



Australian  
Competition &  
Consumer  
Commission

# **Water market rules position paper**

**July 2008**

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## How to make a submission

The Australian Competition and Consumer Commission (ACCC) welcomes submissions on the preliminary views expressed in this paper as well as any other relevant information that could assist and inform its advice to the Minister. Responses to this paper should be supported with evidence and data wherever possible.

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

If there is any information you would like to request the ACCC not make publicly available, you should provide it in a separate document that has 'Confidential' clearly marked on every page.

The document containing confidential information should have a title such as 'Confidential annexure to submission by [INSERT NAME] on [INSERT DATE]'. (Information on the treatment of confidentiality is discussed in section 1.2.)

Provision of electronic submissions by email is preferred. The ACCC encourages interested parties to make submissions either in Microsoft Word or in PDF (OCR-readable text format—that is, they should be direct conversions from the word processing program, rather than scanned copies in which the text cannot be searched).

Submissions should be sent to:

Email: [water@acc.gov.au](mailto:water@acc.gov.au) (submissions should use the word 'Submission' in the title of the email)

Or by mail to the following address:

Water Branch  
Water market rules—preliminary position paper  
Australian Competition and Consumer Commission  
GPO Box 520  
Melbourne Vic 3001

General inquiries may be directed to the ACCC Infocentre on 1300 302 502 or to [water@acc.gov.au](mailto:water@acc.gov.au).



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## Abbreviations

ACCC	Australian Competition and Consumer Commission
ACT	Australian Capital Territory
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
NSW	New South Wales
NWI	National Water Initiative
Qld	Queensland
SA	South Australia
the Act	<i>Water Act 2007</i> (Cwlth)
Vic	Victoria
WAL	water access licence

# 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).
Conveyance loss	Water lost through evaporation and seepage etc., related to distributing water through an operator's network. These losses represent the difference between the volume of water which needs to be diverted, by an operator (from the water source) for distribution to customers and the volume of water actually delivered by the operator to customers.
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 use.
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 (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 Water Act) apply. This includes fees and charges payable to an irrigation infrastructure operator for access to, or terminating access to, the operator's network.

Termination fee	A fee levied by an infrastructure operator when a delivery entitlement is surrendered to the infrastructure operator to terminate any rights or obligations associated with that delivery entitlement (including any requirement to pay an access fee).
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 right	Any right to hold or take water from a water resource, akin to a property right over water. This may be a statutory right or a right against an irrigation infrastructure operator's water access entitlement.
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.

# Summary

## Water market rules

The *Water Act 2007* (the Act) creates new institutional and governance arrangements to address the sustainability and management of water resources in the Murray-Darling Basin (MDB). The Act builds on earlier reform initiatives, including the National Water Initiative (NWI) and the Murray-Darling Basin Agreement (MDBA), and is supplemented by federal government funding commitments of around \$10 billion.<sup>1</sup>

Key elements of this reform include:

- Capping water diversions, addressing over-allocation and the needs of the environment through the federal government’s water buyback scheme which aims to achieve sustainable use of water in the MDB.
- Modernisation of irrigation infrastructure to reduce water losses.
- Removal of barriers to water trade to facilitate the operation of efficient water markets and provide opportunities for water trading. Water trading will allow water to be traded to its highest value use.

The water market rules address the last of these points—barriers to water trade. 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.<sup>2</sup>

The Act gives the Minister for Climate Change and Water the role of making water market rules. The ACCC’s role is to advise the minister on those rules and the role of monitoring compliance with, and enforcing, the rules.

The ACCC’s advice to the minister will comprise proposed rules along with a statement of reasons for the approach adopted. This paper sets out the ACCC’s preliminary positions on the content of the water market rules.

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<sup>1</sup> The Intergovernmental Agreement on the National Water Initiative between the Australian Government 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 (COAG) in 1994, which was incorporated within the National Competition Policy Agreement in 1995.

<sup>2</sup> Explanatory memorandum to the Water Bill 2007, clause 97, paragraph 190, p. 28.

## ACCC consultation

In April 2008 the ACCC released an issues paper on the water market rules that sought information and submissions from interested parties. The ACCC has so far received 61 submissions, all of which can be viewed on its [website](#).

This paper continues the consultation process. The ACCC is seeking submissions on the preliminary positions presented in the paper as well as any other relevant information that could assist with, and better inform, its advice to the minister.

Given the timeframe for the ACCC to develop its advice on water market rules, submissions need to be provided no later than **Friday, 15 August 2008**. Submissions will be published on the ACCC website and provided to the minister, unless there are confidentiality issues.

There will be further opportunities to inform the development of water market rules in October 2008, when the ACCC will:

- release a draft decision that will incorporate draft rules and a supporting statement of reasons
- hold public forums with interested stakeholders to discuss the ACCC's draft advice.

Final advice on water market rules will be provided to the minister in December 2008.

## Transformation and/or trade of water rights

In many cases, statutory water access entitlements are held by irrigators. In these circumstances the irrigators have clearly defined water rights that can be traded. However, in New South Wales and South Australia water entitlements are typically held by irrigation infrastructure operators ('operators') on behalf of member irrigators.<sup>3</sup>

Transformation allows an irrigator to permanently transform an entitlement held on their behalf by an operator into an independently held water access entitlement registered on a state water registry. An individual may prefer this arrangement because they consider it to be of greater value than an entitlement to water under an irrigation right. Once the water access entitlement is independently held, an irrigator can also trade the entitlement if they choose to do so.<sup>4</sup>

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, independently held water access entitlement.

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<sup>3</sup> An irrigation infrastructure operator is any person who owns or operates infrastructure for the purpose of delivering irrigation water to another person (i.e. an irrigator or other water user). Where a group water access entitlement is held by an operator, the irrigation right held by a member is defined in their supply agreement with the operator.

<sup>4</sup> Held by someone other than the operator.

Submissions from irrigators point to a number of areas where inaction by operators impedes transformation and/or trade. Some irrigators have suggested that their operator's transformation and/or trading processes are either poorly documented or not documented at all. In other cases, irrigators have expressed concern about onerous terms and conditions of transformation and/or trade approval, the processes for changing these terms, and the conditions and timeframes within which an operator must respond to any applications.

This position paper proposes rules to improve transformation and/or trading processes and outcomes. The rules would:

- require operators to do all things necessary to facilitate transformation and/or trade and prevent operators from unduly preventing or delaying these arrangements
- require operators to establish clear terms and conditions for transformation and/or trade, and make these readily available to irrigators
- establish consultation processes for changing the terms and conditions of transformation and/or trade
- establish processes for assessing transformation and/or trade requests, including timeframes for responding to requests
- link operator administrative fees and charges for processing a transformation and/or trade application to costs incurred by the operator.

These requirements may prove onerous for small operators, at least initially. The ACCC proposes to establish standard forms for transformation and/or trade to assist such operators. Operators will then have the option of adopting the ACCC forms or developing their own.

The ACCC's preliminary positions on enabling transformation and/or trade of water rights are listed in box 1.

## **Box 1: ACCC preliminary positions—enabling transformation and/or trade of water rights**

### **Enabling transformation and/or trade**

1. An operator must do all things necessary to facilitate transformation and/or trade of all or part of an irrigator's entitlement in accordance with the water market rules.
2. An operator must not prevent or unreasonably delay transformation of all or part of an irrigator's entitlement under any circumstances, other than in accordance with the water market rules.

### **Terms and conditions**

3. Operators should have in place clearly stated terms and conditions to facilitate transformation and/or trade.
4. The terms and conditions relating to transformation and/or trade approvals should:
  - be readily available to all parties and rationalised where possible
  - be published on the operator's website (if applicable) and customers of the operator should be notified in writing of the existence of these documents.
5. Operators should clearly define and document the process associated with making any required changes to the terms and conditions for transformation and/or trade approvals (the ACCC may also provide guidance to operators on the appropriateness of the process undertaken to implement such changes).
6. Operators must **consult** with irrigators who may be materially affected by a change to the terms and conditions (the ACCC may also provide guidance to operators on what could be considered 'material').
7. Operators must **notify** irrigators of all changes to their terms and conditions.
8. In consulting with or notifying irrigators, operators should outline the reasons for the proposed change and supply supporting documentation if applicable.
9. At the completion of the transitory adjustment period of the water market rules (date TBC), an operator must notify all its irrigators in writing of the application of the water market rules; specifically, an information pack should be provided to irrigators that includes a copy of the water market rules and applicable transformation application forms.

### **Application process**

10. Operators must develop a base set of forms for both transformation applications and transformation and trade applications. The basic information required for both processes may include:
  - applicant details
  - account number
  - confirmation of identity
  - the number and type of units/volume to be transformed and/or traded
  - confirmation that all fees have been paid.

11. In addition, additional information for transformation and trade may include:
  - buyer details, including details of any existing water access entitlement for the transformed units to be appended to
  - the number and type of units/volume of water to be traded.
12. An operator must not request details relating to the purpose for transformation and/or trade from applicants.
13. An operator must make information regarding the applicant's irrigation right readily available upon request and within a reasonable time frame.

**Time limits**

14. Operators must process applications efficiently, and not unduly delay the approval process.
15. Time limits for processing transformation and/or trade applications are as follows:
  - initial assessment period—upon lodgment of an application, the operator must ensure that the application has been properly completed and request further details as required within three business days.
  - approval period—upon acceptance of a correctly completed application, the operator must process the application within 10 business days, including completion of the following steps:
    - processing and checking of the application
    - final approval by the operator
    - advising the applicant of the status of the application
    - referral of the application to the relevant jurisdictional authority for further approval (where applicable).
  - updating the register—once the operator has been advised of the final approval, it must ensure that the relevant register has been updated within two business days.
16. These time limits do not include any time taken by the relevant jurisdictional authority in approving the transformation and/or trade.
17. These time limits apply irrespective of an operator's approval procedure or the size of the operator.

**Administrative fees and charges**

18. Any administrative fees and charges for processing a transformation and/or trade must be based on cost recovery.
19. Any administrative fees for processing a transformation and/or trade must be contained within an operator's terms and conditions for transformation and/or trade.

## Water delivery rights

The primary reason for transforming irrigation rights is to enable trade. However, there are a number of other benefits, including more clearly defined water rights, improved access to finance and streamlined trade in the future. These benefits may encourage irrigators to transform their irrigation rights without necessarily trading these out of their district.

Before transformation, irrigators' water rights are bundled in a package that comprises the right to a volume/share of water and the right to have this water delivered both encapsulated in their supply agreements with the operator. Once the right to water is unbundled into a separate water access entitlement through transformation, terms and conditions need to be established for water delivery. These terms and conditions may be substantially the same as those in the bundled package. In some cases, however, irrigation operators and irrigators may wish to re-negotiate terms and conditions of delivery.

This position paper proposes measures to protect irrigators in such negotiations. One of the measures proposed is a requirement for the operator to continue to provide water delivery rights after transformation if required by the irrigator. A second measure is a requirement that the terms and conditions of the negotiated delivery contract should be substantially equivalent to those under the previous supply contract governing the irrigation right.

The ACCC's preliminary positions on water delivery rights are set out in box 2.

### **Box 2: ACCC preliminary positions—water delivery rights**

1. An operator must provide delivery arrangements for a transformed water entitlement if required by an irrigator.
2. Upon transformation, terms and conditions of a delivery contract may reflect those contained in the arrangements as they previously related to the irrigation right.  
Alternatively, if a delivery contract is re-negotiated this must be done so in good faith between an operator and the irrigator with a transformed water entitlement.
3. Unless otherwise negotiated, the terms and conditions of new delivery contracts should be substantially equivalent to those terms and conditions attached to delivery services provided under the previous supply contract governing the irrigation right.
4. In circumstances where an operator's standard delivery contract is not available or negotiation of a new delivery contract is required, the operator must use their best endeavours to negotiate a new contract within 30 days of the transformation being completed.
5. During the time of negotiation, the operator must provide delivery services in accordance with the terms and conditions of delivery services under the previous supply contract governing the irrigation right.

## Restrictions on transformation and trade

As well as the inactions of operators acting as impediments to transformation and trading processes, a number of submissions identified prohibitions and other restrictions on transformation and/or trade that operators apply when assessing applications. These restrictions may be in the operator's supply agreements with irrigators or the terms and conditions for transformation and/or trade, or they may not be documented.

Restrictive provisions identified by the ACCC include:

- fees and charges levied on the sale of water
- restrictions based on the identity of the water purchaser
- restrictions relating to state legislative requirements
- restrictions relating to delivery management
- restrictions relating to conveyancing losses
- metering requirements
- limits on trade out of an irrigation district
- cut-off dates and trading seasons.

Any restrictions likely to reduce trade may lead to inefficient market outcomes and may be inconsistent with the **Basin water market and trading objectives and principles** as set out in schedule 3 of the Act:

- (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 ...

The ACCC's preliminary position is that there should be a general prohibition on restrictive provisions in an operator's supply agreements (or associated terms and conditions) with customers that prevent or unreasonably delay transformation and/or trade.

However, in some cases restrictions on transformation and/or trade are imposed for legitimate operational, regulatory or other compelling reasons. The position paper takes these into account by specifying five permitted restrictions:

1. Administrative fees or charges for processing a transformation and/or trade or a regulated water charge as defined under the Act.
2. Minimum water holding requirements for stock and domestic purposes. Some operators prevent irrigators from trading below specified minimum holding requirements. The ACCC considers such restrictions reasonable where the obligation is specified in state government legislative instruments.
3. Metering requirements. Many submissions supported requirements for an irrigator to have a metered supply before allowing that irrigator to trade, except where the irrigator is terminating access to the operator's network. Submissions noted that metering enables monitoring and detection of theft, more accurate

accounting for water and the provision of data to support efficiency improvements.

4. Caps on the level of permanent water trade-out from irrigation districts. The Council of Australian Governments (COAG) in its meeting on 3 July 2008 stated its ambition to increase the cap from 4 to 6 per cent by the end of 2009. The position paper proposes allowing the cap agreed to by the federal government and state and territory governments.
5. The requirement of security for the future payment of access fees (to be discussed separately).

The ACCC considers the other restrictive conditions identified are unwarranted barriers to trade. The ACCC's preliminary positions on restrictions on transformation and/or trade are listed in box 3.

**Box 3: ACCC preliminary positions—restrictions on transformation and/or trade**

**A general prohibition on restrictions**

- 1 Subject to limited explicit exceptions, provided for in the water market rules, an operator should not be permitted to impose any restrictions in contracts, arrangements or understandings.
- 2 Prohibited restrictions on trade and/or transformation that may be imposed by operators include but are not limited to:
  - Any fees or charges levied on the transformation and/or trade of a water access entitlement except where the fee is an administrative fee or charge for processing a transformation and/or trade, calculated in accordance with the water market rules, or is a regulated water charge as defined under the Act.
  - Any restrictions based on the identity of the water purchaser.
  - Requirements to transform a separately held water access entitlement back into the scheme entitlement.
  - Requirement to maintain a minimum irrigation right on the transformation and/or trade, where this is not a requirement of a community service obligation contained in a state legislative instrument.
  - Restrictions relating to regulating land use and environmental effects of water use.
  - Restrictions relating to the category of the water entitlement.

- Restrictions to manage delivery and the physical constraints of the irrigation infrastructure, except where the transformed water entitlement is sold within the district.
- Restrictions for the purposes of covering conveyance losses.
- Imposition of cut-off dates and trading seasons.

**Permitted restrictions**

3. Administrative fees or charge for processing a transformation and/or trade, calculated in accordance with the water market rules, or a regulated water charge as defined under the Act.
4. Restrictions that relate to minimum water holdings explicitly maintained for stock and domestic purposes, where this obligation is contained in a state legislative instrument.
5. Requirements for an irrigator to have a metered supply before being permitted to transform and/or trade, except where the irrigator is terminating access to the operator's network.
6. The cap on permanent trade out of an irrigation district as agreed to by the federal government and state governments.

## Security

The Act states that the water market rules may permit an operator to require security for payment of future charges.<sup>5</sup> The ACCC has considered whether, and to what extent the water market rules should permit operators to seek security as a condition of trade.

Some operators require security against the future payments of fees, often in the form of security over a portion of irrigators' water rights. The water covered by the security cannot be traded and so this requirement can be considered to prevent or delay trade. These impediments need to be balanced against the legitimate interests of irrigation operators to mitigate the risks of non-payment of fees.

The position paper proposes allowing operators to require security under certain circumstances. It also proposes allowing irrigators to offer security over something other than their water access entitlement and requiring the operator to give due consideration to the offer. The value of the security is capped at 50 per cent of the applicable termination fee.

The ACCC's preliminary positions on security are set out in box 4.

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<sup>5</sup> Water Act, s. 97(5) (a).

#### **Box 4: ACCC preliminary positions—security**

1. An operator should have the ability to seek security to mitigate the risk of an irrigator’s default on the future payment of access fees in specific circumstances.

#### **When security may be required**

2. An operator can only require security for future payment of fees when:
  - the irrigator will retain less than 20 per cent of their original water access entitlement, **and**
  - the infrastructure operator considers, on reasonable grounds, that there is a significant risk that the irrigator may be unable or unwilling to pay future access fees, when they fall due.
3. Reasonable grounds include where an irrigator:
  - has been in arrears in failing to pay the access charge for a period of more than 60 days on more than occasion in the last three years or
  - is a new landholder and has been a member of the scheme for fewer than three years.
4. An operator may register a charge over 20 per cent of the irrigator’s water access entitlement upon transformation to protect its right to require security in the future.
5. Under a registered charge, an operator must give its consent to the trade unless the operator concludes, on reasonable grounds, that there is a significant risk that the irrigator may be unable or unwilling to pay future access fees when they fall due.
6. An operator must not require security for the future payment of access fees as a condition of the transformation of an irrigator’s irrigation right.

#### **Form security may take**

7. If an operator seeks security for future payment of fees, the irrigator has the option to offer the operator security over:
  - an unencumbered portion of the irrigator’s water access entitlement, or
  - a bank guarantee, or
  - a cash deposit to be used as a form of bond.
8. If the irrigator offers one of these forms of security, the operator must give due consideration to that offer.
9. In any other case, the operator may accept any other form of security as negotiated between the operator and the irrigator.

#### **Limit on level of security**

10. The value of security should be limited to the greater of:
  - 50 per cent of the value of the termination fee as applied by the operator in accordance with the cap on termination fees provided under the water charge rules; or
  - where an operator does not charge a fee on termination, the value of the annual access fee multiplied by 1.

## **Application and implementation of water market rules**

All operators will need time to implement and give effect to the water market rules. This position paper proposes a transition process to give operators the time needed.

The position paper proposes that all operators will be covered by the water market rules, subject to the provisions of the Act. Implementing arrangements that comply with the water market rules is likely to prove more onerous for small operators who have limited access to resources to help in the transition process. For this reason, and as touched on above, the ACCC will assist irrigation operators by developing standard forms and documents.

The ACCC's preliminary positions on application and implementation of the water market rules are set out in box 5.

### **Box 5: ACCC preliminary positions—application and implementation of the water market rules**

#### **Application**

1. The water market rules should apply to all operators within the MDB, subject to the provisions of the Water Act.

#### **Implementation**

2. Transition to water market rules is proposed to occur according to the following timetable:
  - Stage 1—rules tabled to September 2009—implementation period for operators to amend contracts and other documents. During stage 1 operators must endeavour to ensure that they do not prevent or unreasonably delay transformation and/or trade.
  - Stage 2—September 2009 onwards—full enforceability of the water market rules and a yet-to-be-determined form of monitoring.

