller. These may take the form of minimum percentages of entitlements previously associated with a landholding that must remain or minimum volumes that must be maintained on each property, sometimes for domestic and stock purposes.

Some operators in the MDB continue to levy exit fees — that is, a fee levied on the seller of a water entitlement that is traded out of the operator's network or district.²² Clause 8 of the Schedule E Protocol on access, exit and termination fees²³ specifies that no exit fees should be levied.

Operators that do not charge exit fees may instead expressly prohibit outward trade of water entitlements or alternatively impose particularly stringent conditions on such transfers.

A variety of other restrictions are imposed by operators on water exports, including:

- requirement on sellers to demonstrate how savings in water use can be achieved to provide adequate surplus entitlement to trade

¹⁹ NWI, clause 63, p. 12.

²⁰ Schedule 1 of the *Water Management Act 2000* (NSW) lists Coleambally Irrigation Ltd, Jemmalong Irrigation Ltd, Western Murray Irrigation Ltd, Murray Irrigation Ltd and Murrumbidgee Irrigation Ltd.

²¹ *Water Management Act* (NSW), s. 71ZA.

²² This does not include any fee associated with the costs of processing the transfer.

²³ Murray Darling Basin Agreement—*Schedule E protocol, access, exit and termination fees*.

- loss of benefits associated with being a member once some water is traded outside the district
- the operator reserving the right to refuse trade to other operators' districts where reciprocal arrangements for trade are not in place or are unacceptable to the operator
- requirement to first offer water entitlements for sale internally.

The rationale offered for constraining outward trade from operators' districts typically relates to concerns regarding the impacts of water trade on third parties.

- Question 4.2: To what extent, and in what circumstances, is it appropriate for an operator to be able to impose restrictions on the export of water?
More specifically:
- a) What other restrictions of this type are imposed by operators and what are their implications?
 - b) To what extent are these restrictions imposed to comply with or reflect jurisdictional requirements? What is the specific jurisdictional requirement and what is the specific restriction imposed?
 - c) What are the impacts and significance of these types of restrictions in terms of achieving the water market and trading objectives and principles?
 - d) What alternate methods could be used to manage concerns related to water exports?

4.3 Other constraints on trade and transformation

A number of other rules and processes imposed by operators may prevent or unreasonably delay transformation and/or trade. These include:

- requiring sellers to have metered supply before water can be traded
- restrictions on transformation and/or trade of specific forms of water rights (i.e. town water, groundwater, stock and domestic, dam fill licences, drainage water or water used for other special purposes)
- restricting trade out of specific districts or predefined zones within an operator's area of operations

- exchange/conversion rates or trade reduction factors applied to water transformation and/or trade (e.g. to account for conveyance losses or to reduce over allocation)
- transitional arrangements and temporary rules to manage matters such as limiting trade in sleeper/dozer entitlements or bringing historic unlicensed use into the licensing regime (e.g. only allowing a trade to proceed if water is attached to land that has been defined as previously irrigated).

These restrictions may have been implemented to address specific infrastructure operational requirements or environmental objectives.

In some cases there may be other options for achieving these operational requirements and environmental objectives, such as through more clearly defined water use rights. However, these alternate arrangements could result in higher transaction costs or may be such that the costs may exceed the benefits.

- Question 4.3: To what extent, and in what circumstances, is it appropriate for an operator to be able to impose other constraints, such as those imposed for operational and environmental purposes, on trade and/or transformation? (Where appropriate please identify the specific constraint to which you are referring) More specifically:
- a) What specific constraints are imposed by operators and what are their implications?
 - b) To what extent are these constraints imposed to comply with or reflect jurisdictional requirements? What is the specific jurisdictional requirement and what is the specific constraint imposed?
 - c) What are the impacts and significance of these constraints in terms of achieving the water market and trading objectives and principles?
 - d) What alternate methods could be used to manage the issues these constraints are intended to address?
 - In what circumstances could delivery entitlements/capacity shares be employed?
 - In what circumstances could specified trading zones be employed?
 - e) Should operators have the option of employing restrictions temporarily or for transitional purposes? If so, in what circumstances and in what manner?

4.4 Security for future payment of fees

Under the Schedule E Protocol on access, exit and termination fees²⁴ water rights are to be unbundled from delivery rights, with the on-going fees for access to the operator's water delivery network applied to the delivery right rather than the water right. As a result, irrigators would be able to choose to maintain their delivery right and continue to pay on-going access fees following the sale of their water right.

While irrigators would remain contractually responsible for the payment of access fees, and existing legal remedies remain available to operators to recover any debts owed to them, some operators have raised concerns with this arrangement as it may:

- give rise to a range of commercial and practical concerns surrounding the recovery of access fees, where access fees are no longer secured against the value of the water entitlement
- lessen the revenue surety of the operator, thereby increasing its overall risk profile.

One option for addressing these concerns could be for an operator to limit the proportion of a member's total irrigation right that can be transformed into a water access entitlement.

However, by requiring security in the form of a share of a member's irrigation right, an operator is likely to inhibit the flexibility of its members by locking up capital that could otherwise be accessed by trading these entitlements. This cost is likely to be exacerbated the greater the proportion of the security required by the operator and the longer the period over which the security is held.