#### **Monitoring**

3. The ACCC proposes to keep reporting requirements to a minimum for the purposes of monitoring.
4. The ACCC is developing the water market rules while having regard to the potential monitoring requirements and associated administrative burden on operators.

# 1. Introduction

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

The *Water Act 2007* (the Act), which came into effect on 3 March 2008, 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)<sup>6</sup> and the Murray-Darling Basin Agreement (MDBA).

The Act creates new functions for the Australian Competition and Consumer Commission (ACCC) (see box 6). These include developing draft water market rules and water charge rules for consideration by the Minister for Climate Change and Water and advising the new MDB Authority on water trading rules. The Act also requires the ACCC to monitor compliance with, and enforce<sup>7</sup>, the water market rules and water charge rules.

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 irrigation infrastructure operators do not represent a barrier to trade. In other words, the water market rules will ensure that the water rights of irrigators are tradeable.

On 4 April 2008 the ACCC released an issues paper on the water market rules for consultation. The issues paper invited stakeholders to provide comments on the issues that may be considered by the ACCC and inform the development of the ACCC advice to the minister. A total of 61 written submissions were received and these submissions have informed the preliminary positions presented in this paper.

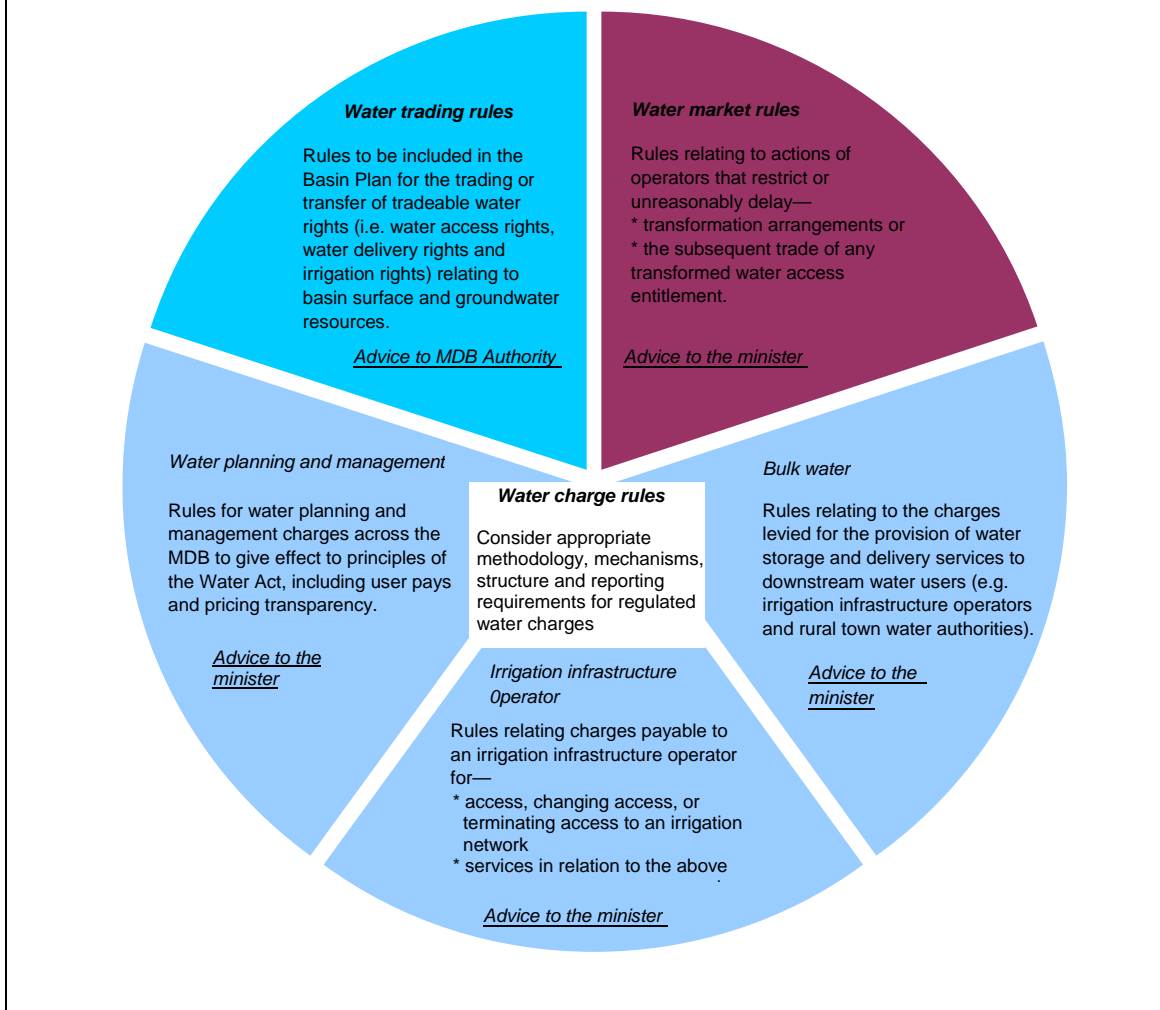
This paper details the ACCC's preliminary positions on the water market rules. The ACCC welcomes submissions on the preliminary positions presented in this paper as well as any other relevant information that could assist and inform its advice to the minister.

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<sup>6</sup> The Intergovernmental Agreement on the National Water Initiative between the Australian Government 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 COAG in 1994, which was incorporated within the National Competition Policy Agreement in 1995.

<sup>7</sup> Part 8 of the Act provides the ACCC with mechanisms to enforce water market rules and water charge rules.

**Box 6: Roles of the ACCC under the Water Act 2007**



**1.1 Consultation process**

Consultation with stakeholders is an important part of the ACCC’s process in developing its advice to the minister. This position paper on the water market rules continues the consultation process that began with the release of the water market rules issues paper.

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, 15 August 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 that will incorporate draft rules and an accompanying draft report in October 2008 for further consultation
- hold public forums with interested stakeholders in October 2008 to discuss the ACCC draft advice

- provide final advice on water market rules to the minister in December 2008.

Submissions provided to the ACCC will be provided in full to the minister as part of the ACCC advice.

## 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 website](#) unless confidentiality is sought and obtained from the ACCC.

Any information that parties would like to request the ACCC not to 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 is not 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 the part of the submission) containing the information. If the submission (or the part of the submission) is withdrawn, the ACCC may not take it into account. If a party elects not to withdraw the submission (or the 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).

## 1.3 What is the role of the 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.<sup>8</sup>

The water market rules must contribute to achieving the basin water market and trading objectives and principles specified in schedule 3 of the Act.

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<sup>8</sup> Explanatory memorandum to the Water Bill 2007, clause 97, paragraph 190, p. 28.

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 arrangement being made or the trade of a transformed water access entitlement.<sup>9</sup>

Broadly speaking, an irrigation infrastructure operator ('operator') is any person<sup>10</sup> who owns or operates infrastructure for the purpose of delivering irrigation water to another person (i.e. an irrigator or other water user).<sup>11</sup> The Act does not distinguish between operators on the basis of the size of the irrigation network, the number of irrigators<sup>12</sup> serviced 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.

⇒ **Water market rules relate to the action or inactions of operators, not all market participants.**

Although many operators, particularly in South Australia and New South Wales, are owned by member irrigators, the operators have separate legal status to their members.

In most cases, these operators own a 'group' water access entitlement<sup>13</sup> and the member irrigators have a right to a share of water under an irrigation right<sup>14</sup> against the operator (as conferred through their supply agreement).

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<sup>15</sup>, thereby reducing the share component of the operator's water access entitlement.

An individual may transform their irrigation right in order to trade the transformed entitlement, or they may 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.

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.

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<sup>9</sup> Water Act, s. 97(1).

<sup>10</sup> 'Person' includes a body politic or corporate as well as an individual.

<sup>11</sup> Water Act, s. 7(4).

<sup>12</sup> 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.

<sup>13</sup> For example, a 'water access licence' in New South Wales and a 'water taking/holding allocation' in South Australia.

<sup>14</sup> Water Act, s. 7(4).

<sup>15</sup> Held by someone other than the operator.

⇒ **Water market rules may limit or prohibit restrictions on transformation imposed by operators**

A transformation arrangement is also a necessary first step if an individual wishes to permanently trade their share of a group entitlement to anybody other than another group member.

The water market rules can consider restrictions that an operator may impose on 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.<sup>16</sup>

⇒ **Water market rules may limit or prohibit restrictions imposed by operators in relation to the trade of a transformed water access entitlement**

This paper will refer to conduct by operators relating to:

- Transformation only—where a person who holds an irrigation right against an operator seeks to obtain a water access entitlement through transformation arrangements.
- Transformation and trade—where a person who holds an irrigation right against an operator seeks to trade or transfer their share of the operator’s water access entitlement or water allocated to this entitlement. This could occur simultaneously with, or subsequent to, a transformation.

For simplicity, these actions will be referred to as ‘transformation and/or trade’.

Restrictions imposed by operators on the trade of irrigation rights by existing irrigation right holders that have not been subject to transformation do not appear to be within the scope of the water market rules. Therefore, the majority of water trading that currently occurs within an operator’s network will not be considered under the water market rules.

⇒ **Water market rules cannot address restrictions imposed on the trade of irrigation rights, such as trade within an operator’s area of operations.**

Similarly, the temporary trade of water allocations associated with untransformed irrigation rights will not be considered under the water market rules. Therefore, many of the more general matters associated with the trade of water allocations (i.e. temporary trade) will extend beyond the scope of the water market rules.

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<sup>16</sup> Water Act, s. 97(3)(b).

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<sup>17</sup>; 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.<sup>18</sup>

The ACCC also has a role in providing advice to the MDB Authority on the water trading rules. As with the water market rules, the water trading rules must contribute to achieving the basin water market and trading objectives and principles specified in schedule 3 of the Act.

Water trading rules are to be included in the Basin Plan and may deal with matters such as the terms, process, manner and restrictions applied to the trade or transfer of water rights. Furthermore, they may deal with market institutional arrangements, including the availability of information to enable trade and the reporting of trade. The application of the water trading rules is likely to be much broader than that of the water market rules and may include state and territory governments and water intermediaries and brokers. Development of water trading rules will be managed through separate consultation processes and are not the subject of this paper.

The ACCC considers that the Act provides sufficient clarity on the scope of the water market rules to suggest that broader trading issues extend beyond the scope of the water market rules. In addition, the water market rules are limited to the actions of operators and any provisions in the water market rules to cover trading matters would not apply as broadly as would be required.

Nevertheless, the ACCC recognises the importance of the broader trading issues, and will consider the existence, nature and extent of any deficiencies in current arrangements in its advice to the MDB Authority on the water trading rules. This could include matters relating to the following issues:

- availability of market information
- registers and accounts
- interaction between operators and intermediaries.

The water market rules issues paper noted that the process of transforming an irrigation right into a water access entitlement may have tax implications for both operators and irrigators. The ACCC has informed the Australian Tax Office of the potential tax implications associated with transformation and does not intend to comment on this matter any further at this stage.

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<sup>17</sup> Water Act, s. 97(6)(a). Regulated water charge is defined in s. 91 of the Act.

<sup>18</sup> Water Act, s. 97(6)(b).

## 2. Facilitating transformation and/or trade

As the owner of the group water access entitlement, an operator can unilaterally prevent or delay any member from transforming their share of the group entitlement into a separate water access entitlement.

Some submissions pointed to actions or inactions of operators that could be considered to delay or prevent trade. For example, the Ricegrowers' Association of Australia identified an operator who requires a full member meeting to approve an annual trade.<sup>19</sup> Another stakeholder commented on the subjective and discretionary policies, reflected in the terms and conditions administered by operators. It was submitted that these arrangements confer too much discretion on the operator to approve transfers and trades.<sup>20</sup> Other submissions considered that operators should not be able to unreasonably refuse to sign documentation that enables such sales or prevent these sales in other ways.<sup>21</sup>

One irrigator estimated that his inability to gain access to his irrigation right has resulted in an ongoing 10-year legal battle with the operator and has cost more than \$150 000.<sup>22</sup>

The ACCC proposes establishing an obligation on operators to assist individual irrigators in transforming and/or trading their transformed entitlements in the water market rules.

An operator must do all things necessary to facilitate transformation and/or trade of all or part of an irrigator's entitlement in accordance with the water market rules.

An operator must not prevent or unreasonably delay transformation of all or part of an irrigator's entitlement under any circumstances, other than in accordance with the water market rules.

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<sup>19</sup> Ricegrowers' Association of Australia, submission 26, p. 5.

<sup>20</sup> Mr Ian Shippen, submission 41, p. 1.

<sup>21</sup> P J and P B Goudie, submission 8, pp. 2–4; Mr Thomas McCallum, submission 4, p. 1.

<sup>22</sup> P J and P B Goudie, submission 8, p. 3.



### **3. Operators' terms and conditions for approving transformation and/or trade**

The terms and conditions governing an operator's approval processes for transformation and/or trade may be contained in its supply agreements with irrigators.<sup>23</sup> Otherwise the supply agreement may point to separately documented policies or the terms and conditions associated with transformation and/or trade may not be documented at all.

An operator's terms and conditions for transformation and/or trade approval may typically include:

- details of the operator's approval process
- matters the operator considers in assessing the application
- obligations of the parties involved in the transaction
- any administrative fees associated with the application.

Clearly defined, transparent terms and conditions for transformation and/or trade support these outcomes by protecting property rights and reducing transaction costs.

#### **3.1 Submissions by stakeholders**

##### **3.1.1 Clearly stated terms and conditions**

A number of stakeholders commented that policies to support transformation and/or trade varied considerably between operators.<sup>24</sup> In addition, some stakeholders submitted that these terms and conditions should be comprehensive, clear and unambiguous, and that where they are not, this may create confusion, introduce market distortions and result in a lower level of transformation and trading activity.<sup>25</sup>

Smaller operators were identified as having fewer prescribed terms and conditions for transformation and/or trade than larger operators.<sup>26</sup> This appears consistent with the

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<sup>23</sup> An operator's supply agreement with irrigators could be defined in the arrangements governing the shareholder/trustee relationship (where an operator's shareholders are also their customers) and/or the arrangements governing the ownership of the share of the water entitlement.

<sup>24</sup> Waterexchange, submission 46, p. 7; National Farmers Federation, submission 41, p. 9; Sunraysia Citrus Growers, submission 17, p. 4; Mourquong Co-operative, submission 14, p. 4.

<sup>25</sup> Renmark Irrigation Trust, submission 47, p. 2; West Corrgan Board of Management, submission 50, p. 3; National Farmers Federation, submission 41, p. 9; Minerals Council of Australia, submission 39, p. 8; State Government of Victoria, submission 61, p. 6; Water for Rivers, submission 51, p. 7; New South Wales Irrigators' Council, submission 31, p. 6.

<sup>26</sup> Sunraysia Citrus Growers, submission 17, p. 5.

views of a number of stakeholders that many smaller operators do not provide transformation and trading information and do not allow trading at all.<sup>27</sup>

Some stakeholders suggested that a model contract or minimum set of standards should be developed or mandated, and should require operators to define and provide clear and comprehensive processes, terms and conditions, and arrangements for transformation and/or trade.<sup>28</sup>

### **3.1.2 Transparency and accessibility**

Several stakeholders recommended that terms and conditions for transformation and/or trade should be fully disclosed and readily available to external parties and operator customers.<sup>29</sup> Submissions noted that where possible these terms should remain relatively stable over time<sup>30</sup>, and that enhanced communication and knowledge of terms and conditions for transformation and/or trade would enable efficient trading because irrigators could make better informed trading decisions.<sup>31</sup>

In regard to current practice, stakeholders noted that terms are located in a variety of documents, which vary from operator to operator and are generally not clearly specified or communicated. Similarly, the means by which these documents are distributed, publicised or made accessible may vary.<sup>32</sup> Another stakeholder considered that the complexity created by these arrangements results in increased transaction costs and can lead to lower rates of transformation.<sup>33</sup>

### **3.1.3 Process for changing terms and conditions**

Some stakeholders noted that while policies should not constantly change, they should have the ability to unilaterally vary the terms and conditions to ensure they keep pace with legislative and commercial realities and company objectives.<sup>34</sup>

Several stakeholders noted that board members or directors are elected by members and are responsible for setting policy, which means that member approval is not generally required.<sup>35</sup> Murray Irrigation Limited noted that while policy is initially endorsed by its

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<sup>27</sup> Water for Rivers, submission 51, p. 2; Mourquong Co-operative, submission 14, p. 4; National Farmers' Federation, submission 41, p. 9.

<sup>28</sup> South Australian Farmers Federation, submission 42, p. 5; Minerals Council of Australia, submission 39, p. 8.

<sup>29</sup> Murray Irrigation Limited, submission 40, p. 32; Murray-Darling Basin Commission, submission 59, p. 2; Water for Rivers, submission 51, p. 7; Murrumbidgee Irrigation, submission 44, p. 6; PJ and P B Goudie, submission 8, pp. 1, 4.

<sup>30</sup> D W Sehestedt, submission 5, p. 1.

<sup>31</sup> Minerals Council of Australia, submission 39, p. 8.

<sup>32</sup> P J and P B Goudie, submission 8, p. 1; Waterexchange, submission 46, p. 7.

<sup>33</sup> State Government of Victoria, submission 61, p. 6.

<sup>34</sup> Murray Irrigation Limited, submission 40, p. ii; Western Murray Irrigation, submission 11, pp. 30–33; Narromine Irrigation Board of Management, submission 33, p. 10; Murrumbidgee Irrigation, submission 44, p. 6; Water for Rivers, submission 51, p. 7.

<sup>35</sup> Narromine Irrigation Board of Management, submission 33, p. 10; Western Murray Irrigation, submission 11, p. 32; Mourquong Co-operative, submission 14, p. 4; Sunraysia Citrus Growers, submission 17, p. 4.

board, where required it seeks ratification by a general meeting of shareholders before the policy is adopted in operating procedures and put into practice.<sup>36</sup>

However, one stakeholder noted that Murray Irrigation Limited's:

rules and the way they continually change them is having a detrimental impact on my business ... and have eroded my property right.<sup>37</sup>

Water for Rivers suggested that there should be a process of review by the ACCC:

where any party can bring forward an operator rule deemed to be non-competitive or against open and free trade for determination and appropriate ... action.<sup>38</sup>

Alternatively, one stakeholder suggested operators should consult with its member irrigators before amending its terms of trade<sup>39</sup>, and another suggested the operator must be accountable to members for such changes.<sup>40</sup>

## 3.2 Preliminary position

Under-developed or inadequate terms and conditions to support the transformation and/or trade of water entitlements are likely to result in increased uncertainty, higher transaction costs for irrigators and constitute a barrier to transformation and/or trade.

Accordingly, operators should have policies in place to support transformation and/or trade. While operators face resource constraints, any imposed administrative burden will not be ongoing.

To the extent that terms and conditions exist, they appear in a range of documents, which are then publicised in different forms. In the interests of promoting transparency, accessibility and informed decision-making by irrigators, there is merit in a more rationalised and simple format.

Operators should ensure that the terms and conditions are set out in a straightforward manner. This document should be published on the operator's website or otherwise made readily available, and operators should notify their customers of the existence of the document.

While terms and conditions need to be sufficiently flexible to ensure they remain relevant over time, the frequency and nature of changes can be problematic.

Many of these changes may be required to reflect changing legislative requirements; however, it appears that changes may also have been made to the terms and conditions for transformation and/or trade simply to protect the commercial interests of operators

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<sup>36</sup> Murray Irrigation Limited, submission 40, p. iii.

<sup>37</sup> Mr Ian Shippen, submission 36, p. 1.

<sup>38</sup> Water for Rivers, submission 51, p. 7.

<sup>39</sup> D W Sehestedt, submission 5, p. 1.

<sup>40</sup> Murrumbidgee Irrigation, submission 44, p. 6.

and residual members. This could be at the expense of an individual irrigator and the interests of MDB stakeholders more broadly.

Operators should consult with affected parties about any change to terms and conditions for transformation and/or trade that may materially affect them. For changes that are more administrative in nature and are unlikely to materially impact irrigators, the operator should still be required to inform its members.

As part of developing the water market rules, the ACCC will consider whether it is appropriate to provide guidance to operators about the circumstances and processes for changing terms and conditions.

Operators should have in place clearly stated terms and conditions to facilitate transformation and/or trade.

The terms and conditions relating to transformation and/or trade approvals should:

- be readily available to all parties and rationalised where possible
- be published on the operator's website (if applicable) and customers of the operator should be notified in writing of the existence of these documents.

Operators should clearly define and document the process associated with making any required changes to the terms and conditions relating to transformation and/or trade approvals (the ACCC may also provide guidance to operators on the appropriateness of the process undertaken to implement such changes).

Operators **must consult** with irrigators who may be materially affected by a change to the terms and conditions (the ACCC may also provide guidance to operators on what could be considered 'material').

Operators **must notify** irrigators of all changes to their terms and conditions.

In consulting with or notifying irrigators, operators should outline the reasons for the proposed change and supply supporting documentation if applicable.

At the completion of the transitory adjustment period of the water market rules (date TBC), an operator must notify all its irrigators in writing of the application of the water market rules; specifically, an information pack that includes a copy of the water market rules and applicable transformation application forms should be provided to irrigators.

## 4. Transformation and/or trade administrative process

As noted in chapter 3, an operator's terms and conditions for transformation and/or trade may include details about the operator's administrative processes for transformation and/or trade.

In general a transformation and/or trade administrative process would involve:

- An irrigator applying to their operator to transform and/or trade their irrigation rights, typically by completing the relevant application forms.
- Approval by the operator of the transformation and/or trade of the irrigation right. In considering applications, the operator will consider compliance of the application with provisions contained in the terms and conditions governing approval.
- The operator applying on behalf of the irrigator to the relevant state department for the transformation and/or trade of the irrigator's share of the operator's water access entitlement.
- Approval by the relevant state department.
- Updating the operator's irrigation right register and, where applicable, renegotiating any ongoing delivery arrangements.

An operator is involved in all but one stage of this process—approval by the relevant state department.

A lack of clearly defined, comprehensive and efficient administrative processes may prevent or unreasonably delay the transformation and/or trade of an individual's irrigation right. Specific actions may be required of an operator in processing an application for transformation and/or trade of an irrigation right.

Providing irrigators with information about the application and approval processes can reduce transaction costs and facilitate the operation of efficient markets.

The practice of transformation is not often performed as a separate process and stakeholder submissions primarily relate to trading processes; however, the transformation process should be similar.

## 4.1 Application process

### 4.1.1 Submissions by stakeholders

Western Murray Irrigation, Murray Irrigation Limited and Murrumbidgee Irrigation all advised that their procedures for processing applications for transformation and/or trade closely reflect those set out in on p. 26 of the water market rules issues paper.<sup>41</sup>

Many submissions supported standardising application forms for transformation and/or trade.<sup>42</sup> This would help to facilitate trade by reducing transaction costs, creating a more streamlined service<sup>43</sup> and allowing dealings between individual irrigators and operators and between operators and operators to become easier.<sup>44</sup> It was also suggested that standardised forms may assist licensed brokers to provide a cost-effective service across Australia.<sup>45</sup>

Some submissions noted that if standardised forms for transformation and/or trade were developed, these would need to be sound, include all relevant information and be agreed to by the operators<sup>46</sup>, and that the approach should be in line with the land titles registry requirements.<sup>47</sup>

Stakeholders also pointed out potential issues with the use of standardised application forms, including the difficulty in developing them because of differences in the class and deliverability of water<sup>48</sup> and jurisdictional requirements.<sup>49</sup>

### 4.1.2 Information required by operators

Many stakeholders made submissions on the contents of application forms when a standardised approach is applied. For permanent trade, several operators advised that they required the following minimum information:

Murray Irrigation Ltd—

- details of the vendor and purchaser
- the volume to be traded
- original water entitlement certificates

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<sup>41</sup> Western Murray Irrigation, submission 11, p. 34; Murray Irrigation Limited, submission 40, p. 34; Murrumbidgee Irrigation, submission 44, p. 7.

<sup>42</sup> Western Murray Irrigation submission 11, p. 35; Queensland Bulk Water Supply Authority, submission 15, p. 4; Ricegrowers Association of Australia, submission 26, p. 6; Murray Irrigation Limited, submission 40, p. 35; West Corurgan, submission 50, p. 4; Macquarie River Food and Fibre, submission 53, p. 14.

<sup>43</sup> National Farmers' Federation, submission 41, p. 10.

<sup>44</sup> Murray Irrigation Limited, submission 40, p. 35.

<sup>45</sup> Ricegrowers Association of Australia, submission 26, p. 6.

<sup>46</sup> Western Murray Irrigation submission 11, p. 35.

<sup>47</sup> Macquarie River Food and Fibre, submission 53, p. 14.

<sup>48</sup> Waterexchange, submission 46, p. 7.

<sup>49</sup> Murrumbidgee Irrigation, submission 44, p. 7.

- land title searches and affirmation of encumbrances (where applicable)
- transfer stamped by the Office of State Revenue when stamp duty is due.<sup>50</sup>

Western Murray Irrigation—

- confirmation of ownership
- the original signatures of all owners
- no outstanding debts with the operator
- approval from third party interests.<sup>51</sup>

Murrumbidgee Irrigation—

- complete description of what the applicant proposes
- the current status of the water entitlement
- completed application forms.<sup>52</sup>

West Corurgan Board of Management—

- third party consent.<sup>53</sup>

#### **4.1.3 Information required by applicants**

To properly complete an application for transformation and/or trade, the applicant also requires certain information from the operator, which may not currently be readily available.<sup>54</sup> Stakeholders considered this could include a clear proof of title, volume of allocations (current and future)<sup>55</sup>, rules of transformation and/or trade, the operator's assessment of any breaches of those rules, processes that must be completed and forms that must be provided.<sup>56</sup>

Several stakeholders noted some of this information is currently made available to irrigators on request, either free<sup>57</sup> or at charge<sup>58</sup>, while other operators issue a certificate containing some of this information.<sup>59</sup>

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<sup>50</sup> Murray Irrigation Limited, submission 40, p. 35.

<sup>51</sup> Western Murray Irrigation, submission 11, p. 35.

<sup>52</sup> Murrumbidgee Irrigation, submission 44, p. 7.

<sup>53</sup> West Corurgan, submission 50, p. 4.

<sup>54</sup> Waterexchange, submission 46, p. 7.

<sup>55</sup> Waterexchange, submission 46, p. 7.

<sup>56</sup> Murrumbidgee Irrigation, submission 44, p. 7.

<sup>57</sup> Western Murray Irrigation, submission 11, p. 35.

<sup>58</sup> Murray Irrigation Limited, submission 40, p. 34.

<sup>59</sup> Jemalong Irrigation Limited currently issues a certificate to its members specifying the shares held (and the payment details related to those shares) and the corresponding water entitlements in accordance with its articles of association.

#### **4.1.4 Preliminary position**

The approval processes for transformation and/or trade appear to differ from operator to operator. Streamlining these processes would benefit all participants and would facilitate efficient water markets.

The standardisation of application forms would provide for a more consistent and simple process, reducing processing times and transaction costs, thereby facilitating transformation and/or trade.

However, different jurisdictional requirements need to be considered. The ACCC proposes that a base set of forms be developed for the process of transformation and/or trade based on the varying state obligations and requirements. It is not proposed that these standardised forms would be included as part of the market rules, rather that they would be circulated as guidelines during the implementation of the market rules.

It appears that much of the information requested by operators is not necessary for the successful processing of applications for transformation and/or trade. Restricting the type of information sought by operators would reduce the burden placed on applicants in ensuring that they have submitted a complete application. It would also benefit operators by reducing paperwork and simplifying the verification process. The use of standard forms may assist in this regard.

The basic information required for a transformation and/or trade application is described below. Unnecessary information—such as details about the applicant’s reasons for transformation and/or trade—should not be required by an operator.

To confirm the minimum information required, the ACCC requires more information about the specific requirements of the various state and territory authorities.

Information necessary for applicants to properly complete an application for transformation and/or trade should be readily obtainable from operators on request.

Operators must develop a base set of forms for both transformation applications and transformation and trade applications. The basic information required for both processes may include:

- applicant details
- account number
- confirmation of identity
- the number and type of units/volume to be transformed
- confirmation that all fees have been paid.

For transformation and trade, additional information may also include:

- buyer details including details of any existing water access entitlement for the transformed units to be appended to.
- the number and type of units/volume of water to be traded.

An operator must not request from applicants details relating to the purpose for transformation and/or trade.

An operator must make information regarding the applicant's water right readily available upon request and within a reasonable time frame.

## 4.2 Timeliness of process

### 4.2.1 Submissions by stakeholders

A number of submissions highlighted the importance of timeliness in the transformation and/or trade of water. Administrative procedures will necessarily take time in order to ensure the integrity of a water register.<sup>60</sup> However, it was submitted that quite often approval processes are not undertaken in an efficient manner<sup>61</sup> and there is often an urgent need for water, with extended delays threatening crops and livestock.<sup>62</sup> It was also noted that processing delays by operators have eroded confidence in the market, hindering the development of more diverse water products.<sup>63</sup>

Stakeholders provided various examples of the sort of delays experienced in the processing of trades. Citrus Growers of South Australia stated that while payment is made upfront or within 48 hours, some irrigators have had to wait up to 60 days for

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<sup>60</sup> Murray Irrigation Limited, submission 40, p. 36.

<sup>61</sup> Murrumbidgee Irrigation, submission 44, p. 8.

<sup>62</sup> Murrumbidgee Private Irrigators, submission 3, p. 3; United Dairy Farmers of Victoria, submission 29, p. 3.

<sup>63</sup> Waterexchange, submission 46, p. 3.

confirmation of a trade.<sup>64</sup> In a specific example, it took two years to complete a single water trade.<sup>65</sup>

Many operators submitted that trades of water allocations are generally processed within one to two business days<sup>66</sup> because there is often an urgent need for water and the administration process is less onerous.<sup>67</sup>

Submissions highlighted that water transformations and water entitlement trades are more complex, which means that an appropriate level of care needs to be taken and approval times vary.<sup>68</sup> Submissions suggested timeframes for approval of permanent trade ranged from 10 to 15 days<sup>69</sup>, to three weeks<sup>70</sup> and up to three months.<sup>71</sup>

It was suggested that timeframes should be structured in a manner similar to those for land transactions<sup>72</sup> or resemble the Australian Stock Exchange (ASX) standard settlement time of three days.<sup>73</sup>

Murrumbidgee Irrigation submitted that it and most other operators in New South Wales have regularly ranked highly in terms of trade processing speed.<sup>74</sup> The South Australia Farmers' Federation also noted that unbundling of water rights is expected to address current delays of trade into South Australia because of jurisdictional requirements that prohibit trade until salinity and drainage assessment is complete.<sup>75</sup>

A large number of the submissions received supported the imposition of time limits for processing transformation and trade applications to improve efficiency and reduce transaction costs.<sup>76</sup>

However, one stakeholder suggested that it may not always be possible to adhere to strict time limits.<sup>77</sup> In addition, the prescription of time limits could act to slow average

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<sup>64</sup> Citrus Growers of South Australia, submission 16, p. 1.

<sup>65</sup> Minerals Council of Australia, submission 39, p. 9. See also Water for Rivers, submission 51, p. 8; Waterexchange, submission 45, p. 3.

<sup>66</sup> Western Murray Irrigation, submission 11, p. 36 (48 hours); Murray Irrigation Limited, submission 40, p. 36 (one business day).

<sup>67</sup> Murray Irrigation Limited noted that it does not require board approval for temporary trades, with only simple checks of the application being undertaken. See further Murray Irrigation Limited, submission 40, p. 35.

<sup>68</sup> Bondi Group, submission 32, p. 15.

<sup>69</sup> Queensland Farmers Federation and Queensland Irrigators Council, submission 58, p. 6.

<sup>70</sup> Western Murray Irrigation, submission 11, p. 36.

<sup>71</sup> Waterexchange, submission 46, p. 3.

<sup>72</sup> Australian Bankers' Association, submission 25, p. 10; Macquarie River Food and Fibre, submission 53, p. 14.

<sup>73</sup> Waterfind, submission 57, p. 2; Bondi Group, submission 32, p. 15.

<sup>74</sup> Murrumbidgee Irrigation, submission 44, p. 7.

<sup>75</sup> South Australia Farmers' Federation, submission 42, p. 4.

<sup>76</sup> Queensland Bulk Water Supply Authority, submission 15, p. 5; Western Murray Irrigation, submission 11, p. 36; Victorian Farmers' Federation, submission 54, p. 10. See also Goulburn Broken Catchment Management Authority, submission 12, p. 2. Ricegrowers Association of Australia, submission 26, p. 6; New South Wales Irrigators' Council, submission 31, p. 9; National Farmers' Federation, submission 41, p. 10;

processing times because ‘the lowest common denominator would be adopted.’<sup>78</sup> Murrumbidgee Irrigation acknowledged this issue; however, it noted that ‘operators can and currently do significantly exceed such benchmarks’, and also suggested that time limits could be reviewed and subsequently reduced.<sup>79</sup> Some stakeholders suggested time limits should consider operators’ limited resources<sup>80</sup>, size and the number of applications received.<sup>81</sup>

It was noted that in some jurisdictions approval is also required by the relevant state authority. Western Murray Irrigation stated that any trades out of its district would involve a reduction in its licence, and the New South Wales Department of Water and Energy would thus be required to complete the process.<sup>82</sup>

Several submissions stated that delays in processing times are generally because of the actions of government agencies and the seller and buyer, not the private sector.<sup>83</sup>

Stakeholders generally agreed that timeframes for processing transformations and trades should commence upon the lodgement of a correctly completed application form.<sup>84</sup> The point at which the time frame should conclude is less clear. A number of suggestions were provided including when the legal transfer documents are delivered to relevant parties and any transaction costs and termination fees paid<sup>85</sup>; when all fees have been received and the operator’s register has been updated<sup>86</sup>; and when final approval has been obtained from the relevant government agency.<sup>87</sup>

Submissions noted that information on processing times is not generally provided to market participants.<sup>88</sup> However, Western Murray Irrigation noted that some water exchanges attempt to track approval time<sup>89</sup>, and there was some support for operators monitoring and reporting on timeframes.<sup>90</sup>

Some operators require final board approval before finalising water entitlement trades.<sup>91</sup> In other instances, approval has been delegated, either to management or the chief

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<sup>77</sup> Western Murray Irrigation, submission 11, p. 36.

<sup>78</sup> Waterexchange, submission 46, p. 8.

<sup>79</sup> Murrumbidgee Irrigation, submission 44, p. 8.

<sup>80</sup> Murray-Darling Basin Commission, submission 59, p. 2.

<sup>81</sup> Western Murray Irrigation, submission 11, p. 36.

<sup>82</sup> Western Murray Irrigation, submission 11, p. 34.

<sup>83</sup> Bondi Group, submission 32, p. 15; West Corugan Board of Management, submission 50, p. 4; Macquarie River Food and Fibre, submission 53, p. 9; Murray Irrigation Limited, submission 40, p. 36.

<sup>84</sup> Macquarie River Food and Fibre, submission 53, p. 14; Western Murray Irrigation, submission 11, p. 36; West Corugan Board of Management, submission 50, p. 4.

<sup>85</sup> Macquarie River Food and Fibre, submission 53, p. 14.

<sup>86</sup> Western Murray Irrigation, submission 11, p. 36.

<sup>87</sup> West Corugan, submission 50, p. 4.

<sup>88</sup> Waterexchange, submission 46, p. 9; Western Murray Irrigation, submission 11, p. 37.

<sup>89</sup> Western Murray Irrigation, submission 11, p. 37.

<sup>90</sup> New South Wales Irrigators Council, submission 31, p. 9; Murrumbidgee Irrigation, submission 44, p. 8.

<sup>91</sup> Western Murray Irrigation, submission 11, p. 34; Murray Irrigation Limited, submission 40, p. 35.

executive officer <sup>92</sup> or another senior executive.<sup>93</sup> The Bondi Group supported the notion of board approval for all large permanent trades.<sup>94</sup>

While one stakeholder noted that requiring board approval politicises the process, acting as a lever to control water movement<sup>95</sup>, others submitted that board approval ensures that no company rules are breached and enables the endorsement of the record in the water registers.<sup>96</sup>

## 4.2.2 Preliminary position

### Time limits

At present, the time taken by operators to process and give effect to transformation and/or trade approvals varies significantly. This process may be inefficient in some instances.

Currently, no prescribed time limits exist. Implementing binding time lines for transformation and/or trade processes would benefit all market participants because it would improve efficiency in the market and lower transaction costs associated with the process. While the time limits imposed should take account of what is considered to be best practice, they should also be practical and cost-effective.

Concerns were raised about the ability of some operators to meet strict time limits because of their lack of administrative resources and protocols or other unforeseen occurrences. However, by establishing clear and comprehensive procedures for transformation and/or trade—such as standardising application forms, streamlining processes and defining information requirements of operators—many delays would appear to be avoidable.

While any universal time limits applied may be longer than the processing time currently being achieved by some operators, it is unlikely that this will cause efficient operators to reduce their efficiency or to change their current practices. Time limits will pull the less efficient operators into line with the more efficient. To encourage efficiency in the approval process, time limits could be subject to periodic review.

Western Murray Irrigation considered that, when determining applicable time limits, consideration should be given to the size of the operator and the number of applications. However, there is a strong argument that all operators should be subject to the same approval time limits. Whilst larger operators may be required to process a larger volume of applications, they are more likely to have better resources and administration practices in place than smaller operators. Conversely, while not having the same resources as a larger operator, a smaller operator would have fewer applications. Standardised application forms would also assist small operators in this matter.

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<sup>92</sup> Murrumbidgee Irrigation, submission 44, p. 8.

<sup>93</sup> Western Murray Irrigation, submission 11, p. 34; Murray Irrigation Limited, submission 40, p. 35.

<sup>94</sup> Bondi Group, submission 32, p. 14.

<sup>95</sup> Waterexchange, submission 46, p. 7.

<sup>96</sup> Murray Irrigation Limited, submission 40, p. 35.

The approval process for transformation and/or trade generally consists of a number of steps, some of which rely on the actions of third parties, such as government. For this reason, separate time limits have been established for three distinct components of the approval process that involve action only by the operator. Time taken by any applicable third party involved in the approval process has not been included in the time limits proposed.

### **Board approval**

In addition to the initial information requirements and procedures regarding the application process, transformation and/or trade of a water entitlement may be subject to final approval by a board or senior executive. The practice of requiring board approval varies among operators. Requiring board approval can draw out transformation and/or trade approval processes.

The ACCC has refrained from prescribing a specific approval procedure for operators to follow for parties that may approve transformation and/or trade. Operators will be free to determine whether board approval is a necessary step in their approval processes. However, the prescribed time limits must be adhered to irrespective of the approval process adopted by the operator.

Operators must process applications efficiently and not unduly delay the approval process.