To address operators' concerns regarding credit risk, the Schedule E Protocol on access, exit and termination fees provides for some circumstances when an operator can seek security over the future payment of access fees. Specifically:

Before approving the transfer of any water entitlement, an infrastructure operator should not require security for the payment of future continuing access fees unless:

- (a) the current market value of any water entitlements retained by the transferor to water within the relevant irrigation district is less than 50 per cent of any termination fee which would be payable upon the surrender of all of the delivery entitlements retained; and
- (b) the infrastructure operator considers, on reasonable grounds, that there is a significant risk that the transferor may be unable to pay future access fees in relation to those delivery entitlements, when they fall due.²⁵

²⁴ Murray Darling Basin Agreement (MDBA)— *Schedule E Protocol, access, exit and termination fees*.

²⁵ Clause 9(1) of the MDBA— *Schedule E Protocol, access, exit and termination fees*.

Question 4.4.1: To what extent do irrigators who elect to maintain their delivery entitlement following the sale of their water entitlement present a risk to the revenue security of an operator?

Question 4.4.2: To what extent, and in what circumstances, is it appropriate for an operator to require security to be offered as a condition on the transformation and/or trade of water rights? More specifically:

- a) What is the impact and significance of operators requiring security in terms of achieving the Basin water market and trading objectives and principles?
- b) What specific requirements relating to security are imposed by operators? What are their implications?
- c) What are the implications for operators if they were unable to require security for payment of future access fees as a condition of transformation and/or trade?
- d) Are existing legal remedies for the recovery of debts adequate for operators to manage their credit risks?
 - Are there impediments that limit an operator's ability to enforce its contractual arrangements?
- e) Is there scope to use other forms of security such as unmortgaged land or bank guarantees where an irrigator elects to maintain their delivery right after the sale of their water entitlement?
- f) Should the amount of any security collateral requested be capped? If so, why and to what extent?
- g) Are operators in a position to assess the extent to which particular irrigators represent a credit risk?

4.5 Administrative fees and charges

Operators may incur costs as a result of enacting transformation and/or trade processes. However, the imposition of excessive administrative fees and charges can increase transactions costs and therefore impede the operation of water markets.

- Question 4.5: In relation to operators' administrative fees and charges for processing a transformation and/or trade:
- a) What is the impact and significance of these fees and charges in terms of achieving the water market and trading objectives and principles?
 - b) Do current fees and charges reflect operators' costs?
 - c) Should the water market rules specify that these fees and charges be based on cost recovery?

4.6 Cut-off dates and trading seasons

Operators' imposition of cut-off dates for completing trades (or submitting trade applications) or their definition of 'trading seasons' that are shorter than the irrigation season could act as barriers to transformation and/or trade.

- Question 4.6: To what extent, and in what circumstances, should an operator to be able to specify cut-off dates for completing trades or define trading seasons?
- a) Do such arrangements act as a barrier to water trade?
 - b) Are these arrangements imposed to comply with or reflect jurisdictional requirements? What is the specific jurisdictional requirement and what is the specific policy implemented?

4.7 Interaction between operators and intermediaries

In some instances operators may delay considering an application to trade because the operator's brokerage services, preferred broker or intermediary may not have been used. Alternatively, operators may provide the opportunity for their own or preferred brokers to expedite the trading process by accepting forms electronically, whereas other brokers are required to provide forms in hard copy.

There may also be discrepancies in operators' administrative fees and charges for processing trades depending on which intermediary is involved.

Question 4.7.1: Do operators recommend specific brokers or exchanges to irrigators seeking to trade? On what basis are any such recommendations made?

Question 4.7.2: Is there evidence that particular applications to trade are expedited or processed differently by operators due to those trades taking place through a particular exchange or broker? If so, what is the justification for this?

5 Actions that should be required

The transformation and/or trade of an individual's water right may be prevented or unreasonably delayed by the inactions of an operator, such as:

- a lack of clearly defined, comprehensive terms and conditions that apply to transformation and/or trade
- a lack of clearly defined, comprehensive arrangements for water delivery so as to enable transformation without trade
- a lack of clearly defined, comprehensive administrative processes for transformation and/or trade
- not completing processes needed to give effect to transformation and/or trade in a timely manner
- incompatibility of operators' water registers and accounts
- limiting the provision of market information.

The ACCC is therefore seeking submissions on what may form a minimum set of actions that an operator should be required to undertake, so as not to prevent or unreasonably delay transformation and/or trade.

5.1 Terms and conditions for transformation and/or trade

Where a group water access entitlement is held by an operator, the irrigation right held by a member is defined in their supply agreement²⁶ with the operator. These supply agreements are often not clearly and comprehensively documented.

As noted in chapter 3, an efficient water market requires that property rights are well defined and participants are well informed. However, supply agreements between operators and their customers or members often leave certain aspects of the agreement unspecified, or state that certain terms and conditions of the agreement can be determined unilaterally by the operator. For example, the supply agreements of many operators provide that trading terms and conditions may be developed by the operator and may be subject to change at the operator's discretion.

In some cases an operator may attempt to duplicate government water trading policy and rules (or create rules that interpret government policy) in its trading terms and conditions. Although this may streamline trading approvals, it has the potential to

²⁶ Where an operator's shareholders are also their customers, supply conditions are often contained in the arrangements governing the shareholder/trustee relationship and/or the arrangements governing the ownership of the share of the water entitlement. All of these arrangements are, in effect, part of the supply agreement.

create inconsistencies in the application of government water trading policies and also blur the line between the policies of government and policies of the operator.

Question 5.1.1: To what extent are operators' terms and conditions for transformation and/or trade presently:

- a) Clearly specified?
- b) Comprehensive?
- c) Readily available?