Time limits for operators processing transformation and/or trade applications are as follows:

- Initial assessment period—upon lodgement of an application, the operator must ensure that the application has been properly completed and request further details as required within three business days.
- Approval period—upon acceptance of a correctly completed application, the operator must process the application within 10 business days, including completion of the following steps:
  - processing and checking of the application
  - final approval by the operator
  - advising the applicant of the status of the application.
- Referral of application to the relevant jurisdictional authority for further approval (where applicable).
- Updating the register—once the operator has been advised of the final approval, it must ensure that the relevant register has been updated within two business days.

These time limits do not include any time taken by the relevant jurisdictional authorities in approving a transformation and/or trade.

These time limits apply irrespective of an operator's approval procedure or the size of the operator.

## 4.3 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 transaction costs and therefore impede the operation of water markets.

### 4.3.1 Submissions by stakeholders

Two stakeholders commented on the negative impact high administration fees and charges may have on market liquidity.<sup>97</sup> Another submission noted that changes in government policy positions increase administrative costs, therefore increasing administrative fees and charges.<sup>98</sup>

A number of stakeholders considered their current administrative fees and charges to be minimal<sup>99</sup> and generally reflective of costs associated with providing transformation and/or trade transaction services.<sup>100</sup> Others noted that in comparison to the value of a water transaction, administrative fees were negligible.<sup>101</sup> Murray Irrigation Limited stated that its fees are transaction-based rather than unit-based, and that it does not charge fees for annual transfers or for the use of its exchange, as these are both considered to be core services.<sup>102</sup>

In contrast, the Australian Water Brokers Association considered that the level of fees and charges is not in line with administrative costs, citing large differences in fees between operators as evidence of this.<sup>103</sup>

#### The basis of fees and charges

The majority of submissions were of the view that that administrative fees and charges for processing a transformation and/or trade should be based on cost recovery.<sup>104</sup>

While one stakeholder supported a prescriptive approach<sup>105</sup>, the general view was that prescribed fees may not be appropriate because of the market structure and range of

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<sup>97</sup> Waterfind, submission 57, p. 4; Australian Conservation Foundation, submission 23, pp. 9–10.

<sup>98</sup> Bondi Group, submission 32, p. 12.

<sup>99</sup> Murrumbidgee Irrigation, submission 44, p. 6; Macquarie River Food and Fibre, submission 53, p. 12; West Corugan, submission 50, p. 3.

<sup>100</sup> Western Murray Irrigation, submission 11, p. 13; Murray Irrigation Limited, submission 40, p. 30; Murrumbidgee Irrigation, submission 44, p. 6; Macquarie River Food and Fibre, submission 53, p. 12.

<sup>101</sup> Bondi Group, submission 32, p. 12; Western Murray Irrigation submission 11, p. 28.

<sup>102</sup> Murray Irrigation Limited, submission 40, p. 29.

<sup>103</sup> Australian Water Brokers Association, submission 24, p. 10.

<sup>104</sup> Australian Water Brokers Association, submission 24, p. 10; Western Murray Irrigation, submission 11, pp. 27–28; Mourquong Co-operative, submission 14, p. 4; Queensland Bulk Water Supply Authority, submission 15, p. 4; Australian Conservation Foundation, submission 23, p. 16; National Farmers' Federation, submission 41, p. 8; West Corugan Board of Management, submission 50, p. 3; Macquarie River Food and Fibre, submission 53, p. 12; Murray-Darling Basin Commission, submission 59, p. 2; Australian Conservation Foundation, submission 23, pp. 9–10.

<sup>105</sup> Thomas McCallum, submission 4, p. 1.

different cost structures that exist for operators.<sup>106</sup> Similarly, the New South Wales Irrigators Council considered that prescribing fees and charges is beyond the scope of the ACCC's role.<sup>107</sup> The Minerals Council of Australia advised the ACCC to exercise caution in developing water market rules in this area to avoid unnecessary cost implications.<sup>108</sup>

The Queensland Bulk Water Supply Authority supported an approach whereby the seller would bear the administrative costs associated with the trade process on the basis that the beneficiaries of a trade should 'bear the full cost of supporting their market and this shouldn't be borne by customers who don't access the market.'<sup>109</sup>

However, this view was not supported by the National Farmers' Federation (NFF). The NFF were of the view that irrigators should not be required to pay for the use of 'antiquated and labour intensive trade processes', and suggested that water trades should be facilitated by electronic exchanges.<sup>110</sup>

The Murray-Darling Basin Commission suggested that administrative fees and charges should be reviewed regularly 'against an agreed set of best practice standards'.<sup>111</sup>

The Ricegrowers' Association of Australia submitted that government and operator charges should be standardised across all jurisdictions, with the relevant information being made available on the internet.<sup>112</sup>

A number of suggestions were offered for reducing transaction costs associated with transformation and/or trade. These include electronic service delivery<sup>113</sup> and the implementation of a national registry.<sup>114</sup>

#### **4.3.2 Preliminary position**

The processes to facilitate transformation and/or trade require operators to use internal resources. Operators should be reimbursed for this activity.

Administrative fees and charges should be based solely on the recovery of costs. Fees and charges in excess of the cost of service provision are not appropriate and give rise to inefficient transformation and/or trading outcomes.

The principle of cost recovery should preclude an operator from imposing fees and charges for administrative processes for which it has already been compensated by a government agency.

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<sup>106</sup> Mourquong Co-operative, submission 14, p. 4. See also Bondi Group, submission 32, p. 12.

<sup>107</sup> NSW Irrigators' Council, submission 31, p. 8.

<sup>108</sup> Minerals Council of Australia, submission 39, p. 4.

<sup>109</sup> Queensland Bulk Water Supply Authority, submission 15, p. 4.

<sup>110</sup> National Farmers' Federation, submission 41, p. 8.

<sup>111</sup> Murray-Darling Basin Commission, submission 59, p. 2.

<sup>112</sup> Ricegrowers' Association of Australia, submission 26, p. 4.

<sup>113</sup> New South Wales Farmers Association, submission 60, p. 3.

<sup>114</sup> Australian Property Institute, submission 37, p. 3.

Operators are best placed to set administration fees and charges that recover costs, not increase profits.

Operators should provide information to irrigators regarding any applicable administrative charges associated with processing transformation and/or trade arrangements to better inform irrigators' decisions concerning transformation.

Any administrative fees and charges for processing a transformation and/or trade must be based on cost recovery.

Any administrative fees for processing a transformation and/or trade must be contained within an operator's terms and conditions for transformation and/or trade.

## 5. Enabling transformation separate to trade

Currently, many irrigators own a right to water through shares in their operator's group water entitlement. Irrigators may wish to hold the right to water directly, without necessarily trading their water. This process of transforming shares of a group entitlement into individually held entitlements can be accomplished separately to trading that water.

In its own right, transformation produces a number of benefits, including more clearly defined, independent statutory rights to water, improved mortgageability and streamlined future trade. However, operators may be concerned about the increased administrative burden of allowing transformation, and irrigators may be concerned about accessing a fair delivery contract if they choose to continue irrigating after transformation. This chapter contains some preliminary views on these issues.

### 5.1 Benefits of transformation

#### 5.1.1 Submissions by stakeholders

##### Clearly defined water rights

Several stakeholders supported the transformation of irrigation rights into separately held water access entitlements<sup>115</sup> and submitted that operators should not be allowed to prevent transformation.<sup>116</sup> Transformation would develop a deeper, more flexible and transparent market better able to respond to the circumstances of individual businesses<sup>117</sup> and forms:

the basis of a robust and transparent set of rights that would provide clarity to water users and ensure that the potential gains from water trade are realized.<sup>118</sup>

However, the Ricegrowers Association of Australia submitted that transformation should not enable irrigators to avoid charges that faced by remaining members.<sup>119</sup>

##### Mortgageability

Several stakeholders confirmed that while finance is achievable under a group entitlement, it is more difficult and costly to obtain.<sup>120</sup>

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<sup>115</sup> PJ and PB Goudie, submission 8, pp. 3–4; Ricegrowers' Association of Australia, submission 26, p. 6; Minerals Council of Australia submission 39, pp. 3, 9; National Farmers' Federation, submission 41, p. 10.

<sup>116</sup> PJ and PB Goudie, submission 8, p. 3.

<sup>117</sup> Minerals Council of Australia, submission 39, p. 3.

<sup>118</sup> Victorian Farmers' Federation, submission 54, p. 9.

<sup>119</sup> Ricegrowers' Association of Australia, submission 26, p. 6.

<sup>120</sup> P J and P B Goudie, submission 8, p. 3; Mourquong Co-operative, submission 14, p. 5; Sunraysia Citrus Growers, submission 17, p. 6; Australian Bankers' Association, submission 25, p. 11.

The Australian Banker's Association submitted that untransformed group entitlements do not afford the equivalent protection to financiers when compared with individually held statutory water access entitlements.<sup>121</sup> Group entitlements are subject to operators rules, which can change often and without notice. Some operators rules do not recognise a financier's interests, do not recognise multiple financial interests or give their own financial interests against the irrigator priority over those of financiers.<sup>122</sup> However, the Australian Banker's Association submitted that it should not be left to financial institutions to move the reform process forward by requiring transformed rights as security.<sup>123</sup>

The National Farmers' Federation submitted that water reform was eroding the perceptions of security of group property rights over time in favour of individually held rights.<sup>124</sup> The Narromine Irrigation Board of Management also anticipated that financial institutions will increasingly require individual water entitlements as security and will be less likely to rely on informal arrangements with operators (such as correspondence only)<sup>125</sup>

Pioneer Valley Water Co-operative, a member of the Bondi Group, submitted that not all financial institutions agree with the position of the Australian Bankers' Association. Pioneer argued that there is more security in untransformed entitlements as membership of an irrigation corporation provides 'a level of protection from outside forces in water management.'<sup>126</sup>

Murrumbidgee Irrigation and Macquarie River Food and Fibre submitted that they had no evidence that transformed entitlements provided irrigators with easier or cheaper access to finance or more favourable terms and conditions for that finance.<sup>127</sup> Macquarie River Food and Fibre said that this was because individual irrigator's rights under group entitlements in the Macquarie schemes are clearly specified and documented already.<sup>128</sup> Murrumbidgee Irrigation noted it had not received any complaints from members to date on this issue.<sup>129</sup>

Sunraysia Citrus Growers submitted that operators will not be able to obtain competitive financing themselves unless they continue to hold group water entitlements.<sup>130</sup>

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<sup>121</sup> Australian Bankers' Association, submission 25, p. 11.

<sup>122</sup> Australian Bankers' Association, submission 25, p. 11.

<sup>123</sup> Australian Bankers' Association, submission 25, p. 6.

<sup>124</sup> National Farmers' Federation, submission 41, p. 11.

<sup>125</sup> Narromine Irrigation Board of Management, submission 33, p. 13.

<sup>126</sup> Bondi Group, submission 32, p. 16.

<sup>127</sup> Murrumbidgee Irrigation, submission 44, pp. 2, 9; Macquarie River Food and Fibre, submission 53, p. 15.

<sup>128</sup> Macquarie River Food and Fibre, submission 53, p. 15.

<sup>129</sup> Murrumbidgee Irrigation, submission 44, pp. 2, 9.

<sup>130</sup> Sunraysia Citrus Growers, submission 17, p. 6.

### **Streamline trade processes**

Several submissions noted that a benefit of transformation is that any subsequent trade will be expedited.<sup>131</sup> Macquarie River Food and Fibre rejected the suggestion that operators hold ‘restrictive powers’ over individuals wanting to trade water out of schemes.<sup>132</sup>

Murrumbidgee Irrigation submitted that transformation is not necessary to enable export.<sup>133</sup> It suggested that the export of a group entitlement can be processed just as easily as an individually held entitlement, because the trade occurs directly between two operators who merely amend their group entitlements.<sup>134</sup>

Central Irrigation Trust noted that having transformed and un-transformed customers would cause increased administrative costs, because of their different reporting, monitoring and membership characteristics.<sup>135</sup>

### **5.1.2 Preliminary position**

Transformation can assist in establishing more clearly defined water rights for irrigators, increasing the security and mortgageability of such property and streamlining future trading processes.

Through transformation an irrigator’s right to water is converted from a contractual right with the operator to a statutory right. A transformed water access entitlement, as a statutory right, will be registered on the relevant state government water registry, increasing the security of the title. Where not transformed, the irrigation rights of individual irrigators under group entitlement arrangements can often be ill-defined. Therefore, transformation is a fundamental step toward a more robust water market.

While opinions in submissions diverge on the issue of whether transformation enhances an irrigator’s access to finance, on balance, having the option to transform can only improve an irrigator’s finance prospects.

Transformation can occur simultaneously to trade and this process need not necessarily involve the creation of a separate individual water access entitlement. However, this does not negate the benefits of transforming separately to trade. This is particularly true for irrigators who may wish to trade a portion of their water entitlements in the future.

The ACCC considers there is a strong case for facilitating the transformation process, and for giving irrigators the choice to transform.

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<sup>131</sup> Minerals Council of Australia, submission 39, p. 9; Australian Bankers’ Association, submission 25, p. 8.

<sup>132</sup> Macquarie River Food and Fibre, submission 53, p. 6.

<sup>133</sup> Murrumbidgee Irrigation, submission 44, p. 2.

<sup>134</sup> Murrumbidgee Irrigation, submission 44, p. 2.

<sup>135</sup> Central Irrigation Trust, submission 10, pp. 3–4.

## 5.2 Terms, conditions and processes

### 5.2.1 Submissions by stakeholders

Currently, most operators do not have a process for transforming entitlements separately from trade. Murray Irrigation Limited noted that individuals wishing to transform their water entitlements can only do so through trade.<sup>136</sup>

The Australian Bankers' Association submitted that it is not aware of any operator allowing transformation separate to trade, and that this process should be explicit.<sup>137</sup>

The Australian Bankers' Association also suggested that it would be more effective if governments were to facilitate a one-off transformation for all and ensured that any adverse consequences for operators were addressed.<sup>138</sup> However, as noted by Murray Irrigation Limited, s. 97(6)(b) of the Act permits operators to require approval from persons holding a legal or equitable interest in an irrigation right before allowing the transformation to proceed. This includes a requirement that irrigators consent to their individual right being transformed.<sup>139</sup>

The Ricegrowers Association of Australia submitted that operators should not require irrigators who import water into the district to un-transform that water back into the operator's group entitlements.<sup>140</sup>

### 5.2.2 Preliminary position

Some current practices by operators are preventing or unreasonably delaying transformation of an irrigator's entitlement.

Operators should be required to develop a process for transforming entitlements separate to trade and develop standard terms and conditions for transformation, including standard forms as identified in chapter 3 and 4.

Irrigators should not be required to add imported water back into their operator's group entitlement. However, the ACCC notes that an irrigator is free to negotiate the 're-transformation' of a separately held water access entitlement back into the scheme entitlement should they wish.

An operator is prohibited from requiring an irrigator to transform a separately held water access entitlement back into the scheme entitlement.

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<sup>136</sup> Murray Irrigation Limited, submission 40, p. 33.

<sup>137</sup> Australian Bankers' Association, submission 25, pp. 5, 8.

<sup>138</sup> Australian Bankers' Association, submission 25, p. 4

<sup>139</sup> Murray Irrigation Limited, submission 40, p. i.

<sup>140</sup> Ricegrowers Association of Australia, submission 26, p. 6.

## 5.3 Right to delivery following transformation

### 5.3.1 Submissions by stakeholders

The Minerals Council of Australia submitted that upon transformation, the parties should negotiate the terms and conditions for delivery.<sup>141</sup>

Murrumbidgee Irrigation allows members to transform their water right to a water access entitlement.<sup>142</sup> After transformation, access to the supply network is through a separate customer supply contract that specifies terms and conditions of delivery services. These terms and conditions are negotiated between the operator and customer. Murrumbidgee Irrigation submitted that operators should be allowed to negotiate different terms and conditions with transformed customers as compared to non-transformed customers. Murrumbidgee Irrigation also submitted that:

subsequent rights to variations by the operator – including circumstances that may trigger variation, review provisions, timing, and processes – should be dealt within the contract.<sup>143</sup>

The Australian Bankers' Association recommended that transformation should be separate to delivery entitlements and capacity share.<sup>144</sup>

The New South Wales Irrigators' Council noted that conditions of transformation should not disadvantage the operator's capacity to seek payment for services provided.<sup>145</sup>

### 5.3.2 Preliminary position

The issues paper noted that explicit delivery contracts are already used by some operators for irrigators who hold water access entitlements.

In instances where an irrigator's irrigation right has yet to be unbundled, the irrigation right to be transformed includes a water entitlement and also a residual right to delivery. This right to delivery must be recognised by operators in order for transformation arrangements to be successful. Accordingly, the rules should provide that existing irrigators have a right to delivery with their operator following transformation.

Operators will need to establish terms and conditions of these separate delivery contracts where they do not already exist. Even where separate delivery contracts are in use, the parties may wish to negotiate new terms and conditions of supply following transformation. The ACCC is concerned that under these circumstances the relative bargaining positions of the parties will provide operators with the opportunity to

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<sup>141</sup> Minerals Council of Australia, submission 39, p. 9.

<sup>142</sup> Murrumbidgee Irrigation, submission 44, p. 7.

<sup>143</sup> Murrumbidgee Irrigation, submission 44, p. 7.

<sup>144</sup> Australian Bankers' Association, submission 25, p. 6

<sup>145</sup> New South Wales Irrigators' Council, submission 31, p. 9.

impose significantly adverse or harsh conditions on irrigators that have transformed their irrigation right.

Irrigators should not be worse off under a new delivery contract simply because they chose to transform their irrigation rights. As such, the terms and conditions of new delivery contracts should be substantially equivalent to the terms and conditions attached to delivery services provided under the previous supply contract governing the irrigation right.

However, the parties are free to negotiate different contract outcomes. For example, an irrigator may wish to pay less for delivery services in exchange for receiving an off-peak-type service. Alternatively, irrigators who transform their water access entitlement may wish to have continued access to benefits from membership of a scheme run by an operator. These may include the operator:

- completing mandatory state and federal reporting requirements as part of the licence conditions
- performing contract negotiations on behalf of members for services such as produce packaging.

The proposed approach allows irrigators to negotiate terms and conditions addressing these additional benefits while still providing a safety net to protect irrigator delivery interests.

This condition should be self-regulating and should act as a guide to determining what terms and conditions of a new delivery contract are acceptable under the water market rules. Irrigators will be able to lodge a complaint with the ACCC and if an operator breaches the water market rules, they may be exposed to civil penalty provisions under the Act.

Where an operator's standard delivery contract is not available or when negotiation of a new delivery contract is required, the operator must use their best endeavours to negotiate a new contract within 30 days of the transformation being completed.<sup>146</sup> During this time, the operator must provide delivery services in accordance with the terms and condition of delivery services in the previous supply contract governing the irrigation right.

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<sup>146</sup> As discussed in chapter 4, a transformation is completed once the operator's register has been updated.

An operator must provide delivery arrangements for a transformed water entitlement if required by an irrigator.

Upon transformation, terms and conditions of a delivery contract may reflect those contained in the arrangements as they previously related to the irrigation right. Alternatively, if a delivery contract is re-negotiated, this must be done so in good faith between an operator and the irrigator with a transformed water entitlement.

Unless otherwise negotiated, the terms and conditions of new delivery contracts should be substantially equivalent to those terms and conditions attached to delivery services provided under the previous supply contract governing the irrigation right.

In circumstances where an operator's standard delivery contract is not available or when negotiation of a new delivery contract is required, the operator must use their best endeavours to negotiate a new contract within 30 days of the transformation being completed.

During the time of negotiation, the operator must provide delivery services in accordance with the terms and conditions of delivery services under the previous supply contract governing the irrigation right.