Question 5.1.2: Should operators' terms and conditions for transformation and/or trade be comprehensive and clearly specified as part of the supply agreement?

- a) What are the implications of not having comprehensive, clearly specified terms and conditions?
- b) What specific terms and conditions should be clearly specified?
- c) Should these terms and conditions be open to unilateral variation by the operator? If so, how often and according to what processes?
- d) Should operators be required to identify where terms and conditions have been adopted to comply with government legislation or policies?

5.2 Enabling transformation separate to trade

Transformation and trade are two distinct processes because some members may choose to transform their irrigation right but may not trade the water access entitlement. When an irrigator that holds a water access entitlement continues to require delivery services, both parties would require certainty in regard to ongoing delivery arrangements.

One way of providing certainty would be for the operator to develop delivery contracts for future supply that define:

- the obligations of the operator, in respect of minimum service standards and delivery conditions
- the rights and payment obligations of the water access entitlement holder
- the conditions under which the contract can be terminated or the arrangements for periodic review by both parties

These delivery contracts may differ from the supply agreements that apply to members who hold irrigation rights.

Explicit delivery contracts are already used by some operators for some irrigators who hold water access entitlements. For example, this may apply when an irrigator purchases a water entitlement under ‘tagged-trade’ arrangements.

The ACCC is aware that designing contracts that clearly define all the rights and obligations of parties going forward once an investment has already been made and/or where there is piecemeal investment (e.g. expenditure on asset renewals) that involves addressing complex issues.

Question 5.2.1: To what extent is it currently possible for an irrigator to transform their irrigation right into a water access entitlement without subsequently trading that entitlement?

a) When has this occurred and were separate contractual arrangements for ongoing delivery entered into?

Question 5.2.2: Should operators be required to establish and clearly specify the minimum terms and conditions on which they will provide delivery services to irrigators who hold a transformed water access entitlement? If so:

a) What should these minimum terms and conditions be?

b) Should operators have the discretion to set terms and conditions that are different to those applied to members with irrigation rights?

c) Should operators have the discretion to set terms and conditions that apply to **individual** water access entitlement holders?

d) Should these terms and conditions be open to unilateral variation by the operator? If so, how often and according to what processes?

5.3 Transformation and/or trade administrative process

Providing irrigators with information about transformation and/or trading approval and administrative processes can reduce these transaction costs and facilitate the operation of efficient markets.

It is understood that before receiving a formal application for transformation and subsequent trade of an irrigation right, operators typically provide the applicant with

information²⁷ that is used to prepare the formal application for transformation and trade of the irrigation right. Some operators have developed trade application forms to ensure that they have all the necessary information.

Although the transformation and trading processes of operators are sometimes not documented, it is understood that upon receipt of the application, operators typically check the following:

- whether data on the application form is readable and correct (e.g. whether the entitlement volume specified is correct, signatures of all signatories have been obtained, and correct forms are attached)
- confirm with the relevant office of state revenue that duty associated with the water right has been paid
- that all liabilities to the operator have been paid in full or the buyer has signed an acknowledgment accepting any liabilities
- if there are mortgages and/or encumbrances, that there is consent from any registered third parties
- whether the original certificates associated with the irrigation right have been received
- whether a statutory declaration has been provided from the seller stating that they own the irrigation right
- whether the associated delivery right will be terminated or maintained, and therefore the fee implications of this arrangement
- whether the proposed trade breaches any terms and conditions of the operator
- whether the proposed trade is likely to be approved by the relevant approval authority, i.e. does it breach trade rules and limits in jurisdictional water plans (typically through a quick check with the approving authority)
- whether the processing fees associated with the transformation and/or trade have been paid.

In addition, the transformation and subsequent trade of a water access entitlement may be subject to final approval by the board or senior executive of the operator.

²⁷ For example, the operator may provide information on the irrigation right held (e.g. ownership, volume and type) and the future liabilities associated with the right (i.e. outstanding water charges, usage to date, any registered encumbrances and any other commitments such as Snowy Hydro borrows, or commitments made under a land and water management plan).

In many cases the operator is not the relevant jurisdictional approval authority and therefore a further application must be made to the relevant authority to approve the trade of the water access entitlement. When transformation and trade occur together, this application is often undertaken by the operator on behalf of their member. The processes of the operator must therefore be compliant with the jurisdiction's trading approval processes.

Question 5.3.1: What other actions (other than those identified above) may be undertaken by an operator to process and/or approve a transformation and/or trade? What is the rationale for this action?

Question 5.3.2: What specific information would an individual require from an operator before an application to transform and/or trade is prepared? Do operators readily provide this information (i.e. in a timely manner and at minimal cost)?

Question 5.3.3: What is the minimum information an operator would need to obtain from an applicant to enable transformation and/or trade?

Question 5.3.4: Is there merit in developing transformation and trading application forms that are standardised across operators? If so, what information would be required in these forms?

Question 5.3.5: Are operators' processes for transformation and/or trade approval efficient? How could these processes be streamlined?

Question 5.3.6: If applicable, what is the rationale for requiring board (or senior executive) approval as part of the transformation and/or trade process?

Question 5.3.7: Is there merit in operators being required to identify which transformation and/or trading processes are in place to comply with state legislation and policies?

5.4 Timeliness

Timely arrangements are important to ensure that transformation and/or trade is not delayed unreasonably and that the transaction costs associated with these processes are minimised. Processing trades is not only influenced by the procedures and timeliness of operators, but may also be affected by the processes of government agencies.

To ensure the timely processing of transformation and/or trading applications, time limits could be imposed on operators for completing these actions (upon receipt of a correctly completed application).

Question 5.4.1: Are the transformation and/or trading approval processes of operators undertaken in a reasonable timeframe?

Question 5.4.2: If the water market rules were to prescribe time limits for processing transformation and trading applications upon receipt of a correctly completed application:

- a) What factors should be considered in determining these time limits?
- b) At what point would the process for transformation and/or trade be deemed to commence and at what point would it be deemed to have been completed?
- c) What should the time limits be?
- d) Are there any other issues associated with this approach?

Question 5.4.3: To what extent do operators provide information on the time taken to process and give effect to transformation and/or trade approvals? To whom do they provide this information and how frequently?

5.5 Operators' water registers and accounts

A water register is a record of the ownership and characteristics of water rights. In general, the various jurisdictional governments are responsible for updating and maintaining water access entitlement registers. However, in some jurisdictions (such as Victoria) this task has been delegated to the relevant operators.

In New South Wales and South Australia an individual irrigator's share of the operator's water access entitlement is not recorded on the states' water registers. Instead each operator maintains a separate water register of their members' irrigation rights.²⁸

A water account shows the actual amount of water (associated with a water right) available to be taken at a particular time. An operator's water account would therefore record the actual amount of water available to be taken by their members at any time.

Water accounts and water registers need to be linked to ensure changes in ownership are reflected in the water accounts.

Considerable work has been undertaken to implement statutory compatible registers which, under the NWI, jurisdictions agreed to have fully implemented by 2006. Schedule F to the NWI provides guidelines for jurisdictions' water registers.

²⁸ Some New South Wales operators (along with other operators outside the MDB) have developed a combined register—the National Irrigation Corporations Water Entitlement Register (NICWER).

Water registers and water accounts protect the integrity of entitlements and convey important information regarding the security and reliability of the entitlement; the availability of water; its location for the purposes of attributing the correct volume to the MDB Cap; and assisting in making future allocation decisions.

Compatible and interoperable registers and accounts can reduce the transaction costs for market participants by providing an up-to-date record of information, as well as reducing the processing time necessary to give effect to maintaining records.

Question 5.5.1: Should requirements be placed on operators in the development and operation of their water registers and water accounts? If so, what should these water registers and water accounts record?

Question 5.5.2: Is interoperability and/or compatibility between the water registers and accounts of operators and jurisdictions a significant issue?

- a) To what extent are operators' registers and accounts interoperable and/or compatible with those of MDB jurisdictions?
- b) Has a lack of interoperability and/or compatibility contributed to duplication in processes and/or impacted on the timeliness of information provided?

Question 5.5.3: Is the timeliness with which operators update their water registers and accounts a significant issue?

- a) How frequently are operators' registers and water accounts updated?
- b) Should the water market rules prescribe time limits for the updating of registers and accounts? If so, what should these be?

Question 5.5.4: Is it possible to gain direct access to information contained in an operators' registers and/or accounts and who can currently directly access this information?

- a) Should all or some of this information be publicly available or available to specific market participants?

5.6 Market information

It is important that market participants have timely and relevant market information (e.g. on market prices, volume traded and seasonal water allocations). Where the cost of obtaining such information is excessive, the efficient operation of the market can be hindered.

- Question 5.6: In relation to water market information (i.e. volumes and/or prices of irrigation rights and/or water access entitlements traded within, into and out of their area of operations):
- a) Is adequate market information currently available from operators?
 - b) What information do operators collect or could they collect?
 - c) Should operators be required to provide market information and what should this include?
 - Is this information available from other sources?
 - Should this information be publicly available or provided on some other basis?
 - d) Is there any market information that operators should not be required to provide?

6 Financial implications of water market rules

6.1 Mortgageability of irrigation rights

Where operators own a group water access entitlement, member irrigators do not have a clear title recorded on a statutory state wide register as would holders of individual water access entitlements.

In its first biennial assessment of the NWI, the National Water Commission stated that the NWI does not specify a need for entitlements to be held at an individual level:

provided that individual 'entitlement holders' within a bulk entitlement holding have the level of security sought by the NWI, and are able to freely trade water out of, or into, the areas covered by a bulk holding.²⁹

It has been suggested that the ability of financial lenders to define risk and legally enforce a mortgage over an irrigation right (rather than an individual water access entitlement) is compromised.³⁰ This could affect the ability of irrigators to access finance on favourable terms and conditions.

Question 6.1.1: To what extent are irrigators that do not hold an individual water access entitlement disadvantaged in terms of access to finance, or the terms and conditions for finance, as a result of this arrangement?

Question 6.1.2: What processes are undertaken by operators to identify whether an irrigation right has an encumbrance? Have there been instances where this process has not been effective?

6.2 Tax implications of transformation and trade

Transformation arrangements are a necessary first step if an individual wishes to permanently trade their share of a group water entitlement to anybody other than another group member.

The process of transforming an irrigation right into a water access entitlement may have tax implications for both operators and irrigators. There may also be tax implications for irrigators upon the subsequent trade of the water access entitlement.

²⁹ NWC, *National Water Initiative: First Biennial Assessment of Progress in Implementation*, 2007, p. 32.