## 6. Restrictive provisions

Currently, a range of conditions are imposed by operators that prevent or unreasonably delay transformation and/or trade. These restrictive provisions may be contained in the operators' supply agreements with irrigators or the terms and conditions for transformation and/or trade, 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 reasons consistent with the water market and the trading objectives of the Act.

This chapter first considers the inclusion in the market rules of a general prohibition on all restrictive provisions imposed by operators.

It then considers the following known restrictive provisions imposed by operators and the extent to which these should be permitted under the water market rules:

- fees and charges imposed on transformation and/or trade
- restrictions based on the identity of the water purchaser
- restrictions relating to state legislative requirements
- restrictions relating to delivery management
- restrictions relating to conveyance losses
- metering requirements
- 4 per cent limits on outward trade
- cut-off dates and trading seasons.

### 6.1 A general prohibition on restrictive provisions

#### 6.1.1 Submissions by stakeholders

A number of submissions suggested that operators have created restrictions or placed outright bans on trade. Around a quarter of submissions, notably those from non-operators, supported removing restrictions to trade.

The Ricegrowers' Association of Australia stated that outright bans and major restrictions on permanent and annual trade are common. It provided the example of one operator who requires a full member meeting to approve an annual trade.<sup>147</sup>

Waterexchange noted that operators:

routinely manipulate restrictions for any purpose and [this] is ultimately used to achieve political or commercial outcomes in order to control the asset movement.<sup>148</sup>

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<sup>147</sup> Ricegrowers' Association of Australia, submission 26, p. 5.

<sup>148</sup> Waterexchange, submission 46, p. 4.

Several submissions supported the removal of an operator's ability to create restrictions on transformation and/or trade. The Minerals Council of Australia submitted that it was not appropriate for operators to determine to whom water should be sold.<sup>149</sup> Macquarie Food and Fibre considered that the only grounds an operator would have for restricting trade are where there are physical or capacity-based limitations or known environmental externalities.<sup>150</sup>

The Queensland Bulk Water Supply Authority argued that there should be no restriction on who may buy water entitlements. It considered that any restrictions should be as limited as possible to fully realise the economic benefits of water trading.<sup>151</sup>

The South Australian Farmers Federation submitted that 'protecting irrigation infrastructure should not be the principal basis for constraining trade out of areas.'<sup>152</sup>

The Australian Bankers' Association submitted that where operators are able to set restrictions, there is also the potential for inconsistencies and uncertainty to develop across districts and jurisdictions, which complicates the market.<sup>153</sup>

Approximately two-thirds of submissions raised concerns about potential adverse socioeconomic effects on water trade of such restrictions.<sup>154</sup> These include attempts by operators:

- to preserve the viability of their own irrigation infrastructure business<sup>155</sup>
- to avoid increases in costs for irrigators remaining in the system<sup>156</sup>
- to prevent the reduction in value of land and infrastructure in the district<sup>157</sup>
- to conserve current population levels and maintain local demand for goods complementary to irrigated agriculture<sup>158</sup> and for other unrelated goods and services such as schools and hospitals.<sup>159</sup>

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<sup>149</sup> Minerals Council of Australia, submission 39, p. 6.

<sup>150</sup> Macquarie River Food and Fibre, submission 53, p. 11.

<sup>151</sup> Queensland Bulk Water Supply Authority, submission 15, p. 4.

<sup>152</sup> South Australian Farmers' Federation, submission 42, p. 4.

<sup>153</sup> Australian Bankers' Association, submission 25, p. 2.

<sup>154</sup> Peter Murray, submission 49, p. 2; Moira Private Irrigation District, submission 52, p. 2; West Corurgan Board of Management, submission 50, p. 2; Murray Valley Community Action Group, submission 9, p. 3; Murrumbidgee Private Irrigators, submission 3, pp. 1–2; .

<sup>155</sup> Sinclair Knight Mertz, submission 28, p. 2; Queensland Bulk Water Supply Authority, submission 15, p. 3; Renmark Irrigation Trust, submission 47, p. 1.

<sup>156</sup> Mourquong Co-operative, submission 14, pp. 1–2; Queensland Bulk Water Supply Authority, submission 15, p. 4; Macquarie Valley Tenandra and Buddah Lakes Scheme, submissions 18 and 19, p. 1; Moira Private Irrigation District, submission 52, p. 2; West Corurgan Board of Management, submission 50, p. 2; Murrumbidgee Private Irrigators, submission 3, pp. 1–2, Sunraysia Citrus Growers, submission 17, p. 1.

<sup>157</sup> Moira Private Irrigation District, submission 52, p. 2; Western Murray Irrigation, submission 11, p. 21; Sunraysia Citrus Growers, submission 17, p. 1.

<sup>158</sup> Peter Murray, submission 49, p. 2; Bondi Group, submission 32, p. 6; Mourquong Co-operative, submission 14, p. 1; Sunraysia Citrus Growers, submission 17, p. 1.

Central Irrigation Trust suggested a solution was to seek the consent of other members before approving external trades.<sup>160</sup> Other submissions suggested maintaining a percentage limit on permanent exports, similar to the current 4 per cent limit, to slow down adjustment.<sup>161</sup>

Conversely, the Australian Conservation Foundation submitted that any percentage or proportional caps on water entitlements that can be held by non-irrigators or local landholders were inappropriate barriers to trade.<sup>162</sup>

### **6.1.2 Preliminary position**

Currently, operators have the ability to set rules and procedures that restrict or prevent transformation and trade.

The ability of operators to set the rules creates the potential for conflict between the interests of the operator and those of potential buyers and sellers.

Even in cases where operators are run in an open, democratic way with an elected board representing member irrigators, there is the potential for conflict between a seller and remaining members acting collectively.

Submissions expressed concerns about inadequate mechanisms to protect third parties, and the potential socioeconomic effects of water trade. However, there are alternative policy instruments available to policy-makers (e.g. the federal and jurisdictional governments) that make them better placed to address these issues rather than operators.

The explanatory memorandum to the Water Bill 2007 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.<sup>163</sup>

Consistent with this objective, the market rules should allow operators only the minimum restrictions necessary to enable efficient trade. To achieve this, the ACCC considers a general prohibition is reasonable and necessary.

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<sup>159</sup> Moira Private Irrigation District, submission 52, p. 2; Sunraysia Citrus Growers, submission 17, p. 1; Vin Byrnes, submission 6, p. 1; Mourquong Co-operative, submission 14, p. 1.

<sup>160</sup> Central Irrigation Trust, submission 10, p. 2.

<sup>161</sup> Moira Private Irrigation District, submission 52, p. 3; Renmark Irrigation Trust, submission 47, p. 1. Renmark Irrigation Trust suggested a limit on large exports (e.g. one trade of more than 20 per cent of the total volume of water delivered by the trust).

<sup>162</sup> Australian Conservation Foundation, submission 23, p. 8.

<sup>163</sup> Explanatory memorandum to the Water Bill 2007, clause 97, paragraph 190, p. 28.

However, operator-imposed restrictions are required in some cases. The water market rules should explicitly permit these restrictions.

Subject to limited explicit exceptions, provided for in the water market rules, an operator should not be permitted to impose any restrictions in contracts, arrangements or understandings. Examples of restrictions that would be prohibited include (but are not limited to):

- some fees and charges levied on the transformation and/or trade of a water access entitlement
- restrictions based on the identity of the water purchaser
- cut-off dates and trading seasons.

## 6.2 Fees and charges

### 6.2.1 Preliminary position

Any fee levied by an operator on the transfer of a water entitlement will act as a barrier to the trade of water from relatively lower to higher value uses. The imposition of these fees results in an inefficient allocation of water between competing users and consequently a loss of economic welfare, since the full potential gains from trade are not realised. The welfare loss increases at an increasing rate as fees become larger relative to the traded price of water.

However, an operator may be warranted in levying administrative fees and charges associated with processing the transformation and trade of a water entitlement for reasons discussed in section 4.3. Similarly the Act states that the water market rules must not prevent an operator from imposing, or requiring payment of, a regulated water charge.<sup>164</sup> These forms of fees and charges should be considered to be exemptions.

Operators should not be permitted to levy any fee or charge on the transformation and/or trade of a water access entitlement except where the fee:

- Is an administrative fee or charge for processing a transformation and/or trade, calculated in accordance with the water market rules, or
- is a regulated water charge as defined in the Act.

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<sup>164</sup> Water Act, s. 97(6)(a). Regulated water charge is defined in s. 91 of the Act.

## 6.3 Restrictions based on the identity of the water purchaser

### 6.3.1 Submissions by stakeholders

#### Market manipulation

Currently, operators can restrict the type of person who can buy water entitlements—for example, by requiring the purchaser to be a landholder in the district.<sup>165</sup>

Water for Rivers considered that there was no case for this kind of restriction, contending that it did not reflect a jurisdictional requirement and made recovery of water for environmental purposes slower and more expensive.<sup>166</sup> The Queensland Bulk Water Supply Authority supported this position:

[R]estrictions on trade should be as limited as possible. The purpose of water markets is to allow water to be traded to its highest value use, enhancing overall economic welfare through making the best possible use of a scarce resource. Operator approval of the use to which traded water is put may interfere with this process.<sup>167</sup>

The Australian Bankers' Association recommended that individual operators should not set their own rules concerning ownership of water entitlement other than those made to implement government policy. The association argued that any potential for inconsistency in setting rules can significantly complicate the market.<sup>168</sup>

A number of submissions supported restrictions that would prevent non-landholders purchasing water because of the potential for speculators to enter the water market, hoard large quantities of water and manipulate the market price.<sup>169</sup> The term 'water barons' featured extensively in submissions.<sup>170</sup>

Mourquong Co-operative, an operator in New South Wales, submitted that large companies could accumulate water licences and then push the price of water up by restricting the timing of seasonal water placed on the market.<sup>171</sup> It advocated restrictions that water be traded within tight geographical zones and to genuine farmers or water users only.<sup>172</sup> This wording was mirrored by Sunraysia Citrus Growers.<sup>173</sup>

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<sup>165</sup> Water for Rivers, submission 51, p. 3.

<sup>166</sup> Water for Rivers, submission 51, p. 3.

<sup>167</sup> Queensland Bulk Water Supply Authority, submission 15, p. 4.

<sup>168</sup> Australian Bankers' Association, submission 25, pp. 1-2.

<sup>169</sup> Bondi Group, submission 32, p. 7; Moira Private Irrigation District, submission 52, p. 4; Mourquong Co-operative, submission 14, pp. 1-2; Sunraysia Citrus Growers, submission 17, p. 1; United Dairy Farmers of Victoria, submission 29, p. 5; Victorian Farmers' Federation, submission 54, p. 6; Vin Byrnes, submission 6, p. 1.

<sup>170</sup> Victorian Farmers' Federation, submission 54, p. 6; Mourquong Co-operative, submission 14, p. 1; Sunraysia Citrus Growers, submission 17, p. 1; United Dairy Farmers of Victoria, submission 29, p. 5.

<sup>171</sup> Mourquong Co-operative, submission 14, p. 1.

<sup>172</sup> Mourquong Co-operative, submission 14, pp. 1-2.

<sup>173</sup> Sunraysia Citrus Growers, submission 17, p. 1.

The Bondi Group submitted that water purchasers should be prevented from withholding water or from selling water back ‘at an unreasonable rate.’<sup>174</sup> It supported trade to non-landholders where a termination fee was paid on surrendered delivery entitlements, as a way to prevent ‘outside corporations buying water and selling it back at inflated prices.’<sup>175</sup>

Western Murray Irrigation submitted that, despite over 20 per cent of its bulk licence being owned by non-landholders and non-irrigators, it found no evidence that water was currently being hoarded or manipulated in its district, as water was transferred annually to related party farms at no charge.<sup>176</sup>

Both Western Murray Irrigation and Murray Irrigation Limited submitted that they do not allow non-landholders to hold delivery entitlements. Western Murray Irrigation requires termination of delivery entitlement and payment of termination fees if water is to be permanently traded to an environmental water purchaser or non-landholder.<sup>177</sup>

Murrumbidgee Irrigation submitted that existing laws should be sufficient to address speculative or predatory behaviour in water markets.<sup>178</sup>

Two submissions noted that the average return on water investment is in the range of 3 to 5 per cent and therefore is not an attractive investment, so there is no reason to exclude investors from the market.<sup>179</sup> Waterexchange submitted that investors may add extra liquidity to flat markets.<sup>180</sup>

### **Government environmental water purchases**

Several submissions were critical of the policy and process relating to government environmental water purchases.<sup>181</sup> These submissions supported restrictions that prevented non-landholders purchasing water, to prevent the government from making purchases.

The Victorian Farmers Federation submitted that the rules should prevent distortions in the market arising from the government entering the market to secure additional water for the environment or to buyback over-allocated water.<sup>182</sup>

Conversely, the Australian Conservation Foundation contended that the environment is a key user of water and therefore must be able to stand in the market on the same footing as other water users. It argued there was no basis for excluding or restricting

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<sup>174</sup> Bondi Group, submission 32, p. 8.

<sup>175</sup> Bondi Group, submission 32, p. 7.

<sup>176</sup> Western Murray Irrigation, submission 11, p. 19.

<sup>177</sup> Western Murray Irrigation, submission 11, p. 18.

<sup>178</sup> Murrumbidgee Irrigation, submission 44, p. 3.

<sup>179</sup> Waterexchange, submission 46, p. 2; Australian Water Brokers’ Association, submission 24, p. 6.

<sup>180</sup> Waterexchange, submission 46, p. 2.

<sup>181</sup> Murrumbidgee Private Irrigators, submission 3, p. 2; Victorian Farmers’ Federation, submission 54, p. 3.

<sup>182</sup> Victorian Farmers’ Federation, submission 54, p. 3.

participation by agents representing the environment in the water market. Such restrictions hinder efforts to address key policy and market failure issues.<sup>183</sup>

### **Offering for internal trade**

Some operators require that water entitlements should first be offered for sale internally.<sup>184</sup> This includes water savings stemming from installation of more efficient irrigation infrastructure.<sup>185</sup> Waterexchange did not support these restrictions, stating that they were ‘used as a handbrake to blunt and control water trading’.<sup>186</sup>

### **Reciprocal arrangements**

Murrumbidgee Irrigation argued that it should be permitted to restrict trade into other districts when reciprocal arrangements for trade are not fair and reasonable as a way of influencing the behaviour of other operators. It submitted that this is ‘a last resort in terms of ensuring a level playing field for its stakeholders and to date has not been applied.’<sup>187</sup>

## **6.3.2 Preliminary position**

Operators place restrictions on the type of person who can buy water entitlements; for example, some operators require the purchaser to be a landholder in the district or to be in the business of irrigated agriculture.

Constraints on the parties to whom water can be sold would not prevent speculation by current landholders or potential traders in future. To the extent that trade in some water markets appears to be thin and therefore potentially more prone to participants wielding market power, this may be exacerbated by restrictions and prohibitions on trading.

There is little evidence that any parties could profitably ‘hoard’ water entitlements. Submissions suggest the return from capital investment in water entitlements is low and only generated when the water is used. In addition, water is difficult and expensive to store for any extended period. While there is likely to be long-term capital growth in the value of water entitlements because of climate change and increasing scarcity of water, the full value of water is best realised from its use as a business input.

On the contrary: entry of non-water users is likely to facilitate trade. New entrants may inject capital and develop new products that allow irrigators to adopt different risk and financing strategies than are currently available. Also, the *Trade Practices Act 1974* provides a level of protection against anti-competitive conduct.

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<sup>183</sup> Australian Conservation Foundation, submission 23, p. 14.

<sup>184</sup> Bondi Group, submission 32, p. 9; Murrumbidgee Irrigation, submission 44; p. 4.

<sup>185</sup> Murrumbidgee Irrigation, submission 44, p. 4.

<sup>186</sup> Waterexchange Australia, submission 46, p. 3.

<sup>187</sup> Murrumbidgee Irrigation, submission 44, pp. 4.

A range of stakeholders expressed concerns about the government's environmental water tenders. These include transparency, accountability and lack of analysis on the socioeconomic impact of purchases. However, the water market rules are not the appropriate mechanism for addressing these concerns.

Operators' restrictions requiring water to be first offered for internal trade should not be permitted. This type of restriction unnecessarily thins the market and prevents gains from trade being realised.

Similarly, operators should not be allowed to place restrictions on trade when dealing with unfamiliar intermediaries or operators. While there is potential for increased compliance costs in these situations, this is considered to be a transitional issue. Similarly, restrictions preventing dealings with other operators because of a lack of reciprocal arrangements should not be permitted. There should be no need for this type of remedial action once the water market rules come into effect.

Operators should not be permitted to impose any restrictions based on the identity of the water purchasers on the transformation and/or trade of a water access entitlement.

## **6.4 Restrictions relating to state legislative requirements**

### **6.4.1 Submissions by stakeholders**

Several submissions received discussed trading restrictions imposed by state governments (as opposed to those imposed by operators). These restrictions cannot be considered through the water market rules as defined under the Act.

However, a number of operators submitted that restrictions are required to comply with state legislative requirements and that these should be permissible under the water market rules.<sup>188</sup>

Some operators hold their bulk entitlements under licences in state legislation and regulation. These licences contain conditions with which operators must comply or face civil penalties. One submission noted that operators had state-based requirements imposed on it under irrigation and drainage management plans.<sup>189</sup>

Beyond the explicit restrictions in state legislation, some stakeholders noted that there is the potential for operators to misinterpret or misapply legislation and policies as a basis for creating and justifying their own restrictions.

For example, both Water for Rivers and the Bondi Group noted that in Victoria, the 4 per cent cap on external permanent trade is applied separately over each zone in the Goulburn-Murray River area by operators.<sup>190</sup> Water for Rivers submitted that Goulburn

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<sup>188</sup> Murray Irrigation Limited, submission 40, p. 23; Murrumbidgee Irrigation, submission 44, p. 4.

<sup>189</sup> Western Murray Irrigation, submission 11, p. 18.

<sup>190</sup> Water for Rivers, submission 45, p. 1; Bondi Group, submission 32, p. 4.

Murray Water applied the 4 per cent cap in each of its six separate zones rather than over the whole bulk entitlement, while in New South Wales the 4 per cent cap is applied to the whole of the bulk entitlement of the irrigation corporations.<sup>191</sup>

For the most part submissions did not identify explicit restrictions on transformation and/or trade applied by operators to comply with state legislation. However, restrictions relating to the following requirements may be imposed for this purpose.

#### **Minimum requirements for stock & domestic use**

Some New South Wales operators submitted that they had an obligation to deliver water to stock and domestic customers.<sup>192</sup> No evidence was submitted that these obligations stemmed from state legislation.

Western Murray Irrigation considered that domestic household supplies should be protected through its 'stock and garden entitlements' being non-tradeable rights that are kept with a dwelling.<sup>193</sup>

Murray Irrigation Limited noted that it currently requires five water entitlements to be retained per landholding for domestic and stock purposes as a condition of trade. It considers it has an obligation to provide a basic service to landholders and that it is not practical to limit access by stock to unfenced channels crossing or adjoining private land.<sup>194</sup>

Moira Private Irrigation District considered it appropriate to allow smaller operators to retain a minimum water holding in the form of a minimum percentage of the entitlement previously associated with the landholding or as a minimum quantity for stock and domestic purposes. This was seen as justified on the basis of protecting third-party interests, particularly in relation to escalating costs for remaining irrigators and the protection of land values in the area.<sup>195</sup>

#### **Environmental regulation**

Several submissions argued that some kind of constraint on trade should exist to limit impacts on the environment.<sup>196</sup> Stakeholders submitted that trade should be restricted when:

- there is no proof that the water use will be sustainable<sup>197</sup>
- there are physical or capacity-based limitations and known environmental externalities<sup>198</sup>

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<sup>191</sup> Water for Rivers, submission 45, p. 1.