³⁰ Scrivco Pty Ltd, *Finance and trade implications of public and private sector entities managing the ownership of bulk water entitlements on behalf of individuals*, prepared for the Australian Bankers Association, September 2006.

Of relevance is a recent class ruling of the Australian Taxation Office that sets out the way in which income tax provisions will apply to the statutory licence roll-over for the replacement of existing water entitlements with new water entitlements in Victoria.³¹

- Question 6.2: What are the possible tax implications in respect of transforming an irrigation right into a water access entitlement for:
- a) Operators?
 - b) Irrigators?

³¹ ATO, class ruling 2008/06.

7 Application and implementation

7.1 Coverage of the water market rules

As discussed in chapter 2, the definition of an operator for the purposes of the Act does not distinguish between operators on the basis of the size of the irrigation network, the number of irrigators or the volume of water rights held by the operator or its irrigators.

As with any new policy regime, implementation of the water market rules is likely to result in upfront costs for the regulated entities. The cost of compliance with water market rules may be largely independent of the size of the operator.

Question 7.1.1: To what extent should the water market rules apply to all operators to the same degree?

- a) Should any distinctions between classes of operators be based on the number of customers serviced, the volume of entitlements or another characteristic of the operator?

Question 7.1.2: Is there merit in a delayed application of the water market rules for specific classes of operators? If so, on what basis should operators be classified?

7.2 Transitional arrangements

The Act provides for the water market rules to take into account transitional arrangements relating to contracts entered into between an operator and another person before water market rules are made or amended.

As previously discussed (section 5.1), not all irrigators have clearly defined contracts with their operator. Even where explicit contracts exist, the specific arrangements and contract period may vary between irrigators. Contract terms may also vary depending on the type of entitlement held.

Question 7.2.1: Do contracts between an operator and its customers or members have a scheduled end date? If not, under what circumstances can existing terms and conditions be reviewed?

Question 7.2.2: How could the water market rules account for any pre-existing contract between an operator and an irrigator?

Question 7.2.3: Are there any other transitional matters that the water market rules should take into consideration?

7.3 Monitoring compliance with the water market rules

The Act provides for the ACCC to monitor compliance with the water market rules. Monitoring will necessarily involve information-gathering and reporting on the part of operators.

When developing the water market rules, the ACCC will consider how the rules can be effectively monitored and enforced, while also having regard to the cost to operators associated with monitoring of compliance with the rules.

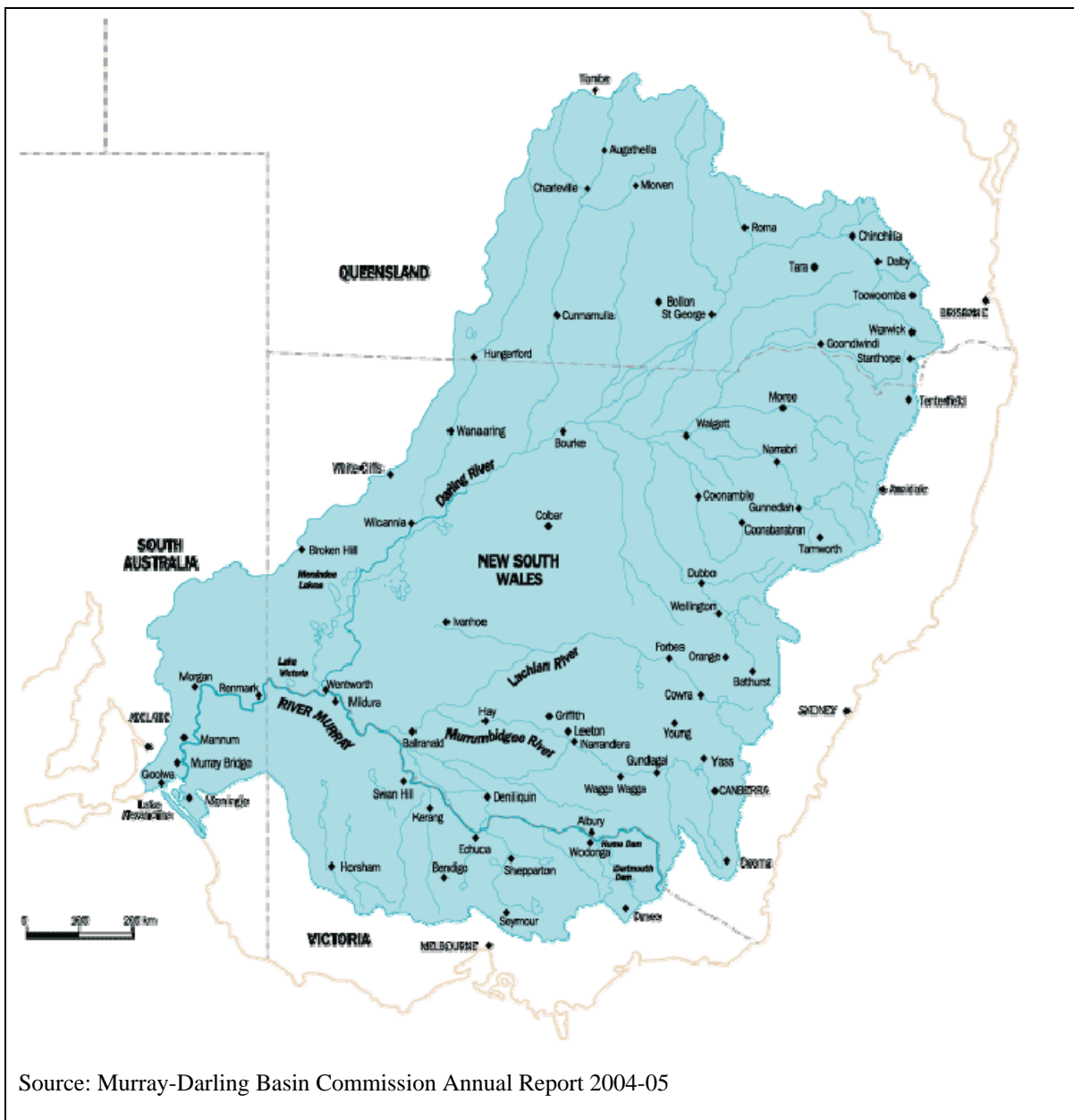
Question 7.3.1: To what extent is the conduct of operators (relevant to the matters the water market rules may relate to) currently monitored? Please provide details.

Question 7.3.2: Are there any other issues the ACCC should be aware of in developing and implementing monitoring arrangements?

Appendix A The Murray-Darling Basin

The Murray-Darling Basin (the Basin) is the catchment for the Murray and Darling rivers and their many tributaries. It covers 1,061,469 square kilometres or 14 per cent of the total area of Australia; it extends from Queensland (north of Roma) and runs through three-quarters of New South Wales, all of the Australian Capital Territory, half of Victoria and through to Goolwa in South Australia.

The Basin contains over 40 per cent of all Australian farms, which produce wool, cotton, wheat, sheep, cattle, dairy produce, rice, oil-seed, wine, fruit and vegetables for both domestic and overseas markets. As Australia's most important agricultural region, the Basin produces one-third of Australia's food supply and supports over a third of Australia's total agricultural production in gross value terms.



Appendix B Water trading rules

Under the *Water Act 2007*, the new Murray-Darling Basin (MDB) Authority is responsible for preparing a Basin plan for adoption by the Minister. The Basin Plan must include the matters set out in section 22 of the Act, including rules for the trading or transfer of tradeable water rights. In developing the water trading rules, the Authority must obtain and have regard to the advice of the ACCC.

The major difference between **water trading rules** and **water market rules** is that:

- Water trading rules will apply to a broad set of water market participants in respect of all tradeable water rights.
- Water market rules will apply only to irrigation infrastructure operators to ensure that the water rights of irrigators are, in fact, tradeable.

As with water market rules, water trading rules must contribute to achieving the Basin water market and trading objectives and principles set out in Schedule 3 of the Act.

Issues that can be addressed through the water trading rules include:

- the terms, conditions and processes that may, or may not, be imposed in relation to water trade
- the imposition or removal of restrictions on trade
- the availability of information relating to trading and reporting of trades
- most of the matters currently addressed in Schedule E to the MDB Agreement and its related protocols.

Schedule E to the MDB Agreement and related protocols cover issues such as:

- environmental and land use impacts, including salinity
- delivery capacity issues
- effect of trade on reliability of supply
- compliance with caps on extraction levels
- the ability to manage the shared aspects of the MDB region as a whole.

The Authority is yet to be established, and the Basin Plan is not scheduled to be completed until early 2011. Work on advising the Authority on water trading rules is therefore expected to be a major focus of the ACCC's work in 2009-10.

Appendix C Current arrangements of operators

Operators in the MDB have varying corporate governance arrangements. The corporate governance arrangements in Victoria and Queensland vary substantially from New South Wales and South Australia. The types of arrangements with customers also vary within jurisdictions.

In New South Wales, the majority of the larger operators are privately owned, non-listed, not-for-profit companies. Many of these organisations were privatised between 1995 and 1999 when the New South Wales Government issued shares in these companies to irrigators within their areas of operation.

Many of the smaller operators that are also privately owned, have a cooperative structure in that the member/irrigators are the shareholders in the entity that owns the shared delivery infrastructure.

Similarly, in South Australia the operators are typically private trusts where the irrigators are the shareholders.

In South Australia and New South Wales, both private diverters and operators can own water access entitlements. In these states, irrigators within the districts of the operators hold a share of the operator's water access entitlement (i.e. an irrigation right). These operators are typically corporations or trusts whereby the shareholders and/or trustees of the operators were also the existing customers creating a quasi-cooperative.

In New South Wales, operators typically have agreements of various forms with their members, under which members are assigned a share of the operator's water access entitlement. In South Australia, s. 53 of the *Irrigation Act 1994* states that a member irrigator of an operator is entitled to use the quantity of water allocated in respect of that irrigator, such that the irrigation right held by the irrigator is recognised in legislation.

Within both New South Wales and South Australia, arrangements regarding an irrigator's share of the water access entitlement are often contained in the arrangements governing the shareholder and/or trustee relationship, and/or the arrangements governing ownership and use of the share of the water access entitlement.

In Victoria operators are statutory authorities owned by the Victorian Government. These authorities must submit their corporate plans each year to the responsible minister to ensure compatibility of their business directions with government policy.

SunWater, the largest operator in Queensland, has recently changed its structure from a statutory government-owned corporation to a company government-owned corporation. However, under both arrangements it is accountable to its shareholding ministers.

In Victoria and Queensland water entitlements are held by individual irrigators, although the arrangements for securing delivery of this water vary across the jurisdictions.

In Queensland, delivery of water is supported by contracts with the water storage operator and the infrastructure operator respectively. The delivery contract with the infrastructure operator (generally SunWater) defines the service standards and delivery conditions as well as the rights and payment obligations of the holder.