<sup>192</sup> Moira Private Irrigation District, submission 52, p. 2; Western Murray Irrigation, submission 11, p. 19; Murray Irrigation Limited, submission 40, p. 11.

<sup>193</sup> Western Murray Irrigation, submission 11, p. 19.

<sup>194</sup> Murray Irrigation Limited, submission 40, p. 11.

<sup>195</sup> Moira Private Irrigation District, submission 52, p. 4.

<sup>196</sup> Goulburn Broken Catchment Management Authority, submission 12, p. 1; Australian Conservation Foundation, submission 23, p. 8.

<sup>197</sup> Western Murray Irrigation, submission 11, p. 18.

- there is a need for minimum water holdings to account for environmental impacts such as salinity<sup>199</sup>
- there is potential for impact on an environmental issue of national significance<sup>200</sup>
- there are sleeper or dozer allocations.<sup>201</sup>

Conversely, a number of stakeholders submitted that restrictions on the basis of possible use of water are more efficiently executed by requiring separate use approval, as set out in clause 30 of the NWI<sup>202</sup> or under statutory water allocation plans, rather than by tying this to trade.<sup>203</sup>

Several stakeholders submitted that operators should only facilitate the physical movement of water to customers in response to trade<sup>204</sup> as the time and cost of gaining approval of land and water management plans can be considerable and can affect trade.<sup>205</sup>

Whether any of these restrictions are, or should be, applied by operators was not often specified in submissions. While not expressly noted, it would appear operators may have some responsibilities to monitor and manage water use within their districts. This appears to be in order to limit environmental effects associated with water use, to be consistent with conditions contained in their licences and land and water management plans.

Murray Irrigation Limited submitted that moving responsibility for implementing environmental policies from operators (through their operating licences) to individual irrigators would:

require more extensive monitoring of the activities of every individual irrigator and an administrative mechanism for attributing the costs to particular causers, possibly through individual pricing.<sup>206</sup>

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<sup>198</sup> Macquarie River Food and Fibre, submission 53, p. 11; Australian Conservation Foundation, submission 23, p. 8.

<sup>199</sup> Bondi Group, submission 32, p. 9.

<sup>200</sup> Sinclair Knight Mertz, submission 28, p. 3

<sup>201</sup> Australian Conservation Foundation, submission 23, p. 15. Sleeper or dozer allocations are those that are held but currently not actively used by the holder. Therefore, they are not currently taken into account in water planning and management activities and water use approvals.

<sup>202</sup> Clause 30 of the NWI provides 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.

<sup>203</sup> Queensland Bulk Water Supply Authority, submission 15, p. 3; National Farmers' Federation, submission 41, p. 5; South Australian Farmers' Federation, submission 42, p. 3. SunWater, submission 21, p. 3; Ricegrowers' Association of Australia, submission 26, p. 5; Minerals Council of Australia, submission 39, p. 5.

<sup>204</sup> Minerals Council of Australia, submission 39, p. 5.

<sup>205</sup> Queensland Farmers' Federation and Queensland Irrigators' Council, submission 58, pp. 4–5.

<sup>206</sup> Murray Irrigation Limited, submission 40, p. 24.

### **Category of the entitlement**

Murray Irrigation Limited noted that the Act is silent on the characteristics attributed to transformed entitlements. However, it considers it reasonable to assume that the transformed water entitlement would be subject to the conditions that attach to the operator's bulk water access entitlement (e.g. supply security or relevant reliability conversion rules).<sup>207</sup>

Murrumbidgee Irrigation submitted that any restriction relating to trade and/or transformation placed by the state on specific types of water rights should be permissible.<sup>208</sup> Murrumbidgee Irrigation also supported restrictions on trade out of a specific districts or defined zones 'when such trade cannot be accommodated because of special hydrological and water supply conditions'. Murrumbidgee cited the Wah Wah irrigation area as an example, noting it is supplied by drainage water.<sup>209</sup>

### **6.4.2 Preliminary position**

It would appear that state government-imposed restrictions on trade can still be applied without needing to be replicated by operators. Where operators introduce restrictions that inappropriately rely on or refer to state government requirements, there is the potential for these requirements to be misinterpreted and applied to members improperly.

#### **Minimum requirements for stock and domestic use**

As noted above, some operators require a minimum irrigation right to be retained by all members, ostensibly to provide for potential stock and domestic requirements. Some of these restrictions may stem from clear community service obligations under relevant state legislation. If the obligation is contained in state legislation, a specific exception to the water market rules general prohibition on restrictions would be warranted.

However, it is possible that operators will use this exception to prevent irrigators from disconnecting supply and exiting the industry.

One justification might be to protect future purchasers from inadvertently buying 'dry' land. In such cases, the purchaser may be liable for reconnection fees, which might be significant if that particular branch of the network has been dormant. However, this problem should become evident through the inquiries of a responsible purchaser before the purchase of any land. The need for this additional protection appears unwarranted.

Operators should only be permitted to require a minimum irrigation right to be maintained on the transformation and/or trade where this is a requirement of a community service obligation contained in a state legislative instrument.
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<sup>207</sup> Murray Irrigation Limited, submission 40, p. 2.

<sup>208</sup> Murrumbidgee Irrigation, submission 44, p. 4.

<sup>209</sup> Murrumbidgee Irrigation, submission 44, p. 4.

## **Environmental regulation**

Linking water use approvals with the transformation and/or trade of water entitlements may not be the most appropriate mechanism for dealing with concerns about the effects of water use on the environment. While such restrictions might mitigate the environmental impact of water use, they would do so in an inconsistent way.

Restrictions on use are fundamentally tied to specific land. The seller's operator should not control who buys the seller's water entitlements or how the sold water is used. The ACCC notes that restrictions relating to use, which may be necessary to comply with licence conditions, can still be applied to landholders and irrigation right-holders who have not transformed.

Operators should not be permitted to impose restrictions on transformation or trade of a transformed water access entitlement in an attempt to regulate land use and the environmental effects of water use.

Operators should not be permitted to impose restrictions on transformation or trade of a transformed water access entitlement relating to regulating land use and environmental effects of water use.

## **Category of the entitlement**

The ACCC assumes that upon transformation a newly created water access entitlement would be subject to the same state-imposed conditions attaching to the operator's 'group' water access entitlement. As noted previously, it would appear that any state government trading restrictions (previously associated with the operator's entitlement) would apply to the irrigators transformed water access entitlement. Therefore, an operator does not need to replicate these requirements.

It is understood that operators may have defined categories of irrigation rights (possibly related to use, security and/or location within the network) in their supply agreements, to manage district specific issues. It is unknown whether these replicate state water access entitlement categories defined in legislation.

Without further information on why the existing state water rights regimes are insufficient to manage district specific issue, operators should not be permitted to impose such restrictions. The ACCC invites stakeholders to provide further information to better inform this judgement.

Operators should not be permitted to impose restrictions on transformation or trade of a transformed water access entitlement relating to the category of the entitlement.

## **6.5 Delivery management**

### **6.5.1 Submissions by stakeholders**

The Minerals Council of Australia argued that operators may have to temporarily decline or postpone a trade when water cannot physically be delivered to all customers at the same time. It suggested that operators are in the best position to plan delivery

timetables because they have the best information about overall water flows and infrastructure capacities at any point in time.<sup>210</sup>

### 6.5.2 Preliminary position

Trades may be inhibited by congestion and the physical constraints of irrigation infrastructure. However, this is only a concern for operators where it relates to trades into the network ('imports') or where it relates to trades within the operator's network ('internal' trades). The ACCC notes that restrictions relating to the physical constraints of the irrigation infrastructure can still be applied to irrigation right-holders who have not transformed. Further, any physical constraints are addressed through water delivery rights.

Operators should not be permitted to impose restrictions on transformation and/or trade of a transformed entitlement to manage delivery and the physical constraints of the irrigation infrastructure except where the transformed water entitlement is sold within the district.

## 6.6 Conveyance losses

### 6.6.1 Submissions by stakeholders

The Minerals Council of Australia identified that if a base load of water is required to operate the infrastructure, this should be delineated in the relevant water sharing plan.<sup>211</sup>

Submissions noted that several irrigation schemes, particularly those in northern New South Wales, were designed around an assumption of socialised transmission losses.<sup>212</sup> This means that irrigators accept that part of their water entitlement would be lost because of evaporation and seepage while in transit to their properties. On export, a proportion is claimed by the operator to cover losses down the channel<sup>213</sup>, and operators in these schemes do not currently hold separate water entitlements specifically to cover these transmission losses.

There is the potential for operators to use this conversion calculation inappropriately to discourage export and dampen trade:

Every water entitlement is one mega litre at the Mulwala Take Off on the Murray River but when the farmer goes to sell his water back to the river, for the environment, MIL claims 17% is theirs. Farmers all accept there is a loss down the channel to their farms but where is this water going when it is put back in the river before the Take Off.<sup>214</sup>

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<sup>210</sup> Minerals Council of Australia, submission 39, pp. 5–6.

<sup>211</sup> Minerals Council of Australia, submission 39, p. 5.

<sup>212</sup> For example, the Tenandra, Buddah Lakes and Greenhide schemes in the Macquarie Valley. See Macquarie Valley, Tenandra and Buddah Lakes schemes, submissions 18 and 19, p. 1.

<sup>213</sup> Thomas McCallum, submission 4, p. 2.

<sup>214</sup> Thomas McCallum, submission 4, p. 2.

It was submitted that evaporations losses are relatively steady regardless of the number of members in the system. Therefore, when members exit these systems, the remaining members share the burden of these losses among a smaller number of irrigators.<sup>215</sup>

The Moira Private Irrigator District noted that where a proposed export would reduce demand on a particular channel below the level that justifies maintenance of that channel system, three options would be available to an operator:

- to prevent the proposed export
- to decommission the channel entirely and stop supplying remaining members (forcing the permanent export of any remaining water entitlements and closure of water-reliant businesses)
- to spread the fixed cost of maintaining the channel across the remaining members.<sup>216</sup>

Namoi Water noted that town water is provided for by operators in some areas, and decommissioning the channel system would not be an option in those cases. It suggested that operators should have the power to block particular trades that are inherently inefficient because of the smallness of the order and the dryness of the particular river system. It noted:

this is the case within the Namoi and other northern systems now – State Water is not obligated to deliver if the orders are small and the system is dry. These decisions are taken through consultation and discussion with users.<sup>217</sup>

Murray Irrigation Ltd mentioned that districts may have specific hydrological characteristics that are best dealt with by operator restrictions.<sup>218</sup>

Moira Private Irrigator District suggested that all irrigation schemes will need to undergo a review of their operational needs to determine what the minimum operating requirements actually are.<sup>219</sup> It was not specified whether this assessment would need to be done at each trade, as a once-off or on a regular annual or semiannual basis.

An alternative to the system of socialised transmission losses is the operator owning sufficient water entitlements in its own right to cover evaporation and minimum operating requirements.<sup>220</sup> SunWater submitted that the risk of distribution losses should be held by operators (as occurs in Queensland) and not borne by water users. Operators would be free to trade these entitlements, at their own risk, subject to the maintenance of service levels within the irrigation system.<sup>221</sup>

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<sup>215</sup> Macquarie Valley, Tenandra and Buddah Lakes schemes, submissions 18 and 19, p. 1.

<sup>216</sup> Moira Private Irrigator District, submission 52, p. 5.

<sup>217</sup> Namoi Water, submission 27, p. 1.

<sup>218</sup> For example, in the Wah Wah irrigation area, drainage water cannot physically be returned to the primary water source. See Murrumbidgee Irrigation, submission 44, p. 4.

<sup>219</sup> Moira Private Irrigator District, submission 52, p. 6.

<sup>220</sup> SunWater, submission 21, p. 3.

<sup>221</sup> SunWater, submission 21, p. 3.

## 6.6.2 Preliminary position

Submissions pointed to restrictions imposed by operators, where, as a condition of trade, they withhold a portion of the seller's irrigation rights out of the network to cover future conveyance losses.

Conveyance (or distribution) losses relate to the water lost in the operator's network through evaporation, seepage etc. These losses represent the difference between the volume of water that needs to be diverted, by an operator (from the water source) for distribution to customers and the volume of water actually delivered by the operator to customers.

Conveyance losses often comprise a fixed component associated with the volume of water required to commence delivery of water, and a variable component that increases as water delivery volumes increase. These losses are understood to be most significant in gravity irrigation districts that use open channels for water delivery, and less significant in piped distribution systems.

The portion of fixed conveyance losses will also depend on the extent of the operator's network. Where customers are dispersed throughout the network, the conveyance losses will be far higher than when they are concentrated.

Where possible, operators should hold water entitlements to cover fixed conveyance losses. Operators are in a position to upgrade common infrastructure and benefit from the resulting drop in evaporation and increased water savings. Where operators hold a water entitlement to cover fixed conveyance losses, this arrangement provides operators with the incentive to perform these upgrades and realise these savings.

Currently, some operators in New South Wales hold a separate 'conveyance' licence to cover the losses associated with delivering water through their network. However, it is understood that operators in South Australia and many operators in New South Wales do not have these separate entitlements.

Where operators do not hold entitlements to cover conveyance losses, these losses may be socialised across irrigators in a district. In this case, trade out of a district may result in the fixed losses associated with operating the network being borne by fewer remaining irrigators, so that they experience an increase in the average fixed conveyance losses.

However, the effects on these third parties do not have implications for economic efficiency. It is noted that operators with separately held conveyance entitlements would be insulated from the effect of a prohibition on restrictions of these forms.

Operators must not restrict the transformation and/or trade of a portion of an irrigator's entitlement for the purposes of covering conveyance losses.
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## 6.7 Metering

### 6.7.1 Submissions by stakeholders

Stakeholders that commented on metering all supported requiring an irrigator to be metered before allowing that irrigator to trade.<sup>222</sup> Some submissions noted that metering provides data to support efficiency improvements, enables monitoring and detection of theft and provides more accurate accounting for water.<sup>223</sup>

One irrigator suggested that transitional arrangements may be needed to assist with the cost of installing meters.<sup>224</sup> It was noted that metering is already a requirement for water licence holders in South Australia.<sup>225</sup> Another operator noted that it supports metering, but allows irrigators to trade out an unmetered entitlement if the supply outlet is closed to the satisfaction of the operator.<sup>226</sup>

### 6.7.2 Preliminary position

The ACCC supports restrictions that prevent trade where there is no meter on the relevant property if the seller does not intend to sell all their water entitlement and disconnect from the operator's infrastructure. In this scenario, a meter is not required going forward and a requirement for metering would create an unnecessary cost and deter structural adjustment.

Further, operators should be allowed to require new customers to install a meter as part of the new supply contract and/or before connecting the land to its irrigation infrastructure.

Operators should be permitted to prevent transformation and/or trade until supply is metered except where the irrigator is terminating access to the operator's infrastructure.

## 6.8 The 4 per cent limit on trade out of a district

The NWI established an interim threshold limit on the level of permanent trade out of all water irrigation areas of 4 per cent per annum of the total water access entitlement for the water irrigation area, subject to review.<sup>227</sup>

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<sup>222</sup> Minerals Council of Australia, submission 39, p. 5; Rod Leavold, submission 48, p. 4; Murrumbidgee Private Irrigators, submission 3, p. 2; Vin Byrnes, submission 6, p. 1; Western Murray Irrigation, submission 11, p. 21; Murrumbidgee Irrigation, submission 44, p. 4.

<sup>223</sup> Minerals Council of Australia, submission 39, p. 7.

<sup>224</sup> Rod Leavold, submission 48, p. 4.

<sup>225</sup> South Australian Farmers' Federation, submission 42, p. 4.

<sup>226</sup> Murrumbidgee Irrigation, submission 44, p. 4.

<sup>227</sup> Intergovernmental Agreement on a National Water Initiative, paragraph 63.

Several submissions supported the maintenance of the 4 per cent limit on permanent trade out of an irrigation district.<sup>228</sup> At its meeting on 3 July 2008 COAG stated its ambition to increase the cap on the trade of water entitlements out of districts from four to six per cent. The water market rules should accommodate the outcomes of this agreement.

Operators should be permitted to impose a cap on permanent trade out of an irrigation district in accordance with any agreement between the federal government and state governments as reflected in state legislation.

## 6.9 Cut-off dates and trading seasons

An operator's 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.

### 6.9.1 Submissions by stakeholders

Numerous stakeholders submitted that cut-off dates and trading seasons are anti-competitive, disadvantage some irrigators in favour of others and are generally an impediment to trade.<sup>229</sup>

Conversely, some stakeholders submitted that cut-off dates do not act as a barrier to trade and are necessary for operators to effectively manage the operation of their water access entitlement.<sup>230</sup> Operators rely on cut-off dates to allow for the balancing of accounts by finalising season water use and determining carryover.<sup>231</sup>

Some stakeholders recommended that trading windows should be increased to provide more flexibility for irrigators, particularly in the case of late season water<sup>232</sup>, and that there should not be any substantive reason to justify cut-off dates for permanent trade in water entitlements.<sup>233</sup> One stakeholder went further to suggest the use of carryover eliminates the need for cut-off dates.<sup>234</sup>

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<sup>228</sup> New South Wales Irrigators' Council, submission 31, pp. 6–7; Victorian Farmers' Federation, submission 54, pp. 3, 7; United Dairy Farmers of Victoria, submission 29, p. 5. UDFV did not support an early review of the 4 per cent limit.

<sup>229</sup> Murrumbidgee Private Irrigators, submission 3, p. 3; Australian Water Brokers' Association, submission 24, p. 11; Minerals Council of Australia, submission 39, p. 8.

<sup>230</sup> Narromine Irrigation Board of Management, submission 33, p. 9; Renmark Irrigation Trust, submission 47, p. 1; Murrumbidgee Irrigation, submission 44, p. 6; Bondi Group, submission 32, p. 13.

<sup>231</sup> Murray Irrigation Limited, submission 40, p. 30.

<sup>232</sup> Murrumbidgee Private Irrigators, submission 3, p. 3.

<sup>233</sup> Murray Irrigation Limited, submission 40, p. 30; Australian Bankers' Association, submission 25, p. 5.

<sup>234</sup> Goulburn Broken Catchment Management Authority, submission 12, p. 1.

Various submissions included information on the current practice of some operators and government agencies in relation to cut-off dates. Some operators noted that the New South Wales Government determines annual temporary trading cut-off dates to accommodate critical water planning.<sup>235</sup> Western Murray Irrigation also allows for internal trading until late June. However, it has never specified cut-off dates for external trades and does not define trading seasons which are different from the New South Wales Government directive.<sup>236</sup>

The Ricegrowers' Association of Australian noted that StateWater in New South Wales has closed the season a month earlier for the last couple of years on the basis that it gives it more time to do end-of-season adjustments.<sup>237</sup> In the case of permanent trade of entitlements if undertaken part-way through a season, StateWater only assigns the associated allocation to that entitlement at the beginning of the next full irrigation season.<sup>238</sup>

Murray Irrigation Limited noted operators are often restricted by licence conditions—for example, the New South Wales Murrumbidgee regulated river water sharing plan that includes cut-off dates for both inter-valley and intra-valley trade before the end of the irrigation supply season. Murray Irrigation Limited claims these dates act to limit use of available water and benefit water users within the irrigation corporations in the Murrumbidgee Valley.