In Victoria, delivery shares have been created that define the rights and responsibility of the irrigator and operator. Delivery shares are essentially separately defined entitlements to have water delivered at specified times, rates and locations under specified circumstances. These can be traded within Victoria subject to the infrastructure arrangement within the various irrigation areas.

Appendix D MDB state legislative arrangements

New South Wales

Under the *Water Management Act 2000*, the New South Wales Department of Water and Energy (DWE) is empowered to develop water sharing plans that define the rights of water users and the environment.

Water access entitlements in New South Wales are termed water access licences (WALs) and specify:

- a share component — a unit share of the relevant security pool
- an extraction component — entitles the holder to take water at specified times, rates, locations and circumstances.³²

The right to apply or use water is defined in a water use approval.

Operators hold WALs on behalf of their shareholders and/or trustees, and irrigators supplied by these operators receive a share of the WAL according to varying contractual arrangements.

The Water Management Act (NSW) also governs the trading of WALs. Transformation of an individual's irrigation right against an operator into a water access entitlement (or assignment of a WAL share component) requires an application from the operator holding the original WAL and ministerial consent (exercised by DWE).

Similarly, the assignment of water allocations by a member of an operator will require operator agreement and ministerial consent (delegated to State Water).

South Australia

In South Australia, the *Natural Resources Management Act 2004* (the NRMA) authorises the Minister to grant entitlements for prescribed water resources for consumption through issuing water licences for private diverters, water authorities and operators.

An operator is required to abide by the conditions of its licence (water access entitlement) issued to it under the NRMA. Licence conditions may govern water extraction, conveyance and use, and can be varied by the Minister.

³² The extraction component broadly corresponds to a delivery share. At present, the extraction right is still bundled with the WAL; however, its separation is being considered in congested systems.

At present, South Australia has two types of water licences—a licence endorsed with a water (holding) allocation and a licence endorsed with a water (taking) allocation.^{33, 34, 35}

Rural water infrastructure services in South Australia are predominately provided by private irrigation trusts. The *Irrigation Act 1994* or other trust-specific Acts, such as the *Renmark Irrigation Trust Act 1936* are the main instruments governing the provision of water delivery and drainage services. However, the *Irrigation Act* is, for the most part, silent on the arrangements by which irrigation trusts may hold entitlements on behalf of individual irrigators.

Section 157 of the *NRMA* enables the transfer of water licence and allocations subject to various conditions. Water trading in South Australia is largely administered by the Department of Water Land and Biodiversity Conservation (DWLBC), with the exception of transfers within private irrigation districts (administered by trusts).

Section 34 of the *Irrigation Act* also covers arrangements for the transfer of water allocations. It notes that the transfer of a water allocation is subject to the approval of the authority — or operator in relation to the private irrigation districts constituted by the Act — which may be either conditional or non-conditional.³⁶

Queensland

The *Water Act 2000* is the overarching legislative framework for water planning and management in Queensland. This Act is administered by the Queensland Department of Natural Resources and Water (NRW). In Queensland, water entitlements (termed water allocations) are established by the Act and conditions for the taking of water (e.g. location, pumping conditions) are included on the entitlement. Water allocations are only created once a resource operations plan (ROP) has been finalised for the relevant water resource area.

In Queensland's regulated systems, the delivery of water is managed through contracts with the relevant operator, the most prominent of which is SunWater.

³³ The current arrangements will change in the near future because South Australia is separating water rights into water access entitlements (a right to a share of the resource); water allocations (a right to a specific volume of water); site use approvals (an approval to use the water); water resource works approvals (an approval to extract or take the water); and delivery capacity entitlements (a right to up-stream capacity to allow water to be available for taking when needed).

³⁴ A holding allocation is an ongoing right that preserves the right to take water in the future but does not allow the physical extraction or use of water. Further, it is not related to a particular piece of land and does not contain conditions relating to the extraction or use of water. It can, however, be converted into a taking allocation (where capacity allows, and subject to the provisions of the water allocation plan).

³⁵ A taking allocation is an ongoing right to take and use a quantity of water. It typically defines how that water can be taken and used and the piece of land to which it applies. It may also list other conditions relating to salinity or the timing or rate of pumping.

³⁶ The *Renmark Irrigation Trust Act* is silent on the ability for irrigators or the trust to trade water.

Permanent water trading in Queensland is mainly possible in ‘water allocations’ i.e. where an ROP has been finalised.³⁷ The ROP contains ‘change’ rules that detail permitted and prohibited changes to water allocations against which proposed trades can be assessed. The NRW is responsible for this assessment. All water entitlement dealings must be registered on the water allocations register (WAR) to have legal effect.

SunWater is the responsible approval authority in regard to the trading of seasonal assignments. The ACCC is not aware of any statutory or policy arrangements that govern SunWater’s trading approval processes.

While SunWater is not involved in approving trade in water access entitlements, a transfer can not be registered without a supply contract issued by SunWater. However, it is understood SunWater must agree to provide water to the new purchaser should a trade take place. In addition, interest holder consent (e.g. mortgagees, SunWater etc.) may also be required to allow certain dealings to be registered on the WAR and therefore have legal effect.

Victoria

The *Water Act 1989* (Vic) is the principal legislation for water management in Victoria. Pursuant to s. 22(3) and Part 4 of this Act, water may be allocated by the Minister as an environmental entitlement, a bulk entitlement (held by the operators), a water share or other licences to take and use water.

All operators in Victoria are government-owned water authorities. The Victorian Water Act defines the functions and powers of these operators (such as the power of an operator to levy charges). These businesses are also subject to price regulation by the Essential Services Commission of Victoria under the Water Industry Regulatory Order (WIRO).

Obligations on a Victorian operator in relation to the supply of water (including the obligation to supply customers) are conveyed through both bulk entitlement orders and Part 7 of the *Water Act* (Vic).³⁸

Water rights were further reformed in Victoria through the *Water (Resource Management) Act 2005* (Vic). That Act declares areas for the disaggregation (or unbundling) of individual water rights into water shares, water-use licence and/or registration and delivery shares.

In Victoria, the Minister has the power to make rules regarding the trade of water shares under Part 3A of the *Water Act* (Vic). This includes circumstances in which the consent of any authority will be required (s. 33AZ(b)). A trade application is refused if

³⁷ The *Water Regulation 2002* is subordinate legislation to the *Water Act* that provides an interim trading regime, whereby the holders of interim water allocations may trade.

³⁸ The Statement of Obligations (‘SoO’) developed for each Authority under the WIRO establishes a set of ‘guiding principles’ each authority must comply with in performing its functions under this instrument, which includes the preparation of Water Plans, and consequently the setting of fees and charges.

the application does not comply with the Act or with trading rules. However, it is understood that this power has been delegated to the Victorian operators under s. 306 of the Water Act (Vic).

Victorian operators do not have a role in declaring trading zones and applying conditions between trading zones. However, an operator is able to set the irrigation season length under s. 222 of the Water Act (Vic), which may limit the delivery of traded water within an irrigation district.

Appendix E Basin water market and trading principles

Clause 4 of Schedule 3 to the Water Act is as follows:

- (1) This clause sets out the Basin water market and trading principles.
- (2) Water access entitlements may be traded either permanently, through lease arrangements or through other trading options that may evolve over time, if water resources are physically shared or hydrologic connections and water supply consideration would permit water trading.
- (3) All trades should be recorded on a water register. Registers will be compatible, publicly accessible and reliable, recording information on a whole of catchment basis consistent with the National Water Initiative.
- (4) Restrictions on extraction, diversion or use of water resulting from trade can only be used to manage:
 - (a) environmental impacts, including impacts on ecosystems that depend on underground water; or
 - (b) hydrological, water quality and hydro-geological impacts; or
 - (c) delivery constraints; or
 - (d) impacts on geographical features (such as river and aquifer integrity); or
 - (e) features of major indigenous, cultural heritage or spiritual significance.
- (5) A trade may be refused on the basis that it is inconsistent with the relevant water resource plan.
- (6) Trades must not result in the long term annual diversion limit being exceeded. That is, trades must not:
 - (a) cause an increase in commitments to take water from water resources or parts of water resources; or
 - (b) increase seasonal reversals in flow regimes;
above sustainable levels identified in relevant water resource plans such that environmental water or water dependent ecosystems are adversely affected.
- (7) Trades within over allocated water resources (including ground water resources) may be permitted in some cases subject to conditions to manage long-term impacts on the environment and other users.
- (8) Where necessary, water authorities will facilitate trade by specifying trading zones and providing related information such as the exchange rates to be applied to trades in water allocations to:
 - (a) adjust for the effects of the transfer on hydrology or supply security (transmission losses) or reliability; and

- (b) reflect transfers between different classes of water resources, unregulated streams, regulated streams, supplemented streams, ground water systems and licensed runoff harvesting dams.
- (9) Water trading zones, including ground water trading zones, should be defined in terms of:
- (a) the ability to change the point of extraction of the water from one place to another; and
 - (b) the protection of the environment.

The volume of delivery losses in supplemented systems that provide opportunistic environmental flows will be estimated and taken into account when determining the maximum volume of water that may be traded out of a trading zone.

- (10) Exchange rates must not be used to achieve other outcomes such as to alter the balance between economic use and environmental protection or to reduce overall water use.
- (11) Trade in water allocations may occur within common aquifers or surface water flow systems consistent with water resource plans.
- (12) Trade from a licensed runoff harvesting dam (that is, not a small farm dam) to a river may occur subject to:
- (a) a reduction in dam capacity consistent with the transferred water access entitlement; or
 - (b) retention of sufficient capacity to accommodate evaporative and infiltration losses; or
 - (c) conditions specified in water resource plans to protect the environment.
- (13) Compatible institutional and regulatory arrangements will be pursued to improve intra and interstate trade, and to manage differences in entitlement reliability, supply losses, supply source constraints, trading between systems and cap requirements.
- (14) The transfer of water allocations and entitlements will be facilitated (where appropriate) by water access entitlement tagging, water access entitlement exchange rates or other trading mechanisms that may evolve over time.
- (15) Institutional, legislative and administrative arrangements will be introduced to improve the efficiency and scope of water trade and to remove barriers that may affect potential trade.
- (16) Barriers to permanent trade out of water irrigation areas are up to an annual threshold limit of four per cent of the total water entitlement of that areas will be immediately removed, subject to a review by 2009 by the National Water Commission under paragraph 7(2)(h) of the *National Water Commission Act 2004*, with a move to full and open trade by 2014 at the latest.
- (17) Subject to this clause, no new barriers to trade will be imposed, including in the form of arrangements for addressing stranded assets.