The Winemakers' Federation of Australia submitted that its members have noted a level of confusion about variations in trading 'windows' between irrigation districts.<sup>239</sup> While Macquarie River Food and Fibre observed that trading seasons are generally not applicable in the Macquarie Valley but noted that some operators may wish to have a cut-off date for permanent transfers within the water year.<sup>240</sup>

Some stakeholders noted that a key issue regarding cut-off dates and trading seasons is that those dates should be predetermined and sufficiently publicised in the industry.<sup>241</sup> Stakeholders also noted that these dates should be consistent across the Murray-Darling Basin<sup>242</sup>, should be reviewed regularly to account for improvements in efficiency in the trading process and should reflect operational constraints.<sup>243</sup>

## 6.9.2 Preliminary position

There may be legitimate business reasons for operators to implement the use of cut-off dates and trading seasons for temporary trades to allow the sufficient processing time

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<sup>235</sup> Murray Irrigation Limited, submission 40, p. 31; Western Murray Irrigation, submission 11, p. 27.

<sup>236</sup> Western Murray Irrigation, submission 11, pp. 27–28.

<sup>237</sup> Ricegrowers' Association of Australian, submission 26, p. 6.

<sup>238</sup> Bondi Group, submission 32, pp. 12.

<sup>239</sup> Winemakers' Federation of Australia, submission 22, p. 2.

<sup>240</sup> Macquarie River Food and Fibre, submission 53, p. 13.

<sup>241</sup> Bondi Group, submission 32 p. 12; West Corugan Board of Management, submission 50, p. 3.

<sup>242</sup> Water for Rivers, submission 51, p. 6.

<sup>243</sup> National Farmers' Federation, submission 41, pp. 8–9; Ricegrowers' Association of Australian, submission 26, p. 6.

and finalisation of accounts referred to by many stakeholders. However, cut-off dates and trading seasons shorter than the state-defined trading season may also be used by operators to prohibit or unreasonably delay transformation and/or trade.

Permanent trade and the process of transformation separate to trade should not be restricted through the use of cut-off dates and trading seasons. In particular transformation should be permitted irrespective of the trading season as it represents a solidifying of an irrigator's right. The timing of any application to transform should not impact on the operator.

Operators should not be permitted to impose cut-off dates and limit trading seasons for transformation and/or trade of a transformed water entitlement.



## 7. Security for future payment of fees

An operator's requirement for security for future payment of fees before the trade of a transformed water access entitlement can prevent or unreasonably delay trade. This chapter details the ACCC's considerations about:

- the need for security
- instances when security should be required of an irrigator
- the form security should take
- the value or quantum of security.

Under the schedule E protocol on access, exit and termination fees<sup>244</sup> in the Murray-Darling Basin Agreement, water rights are to be unbundled from delivery rights, with the ongoing fees for access to the operator's water delivery network applied to the delivery right. As a result, irrigators can maintain their delivery right and continue to pay ongoing access fees following the sale of their water right.

In its 2006 exit, access and termination fees report (exit fees report), the ACCC noted operators' concerns that allowing irrigators to elect to maintain their delivery entitlements following the sale of their water entitlements could reduce the revenue security of an operator in some circumstances.<sup>245</sup>

To address this concern, the schedule E protocol allows operators to seek security over the future payment of access fees in specific circumstances:

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.<sup>246</sup>

The exit fees report noted that allowing for operators to seek security as a condition of approval for trade could represent an unnecessary barrier to trade. The ACCC recommended a review of these arrangements to consider whether they unduly restrict trade.

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<sup>244</sup> Murray-Darling Basin Commission, Murray-Darling Basin Agreement, 'Schedule E protocols on access, exit and termination fees', May 2008.

<sup>245</sup> ACCC, *A regime for the calculation and implementation of exit, access and termination fees charged by irrigation water delivery businesses in the southern Murray-Darling Basin*, November 2006, p. 53.

<sup>246</sup> Clause 9(1) of the Murray-Darling Basin Agreement, 'Schedule E protocols on access, exit and termination fees', May 2008.

## 7.1 The need for security

### 7.1.1 Submissions by stakeholders

Many operators were concerned that irrigators who elect to maintain their delivery entitlement following the sale of their water entitlement represent a significant credit risk to the operator.<sup>247</sup> The submissions argued that credit risk can result in difficulties for ongoing investment in water delivery services.<sup>248</sup> Some operators submitted that there is a risk of stranded assets, in terms of abandoned land left with large liabilities and irrigation systems that cannot be maintained by exiting customers.<sup>249</sup>

Several stakeholders recommended that operators should be able to require security to allow them to manage their risks.<sup>250</sup> Further, Murray Irrigation Limited submitted that:

(the) application of security requirements facilitates the basin water market by providing a secure financial base for irrigation operators and certainty for irrigators and other parties owning water entitlements.<sup>251</sup>

Murrumbidgee Irrigation recognised that ‘security arrangements may lock up capital but are consistent with reasonable risk sharing between operators and individual members.’<sup>252</sup>

Numerous infrastructure stakeholders noted that while they had the ability to commence legal action to enforce contractual arrangements and recover debts, the costs associated with such legal action may be prohibitive and time-consuming, particularly for small operators.<sup>253</sup> From a practical perspective, Murray Irrigation Limited noted that its members would be unlikely to endorse more ‘aggressive’ debt-recovery action such as forced liquidation.<sup>254</sup>

Some operators said the probability of recovering outstanding debts in the event of insolvency would be low because operators have unsecured creditor status and would be ‘placed behind the banks.’<sup>255</sup> However, one submission noted that operators should

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<sup>247</sup> Western Murray Irrigation, submission 11, p. 25; Moira Private Irrigation District, submission 52, p. 5; Sunraysia Citrus Growers, submission 17, p. 3; Narromine Irrigation Board of Management, submission 33, p. 8.

<sup>248</sup> SunWater, submission 21, p. 3; Murrumbidgee Irrigation, submission 44, p. 5; Murray Irrigation Limited, submission 40, p. 26.

<sup>249</sup> Western Murray Irrigation, submission 11, pp. 1, 9; Macquarie River Food and Fibre, submission 53, p. 12; Mourquong Co-operative, submission 14, p. 2.

<sup>250</sup> Narromine Irrigation Board of Management, submission 33, p. 8; Murrumbidgee Irrigation, submission 44, p. 5; Mourquong Co-operative, submission 14, pp. 2–3; Renmark Irrigation Trust, submission 47, p. 1.

<sup>251</sup> Murray Irrigation Limited, submission 40, p. 26.

<sup>252</sup> Murrumbidgee Irrigation, submission 44, p. 5.

<sup>253</sup> Sunraysia Citrus Growers, submission 17, p. 4; Western Murray Irrigation, submission 11, p. 26; Mourquong Co-operative, submission 14, p. 3; Moira Private Irrigation District, submission 52, p. 5.

<sup>254</sup> Murray Irrigation Limited, submission 40, p. 27.

<sup>255</sup> Murray Irrigation Limited, submission 40, pp. 26–28. See also: Sunraysia Citrus Growers, submission 17, p. 3; Mourquong Co-operative, submission 14, p. 2.

have a similar status to that of all other unsecured creditors without any special security rights.<sup>256</sup>

Murray Irrigation Limited contended that irrigators who transfer the majority of their water entitlements fall into three categories: those who intend to rely on the purchase of allocations; those who speculate that the future price of permanent water entitlements will be lower and sell with a view to re-purchasing; or those who have commenced an exit strategy. Murray Irrigation Limited considers those who intend to exit to be the most common.<sup>257</sup>

In view of the credit risk, several operators submitted that they should retain the ability to manage delivery entitlements and their termination.<sup>258</sup> The New South Wales Farmers' Association noted operators are in practice electing to impose compulsory termination fees rather than a security.<sup>259</sup> This is evidenced by Murray Irrigation Limited and Western Murray Irrigation requiring payment of a termination fee on all water entitlements transferred from a landholding without delivery entitlements.<sup>260</sup>

Various stakeholders suggested that the time of sale of a water entitlement represents a good opportunity to recover the costs of termination rather than providing security.<sup>261</sup>

Some stakeholders, particularly water brokers and water exchanges, suggested that security is only necessary in the short term. They argued that the longer term access by market participants to the 'full suite' of water products (such as derivatives and futures)<sup>262</sup> and customer retention through marketing, individual contractual negotiations, price discounting and service delivery<sup>263</sup> should adequately address operator credit risks.

### **7.1.2 Preliminary position**

In specific circumstances, operators may face additional credit risks when irrigators hold delivery entitlements in the absence of corresponding water access entitlements.<sup>264</sup>

Stakeholders also highlighted the costs associated with recovering outstanding fees and charges in the event of default. The ACCC acknowledges that normal business practices of enforcing bad debts may not be suitable in all situations because of the disproportionate legal and administrative costs associated with debt recovery.

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<sup>256</sup> D W Sehestedt, submission 5, p. 1.

<sup>257</sup> Murray Irrigation Limited, submission 40, p. 25. See also Southern Riverina Irrigators, submission 34, p. 2.

<sup>258</sup> Western Murray Irrigation, submission 11, p. 1.

<sup>259</sup> New South Wales Farmers' Association, submission 60, p. 2.

<sup>260</sup> Western Murray Irrigation, submission 11, p. 25.

<sup>261</sup> Queensland Bulk Water Supply Authority, submission 15, p. 4; Murray Irrigation Limited, submission 40, p. 27.

<sup>262</sup> Waterexchange, submission 46, p. 4; Australian Water Brokers Association, submission 24, p. 9.

<sup>263</sup> Minerals Council of Australia, submission 39, p. 7.

<sup>264</sup> This view is based on the assumption that an irrigator with a 'reasonable' quantum of remaining water entitlements is more likely to have sufficient financial creditworthiness not to present a significant credit risk.

Operators should be able to mitigate such a risk by seeking security for the future payment of access fees. When applied appropriately, the use of security can have a beneficial impact on the water market by providing a degree of certainty for all participants, particularly operators.

Some stakeholders suggested that security is only required as a temporary measure and that alternate water products will eliminate the need for security in the longer term. The ACCC has not fully investigated the effects that alternative water products, such as futures and derivatives, may have on the water market. It may well be that these products and a focus by infrastructure operators on service delivery may improve the strength of the water market and reduce the need for security generally. However, these options are possible long-term solutions and the water market rules must have immediate application in order to address the objects contained in the Act.

An operator should have the ability to seek security to mitigate the risk of an irrigator's default on the future payment of access fees in specific circumstances.

## **7.2 When security should be required of an irrigator**

### **7.2.1 Submissions by stakeholders**

Several operators noted they were not in a position to assess the risk presented by individual irrigators holding a delivery entitlement in the absence of a water entitlement.<sup>265</sup> Reasons cited include:

- Any risk assessment needs to be ongoing and holding; tracking or managing security over exiting members' delivery rights contributes to significant ongoing administrative costs.<sup>266</sup>
- The risky nature of agricultural businesses.<sup>267</sup>
- A lack of resources or expertise.<sup>268</sup>
- Operators only become aware of an irrigator's financial difficulties when payment of outstanding accounts becomes overdue.<sup>269</sup>
- Operators are not always privy to the financial circumstances of new landholders and their ability to meet the access fees.<sup>270</sup>

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<sup>265</sup> Mourquong Co-operative, submission 14, p. 3.

<sup>266</sup> Sunraysia Citrus Growers, submission 17, pp. 3–4; Macquarie River Food and Fibre, submission 53, p. 12.

<sup>267</sup> Sunraysia Citrus Growers, submission 17, p. 4.

<sup>268</sup> Sunraysia Citrus Growers, submission 17, p. 3; Mourquong Co-operative, submission 14, p. 3; Western Murray Irrigation, submission 11, p. 26.

<sup>269</sup> Murray Irrigation Limited, submission 40, p. 29.

<sup>270</sup> New South Wales Farmers' Association, submission 60, p. 2; Western Murray Irrigation, submission 11, p. 27.

- The complexity of transactions is such that many market participants, including solicitors advising participants, remain uneducated about the new water trading regime.<sup>271</sup>

Western Murray Irrigation suggested that difficulties in assessing risk were why a termination fee is charged on external transfers of water entitlements.<sup>272</sup> Western Murray Irrigation did acknowledge that operators may have a credit payment history for water charges in cases where the irrigator is not a 'new' landholder.<sup>273</sup>

In contrast, Murrumbidgee Irrigation submitted that:

operators are well placed to assess credit risks, and Murrumbidgee Irrigation has accepted the current Schedule E Protocol in respect of seeking security over future payment of access fees.<sup>274</sup>

Similarly, Murray Irrigation Limited noted its assessment of security requirements considers whether the landholder has been on stop-supply for a period of more than 60 days within the preceding three years.<sup>275</sup>

Several submissions argued that the motives of an irrigator maintaining delivery entitlements following trade of their water access entitlement are questionable. Given their concerns about irrigators' motives and difficulties in identifying risk, security is automatically required to 'replace the security of control of that [irrigation right] which the Scheme previously had.'<sup>276</sup>

Murrumbidgee Irrigation preferred security to apply when the value of retained water falls below the value of the termination fee on delivery entitlement (rather than 50 per cent as currently indicated in schedule E), but noted the risk differential was manageable.<sup>277</sup> Similarly, the Murray-Darling Basin Commission noted that operator concerns about credit risk can be addressed if the principles contained within the schedule E are fully adopted by operators and parallel principles for intrastate trade are developed.<sup>278</sup> The Murray-Darling Basin Commission also noted that security for future payment of fees should only be sought when absolutely necessary.<sup>279</sup>

Macquarie River Food and Fibre suggested that irrigators should not be allowed to waive their obligation to pay a termination fee just because they have transformed or

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<sup>271</sup> Western Murray Irrigation, submission 11, p. 27.

<sup>272</sup> Western Murray Irrigation, submission 11, p. 25.

<sup>273</sup> Western Murray Irrigation, submission 11, p. 26.

<sup>274</sup> Murrumbidgee Irrigation, submission 44, p. 5.

<sup>275</sup> Murray Irrigation Limited, submission 40, p. 26.

<sup>276</sup> Trangie Nevertire Irrigation Scheme, submission 56, p.2. See also Western Murray Irrigation, submission 11, p. 25; Moira Private Irrigation District, submission 52, p. 5; Sunraysia Citrus Growers, submission 17, p. 3; Narromine Irrigation Board of Management, submission 33, p. 8.

<sup>277</sup> Murrumbidgee Irrigation, submission 44, p. 5.

<sup>278</sup> Murray-Darling Basin Commission, submission 59, p. 2.

<sup>279</sup> Murray-Darling Basin Commission, submission 59, p. 2.

transferred their share of a group water access entitlement into an individual entitlement.<sup>280</sup>

In contrast, the Bondi Group and the West Corugan Board of Management submitted that once water rights are transformed the only applicable fees will be government fees, (that are the responsibility of the individual), which implies no termination fee will be payable. They suggested that operators should only need to require security on the basis that the water will be used within the operator's district.<sup>281</sup>

### 7.2.2 Preliminary position

There may be some difficulties for operators in assessing the credit risk of each irrigator within the scheme. This position was supported in the ACCC's exit fees report:

infrastructure operators have not developed appropriate credit risk management systems because in most cases they have had security of future payments because of restrictions on the trade of water entitlements.

The schedule E protocol on access, exit and termination fees provides that infrastructure operators should only seek appropriate security for future payment of fees as a condition of the sale of water entitlements where:

- the value of the seller's remaining water entitlements (at the time of sale) is less than 50 per cent of the termination fee associated with any remaining delivery entitlements, **and**
- the infrastructure operator has significant concerns with respect to the possibility of the seller defaulting on the payment of ongoing access fees.

Some industry participants have incorrectly interpreted the 50 per cent threshold as allowing security for future payment of fees as a condition of transformation and/or trade where an irrigator trades more than 50 per cent of their water entitlement.

There may be an administrative burden for operators in carrying out risk assessments and there is a case to modify the threshold test to provide more certainty for stakeholders.

The sale of a water entitlement is only relevant to security considerations if the sale has a direct and consequential impact on the irrigator's capacity to meet their ongoing access fee responsibilities.

The ACCC acknowledges the concerns of some operators who suggest that once an irrigator has traded all of their water entitlement, the farm may have little value. However, it does not necessarily follow that the irrigator's operations will be unviable in all cases. As Western Murray Irrigation noted in its submission, an irrigator could trade all of their water entitlement and source all of their water from the temporary water market. In some circumstances, selling water entitlements may improve the

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<sup>280</sup> Macquarie River Food and Fibre, submission 53, p. 12.

<sup>281</sup> Bondi Group, submission 32, pp. 11–12; West Corugan Board of Management, submission 50, p. 2.

irrigator's ability to pay ongoing access fees as can provide capital for the irrigator to move into other farming methods or crops.

The threshold percentage limit of water held by an irrigator should balance the considerations of the operator's need for security for future payment of fees, but also recognise that the water entitlement asset is the irrigator's to use and/or trade.<sup>282</sup>

In the absence of any further evidence or general information from operators to suggest an appropriate threshold, a judgment has been made about the circumstances in which an irrigator would represent a potential credit risk. The ACCC considers that irrigators should be permitted to trade up to 80 per cent of their original water entitlement before the operator **considers** whether there is a significant risk that the irrigator will be unable or unwilling to pay future access fees.

Murrumbidgee Irrigation gave the example of a watered property where its water entitlement typically represents about 80 per cent to 95 per cent of total assets, with a capitalised liability for delivery entitlement in Murrumbidgee Irrigation of about 15 per cent of water entitlement.<sup>283</sup> The ACCC has understood this to imply that 15 per cent of the value of an irrigator's water entitlement should be sufficient to meet the potential future payment of a termination fee.

The threshold whereby an operator can only require security for future payment of fees when the irrigator retains less than 20 per cent (or trades over 80 per cent) of their original water access entitlement appears broadly consistent with schedule E.

The ACCC proposes the following two-part threshold test to determine when security for future payment of fees can be required of an irrigator as a condition of transformation and/or trade:

#### **PART 1**

An operator can only require security for future payment of fees when:

- the irrigator will retain less than 20 per cent of their original water access entitlement; **and**
- the infrastructure operator considers, on reasonable grounds, that there is a significant risk that the irrigator may be unable or unwilling to pay future access fees, when they fall due.

The ACCC considered what constitutes 'reasonable grounds' and proposes further criteria defining the term reasonable grounds as Part 2 of the threshold test.

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<sup>282</sup> National Competition Council, *Water reform under National Competition Policy: background papers - water property rights*, February, 2001, p. 2. Available at [www.ncc.gov.au/pdf/PIReWa-007.pdf](http://www.ncc.gov.au/pdf/PIReWa-007.pdf).

<sup>283</sup> Murrumbidgee Irrigation, submission 44, p. 5.

In the absence of specific default data in submissions, a judgment has been made as to the circumstances in which an irrigator would represent a potential credit risk. The ACCC invites stakeholders to provide further information to better inform this judgment.

The reasonable grounds test described below includes an assessment of when an irrigator is in 'arrears'.

Murray Irrigation Limited noted that one indicator it uses to determine whether security is required is whether the landholder has been on stop-supply for a period of more than 60 days within the preceding three years.<sup>284</sup> In the absence of any further information, the ACCC believes this is a reasonable ground upon which an operator may require security.

In addition, new irrigators may represent a risk to operators because they do not have a credit history with the operator. The ACCC believes the water market rules should allow operators to address this risk.

## **PART 2**

Reasonable grounds are considered to be where an irrigator:

- has been in arrears in failing to pay the access charge for a period of more than 60 days on more than one occasion in the last three years, **or**
- is a new landholder and has been a member of the scheme for fewer than three years.

Once an irrigator transforms their water access entitlement, an operator may not have any recourse to restrict the trade of that entitlement and therefore require security when the threshold test is met. However, transformation itself does not necessarily represent a risk to an operator in the absence of trade in the water access entitlement.

To address this concern, an operator should be permitted to register a charge over the irrigator's water access entitlement at the time of transformation. The terms of the registered charge should restrict its application to 20 per cent of the irrigator's water access entitlement.

If an irrigator wishes to trade more than 80 per cent of its water access entitlement, the irrigator must seek the operator's approval for the trade in accordance with the registered charge. An operator must give its consent to the trade unless the operator concludes, on reasonable grounds, that there is a significant risk that the irrigator may be unable or unwilling to pay future access fees when they fall due (under Part 2 of the threshold test). In these circumstances an operator may require security for the future payment of access fees in accordance with the water market rules concerning the form of, and limits on, security.

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<sup>284</sup> Murray Irrigation Limited, submission 40, p. 26.

To avoid any uncertainty, an operator may register a charge on the irrigator's water access entitlement upon transformation to protect its right to require security in the future. However, an operator must not require security for the future payment of access fees upon transformation.

An operator may register a charge over 20 per cent of the irrigator's water access entitlement upon transformation to protect its right to require security in the future.

Under a registered charge, an operator must give its consent to the trade unless the operator concludes, on reasonable grounds, that there is a significant risk that the irrigator may be unable or unwilling to pay future access fees when they fall due.

An operator must not require security for the future payment of access fees as a condition of the transformation of an irrigator's irrigation right.

## **7.3 The form security should take**

### **7.3.1 Submissions by stakeholders**

Several operators submitted that in the case of default there may be no other assets of value available to recover the value of debt, which would limit the operator's ability to enforce its contractual arrangements.<sup>285</sup>

In terms of the success of 'dry area' properties, Western Murray Irrigation gave the example in its districts of an irrigator that sold all water entitlements but retained a permanent planting on the farm. The irrigator has had to source all of its water from the temporary water market at prices well in excess of \$500 per megalitre (ML) in the past 12 months. Western Murray Irrigation noted that if the price remains high, its operations will be unviable and its ability to pay an access charge will be severely diminished.<sup>286</sup>

#### **Water**

Some operators suggested that water is the most suitable form of security as the operator has the ability to deny supply for non-payment of fees. In cases where all an irrigator's water entitlement is transferred out, operators no longer have this protection.<sup>287</sup>

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<sup>285</sup> Sunraysia Citrus Growers, submission 17, p. 3; Murrumbidgee Irrigation, submission 44, p. 5; Mourquong Co-operative, submission 14, p. 2; Narromine Irrigation Board of Management submission 33, p. 8.

<sup>286</sup> Western Murray Irrigation, submission 11, p. 25.

<sup>287</sup> Mourquong co-operative, submission 14, p. 3; Queensland Bulk Water Supply Authority, submission 15, p. 4.

## Bank guarantees

Several submissions recommended bank guarantees, mortgages and deeds as alternatives to water as a form of security.<sup>288</sup> Until 8 April 2008 Murray Irrigation Limited had a conditional requirement for landholders to lodge a security deposit in the form of a bank guarantee or cash deposit against future payment of access fees when water entitlements were permanently sold out.<sup>289</sup>

Several submissions noted that bank guarantees incur upfront legal costs, so are relatively expensive to provide, both for the operator and the irrigator.<sup>290</sup> Narromine Irrigation Board of Management submitted that:

the charge or security may not, of itself, constitute a caveatable interest thereby limiting the use of caveats as a form of security.<sup>291</sup>

## Land

The West Corugan Board of Management suggested delivery entitlements should be attached to land because this would provide a way for an operator to secure revenue.<sup>292</sup> The Australian Bankers' Association advised that infrastructure operators in New South Wales, South Australia and Victoria have the right to recover their fees and charges against land on the same terms as local government, which gives them priority over mortgagees. The Australian Bankers' Association noted that while these provisions give absolute security over fees and charges, the timeframes for recovery may need to be reviewed, taking into account the cash-flow needs of a private business.<sup>293</sup>

While several submissions noted the possibility of using land as security, most dismissed it on the following bases:

- The remaining land may be worthless without an attached water access entitlement or irrigation right, particularly when it is in a state of abandonment.<sup>294</sup>
- Un-mortgaged land is unlikely to exist on a landholding with credit risk. If a first mortgage already exists on the land with a bank, the infrastructure operator has little

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<sup>288</sup> Narromine Irrigation Board of Management, submission 33, p. 9; Murray Irrigation Limited, submission 40, pp. 12, 26; Moira Private Irrigation District, submission 52, p. 5; Trangie Nevertire Irrigation Scheme, submission 56, p.2.

<sup>289</sup> Murray Irrigation Limited, submission 40, p. 26.

<sup>290</sup> Moira Private Irrigation District, submission 52, p. 5, Murray Irrigation Limited, submission 40, p. 28.

<sup>291</sup> Narromine Irrigation Board of Management, submission 33, p. 9.

<sup>292</sup> West Corugan Board of Management, submission 50, p. 2.

<sup>293</sup> Australian Bankers' Association, submission 25, p. 4. See further the *Local Government Act 1993* (NSW), ss. 354, 355, 359, 718 and 720; the *Irrigation Act 1994* (SA), ss. 62–64; the *Water Act 1989* (Vic), ss. 278–80.

<sup>294</sup> Mourquong Co-operative, submission 14, p. 2.

hope of obtaining adequate security and ‘would be a very poor second in the collection of debts if the land owner is facing financial difficulty’.<sup>295</sup>

- ‘In any practical sense, the relevant [irrigator’s] (un-mortgaged) land would have to be sub-divided and then sold to recover outstanding water accounts’.<sup>296</sup>

As discussed above, Murray Irrigation Limited noted that its members would be unlikely to endorse more ‘aggressive’ debt recovery action, such as forced liquidation.<sup>297</sup>

### **Insurance**

Another suggestion was that operators seek insurance against the risk of default. The National Farmers’ Federation suggested that an entity similar to the Export Finance Insurance Corporation should be established and administered by the MDB Authority to underwrite bad debts. The National Farmers’ Federation also suggested that the scheme could include agreed credit standards with operators.<sup>298</sup> However, some operators submitted the costs associated with insuring against bad debt may be prohibitive.<sup>299</sup>

### **7.3.2 Preliminary position**

Administrative and legal costs are associated with establishing security arrangements and these costs may vary according to the form of security. The costs of enforcing the security can also be significant. If security for future payment of fees is required under the threshold test, the irrigator is considered to represent a significant risk and should therefore bear the burden of the costs associated with establishing appropriate security.

An irrigator should be entitled to the exclusive use of an entitlement and should be allowed to trade that entitlement for value. This right should be reflected in the water market rules by providing the irrigator with the ability to offer different forms of security. However, the value that can be realised from different forms of security may vary. For instance, if there are competing legal interests attached to an irrigator’s land, that land may not hold the same security as a cash deposit lodged as a bond.

There are benefits for both operators and irrigators in using a bank guarantee or cash deposit as security. Under this arrangement, an irrigator would make a cash deposit to the operator and the operator would hold that deposit only as security until the contract is discharged. The operator cannot use the funds as any type of revenue. The administrative costs of a bond are minimal and the realisation value for the operator would be 100 per cent.

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<sup>295</sup> Western Murray Irrigation, submission 11, p. 25. See also Murray Irrigation Limited, submission 40, p. 28.

<sup>296</sup> Murray Irrigation Limited, submission 40, p. 28.

<sup>297</sup> Murray Irrigation Limited, submission 40, p. 27.

<sup>298</sup> National Farmers’ Federation, submission 41, p. 8.

<sup>299</sup> Mourquong Co-operative, submission 14, p. 3; Sunraysia Citrus Growers, submission 17, p. 4.

It may be most cost-effective for an irrigator to offer a water holding as security for future payment of fees because of the low administrative costs. A minimum holding of water access entitlement would have a realisation value for the operator of 100 per cent as long as no other legal interest was held over that entitlement. This form of security restricts an irrigator's ability to trade the entitlement for value, but the irrigator would still be able to trade any allocations associated with those entitlements on a temporary basis.

The ACCC proposes allowing irrigators to choose what form of security could be offered and requiring the operator to give due consideration to the offer.

If an operator seeks security for future payment of fees, the irrigator has the option to offer the operator security over:

- an unencumbered portion of the irrigator's water access entitlement, or
- a bank guarantee, or
- a cash deposit to be used as a form of bond.

If the irrigator offers one of these forms of security, the operator must give due consideration to that offer.

In any other case, the operator may accept any other form of security as negotiated between the operator and the irrigator.

## 7.4 The value or quantum of security

### 7.4.1 Submissions by stakeholders

Different views were submitted on whether the amount of security should be limited. Several stakeholders suggested that the security should be consistent with the value of the remaining liability for delivery entitlement to the operator and therefore should be limited to the total termination fee liability.<sup>300</sup> Another stakeholder suggested the termination fee liability should be a minimum value.<sup>301</sup>

In contrast, a number of stakeholders recommended the amount of security should not be capped. These stakeholders reasoned that operators are not in a position to assess the extent to which a particular irrigator represented a credit risk, and the value of security would need to be sufficient to generate an annual return that could meet the ongoing access fee obligation. A limit on security may result in a shortfall in debt recovery, which would then need to be met by remaining irrigators.<sup>302</sup>

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<sup>300</sup> Western Murray Irrigation, submission 11, p. 26; Murrumbidgee Irrigation submission 44, p. 5.

<sup>301</sup> Murray Irrigation Limited, submission 40, p. 26.

<sup>302</sup> Narromine Irrigation Board of Management, submission 33, p. 9; Sunraysia Citrus Growers, submission 17, p. 3; Mourquong Co-operative, submission 14, p. 3.

## 7.4.2 Preliminary position

The ACCC's exit fees report noted:

the quantum of any security collateral requested could at most be the termination fee that would be required upon the termination of any delivery entitlements kept by the irrigator.<sup>303</sup>

Again, a balance should be struck between the needs of the operator in securing against the risk of default in future payment of fees and the irrigator's exclusive water rights. Security in these circumstances should only be sufficient to meet a default in future payment of fees. Security should be considered a safety net so that if default occurs, the operator has immediate recourse to recover part of the debt owed. The operator remains free to enforce collection of the remainder of debt under normal business practices by, for instance, seeking legal remedies. Additionally, the legal and social/community disciplines on an irrigator paying the access fee are unchanged.

The balance between operator and irrigator interests is best achieved by a proposed limit on security. Security should be limited to a level that contributes toward recovering the amount of the bad debt owed and, if delivery entitlements are terminated by the operator as a result of default, a proportion of the termination fee if applicable. The remainder of fees payable can be pursued using normal business practices.

Operators should not be secured to the full value of the termination fee as this would represent an unreasonable burden on irrigators in exercising their individual water rights. Furthermore, in some limited circumstances, payment of termination fees is not required where delivery entitlements are not terminated as a result of default.

The ACCC proposes a limit on the value of security up to 50 per cent of the termination fee.

In some instances, a termination fee may not be applicable under the water charge rules. Under these circumstances, an operator can still face credit risks for delivery fees that have accrued in arrears. The ACCC proposes that the water market rules should permit security to cover one year's access fees in cases where a termination fee is not applied by the operator. The appropriate limit on security should be the greater of these two values.

The 50 per cent limit will help operators manage their credit risk while limiting the impact on an irrigator's water rights. The limit is also consistent with the provisions of the schedule E threshold test discussed earlier in this chapter. Specifically, schedule E provides that an operator can not require security unless the current market value of any water entitlements held by an irrigator is less than 50 per cent of any termination fee payable on surrender of all delivery entitlements.

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<sup>303</sup> ACCC, *A regime for the calculation and implementation of exit, access and termination fees charged by irrigation water delivery businesses in the southern Murray-Darling Basin*, November 2006, p. 54.

The value of security should be limited to the greater of:

- 50 per cent of the value of the termination fee as applied by the operator, in accordance with the cap on termination fees provided under the water charge rules, or
- where an operator does not charge a fee on termination fee, the value of the annual delivery fee multiplied by 1.

## 8. Application and implementation of water market rules

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. In addition 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.

### 8.1 Coverage

#### 8.1.1 Submission by stakeholders

Numerous stakeholders, primarily smaller operators, submitted that the water market rules should differentiate in application between smaller and larger operators, predominantly because of the administrative costs associated with compliance activities.<sup>304</sup> A lack of administrative capability to implement changes in order to operate under the water market rules was a common response to the issues paper.

Several stakeholders considered a small operator should be defined according to the size of the irrigation network, the number of irrigators serviced or the volume of water rights held by the operator or their customers.<sup>305</sup> Moira Private Irrigation District went further and suggested that smaller infrastructure operators should be defined as those with fewer than 50 000 ML of water entitlements or, alternatively, by reference to irrigation infrastructure owners whose assets have always been in private ownership.<sup>306</sup> Another suggestion was that the distinction should be made by reviewing the added cost of administrative compliance as a portion of an operator's existing cost structure to determine the extent of the financial burden on specific classes of operators.<sup>307</sup>

Some stakeholders submitted that exemptions should be given to other 'classes' of operators—for instance, off-river schemes that are generally small in size, are owned and operated by a group of small users and have relatively small volume of entitlement.<sup>308</sup> In support of this, the Gol Gol Creek Growers Association submitted that private water diverters can operate and manage themselves cooperatively.<sup>309</sup>

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<sup>304</sup> Gol Gol Creek Growers Association, submission 55, p. 1; Moira Private Irrigation District, submission 52, pp. 5–6; Mourquong Co-operative, submission 14, p. 6; Sunraysia Citrus Growers, submission 17, p. 5; Bondi Group, submission 32, p. 18; Narramine Irrigation Board of Management, submission 33, p. 4; Trangie Nevertire Irrigation Scheme, submission 56, p. 3.

<sup>305</sup> Murrumbidgee Private Irrigators, submission 3, p. 4; Sunraysia Citrus Growers, submission 17, p. 6. Bondi Group, submission 32, p. 18; Mourquong Co-operative, submission 14, p. 6.

<sup>306</sup> Moira Private Irrigation District, submission 52, p. 6.

<sup>307</sup> Sunraysia Citrus Growers, submission 17, p. 7.

<sup>308</sup> Macquarie River Food and Fibre, submission 53, p. 16; Narramine Irrigation Board of Management, submission 33, p. 4.

<sup>309</sup> Gol Gol Creek Growers Association, submission 55, p. 1

Some stakeholders suggested another class exemption should be based on vulnerability to asset stranding and short-term opportunistic conduct by individual members or predatory conduct by larger organisations.<sup>310</sup>

Many stakeholders suggested that the water market rules should have a tiered structure, with some fundamental rules applying to all and selected others only to larger operators.<sup>311</sup>

Primarily, larger operators submitted that the water market rules should apply to all operators with no exceptions for a particular class of operator.<sup>312</sup> Western Murray Irrigation noted that smaller operators would need significant assistance to implement water market rules because many would not even be aware that they are considered operators under the Water Act.<sup>313</sup>

Several stakeholders noted that smaller operators have been excluded from the NWI and larger operators have been consistently discriminated against.<sup>314</sup> Further, it was submitted that unless there is rigour in respect of compliance and deadlines, the current discrimination against members of larger operators will continue.<sup>315</sup> In support of this, the Australian Bankers' Association submitted that the less variation among application of the market rules, the better.<sup>316</sup>

Various suggestions were made by stakeholders about minimising the administrative burden of the water market rules. The Ricegrowers' Association of Australia suggested that administrative costs for small operators could be minimised by standardising the transformation and trade procedures.<sup>317</sup> Similarly, some stakeholders suggested the water market rules should be drafted with consideration given to compliance costs and that these should be sufficiently simple for any operator to implement, irrespective of scale.<sup>318</sup>

Stakeholders also suggested ways in which this administrative burden could be recouped. Suggestions included that the costs could be recovered as part of the charges for processing water transformation and/or trade.<sup>319</sup> However, others suggested that

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<sup>310</sup> Moira Private Irrigation District, submission 52, p. 5; Murrumbidgee Private Irrigators, submission 3, p. 1.

<sup>311</sup> Citrus Growers, submission 17, p. 3; Narromine Irrigation Board of Management, submission 33, p. 14; Macquarie River Food and Fibre, submission 53, p. 16.

<sup>312</sup> Ricegrowers' Association of Australia, submission 26, p. 7; New South Wales Irrigators' Council, submission 31, pp. 2, 12; Minerals Council of Australia, submission 39, p. 10; Murray Irrigation Limited, submission 40, p. 42; National Farmers Federation, submission 41, p. 4; Murrumbidgee Irrigation, submission 44, p. 2; Waterexchange, submission 46, p. 11; Murray-Darling Basin Commission, submission 59, p. 2.

<sup>313</sup> Western Murray Irrigation, submission 11, p. 7.

<sup>314</sup> Ricegrowers' Association of Australia, submission 26, p. 7; Murray Irrigation Limited, submission 40, p. 42; Western Murray Irrigation, submission 11, p. 41.

<sup>315</sup> Murray Irrigation Limited, submission 40, p. 42.

<sup>316</sup> Australian Bankers' Association, submission 25, p. 12.

<sup>317</sup> Ricegrowers' Association of Australia, submission 26, p. 7.

<sup>318</sup> Murrumbidgee Irrigation, submission 44, p. 3; Minerals Council of Australia, submission 39, p. 10; Murray Irrigation Limited, submission 40, p. 42.

<sup>319</sup> Murrumbidgee Irrigation, submission 44, p. 9; Minerals Council of Australia, submission 39, p. 10.

government funds should be made available to smaller operators to enable them to meet increased compliance costs, which are large and unrecoverable, and that the funding should not be subject to cost-recovery provisions.<sup>320</sup>

The New South Wales Irrigators' Council contended that coverage of the water market rules should be extended to government water utilities because these utilities should be exposed to the discipline of competitive forces in their service delivery.<sup>321</sup>

SunWater submitted that the water market rules will not apply in Queensland because all water entitlements were clearly vested with individual irrigators by the *Water Act 2000* (Qld).

Central Irrigation Trust questioned whether the ACCC intends the water market rules to apply to corporate or managed investment schemes, and whether these schemes would be bound by the same trading and reporting obligations as Central Irrigation Trust.<sup>322</sup>

### **8.1.2 Preliminary position**

Water market rules should apply to all operators within the MDB, subject to the provisions of the Act.

There is little merit in limiting the scope of application of the water market rules beyond what is consistent with the Act. The objectives and principles of the Act would best be achieved with universal application of the water market rules. This would ensure certainty for all market participants about their rights and obligations and consistency in transformation and trading processes, which would thereby increase the efficiency associated with such processes.

Operators may incur administrative costs as part of complying with the water market rules; however, these concerns can be addressed using ACCC assistance in the form of standard application forms and educational material.

The ACCC is of the view that the water market rules should apply to all operators within the MDB, subject to the provisions of the Water Act.

## **8.2 Transitional arrangements**

### **8.2.1 Submission by stakeholders**

Numerous stakeholders submitted that the water market rules should permit a transition to full compliance for small operators, including off-river schemes. Concerns related to

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<sup>320</sup> New South Wales Irrigators' Council, submission 31, p. 12.

<sup>321</sup> New South Wales Irrigators' Council, submission 31, p. 14.

<sup>322</sup> Central Irrigation Trust, submission 10, p. 4.

a lack of resources, for instance, because committee members of operators were often employed voluntarily.<sup>323</sup>

Some stakeholders submitted that there would be no merit in the delayed application of the rules for any class of operator, especially if assistance is provided to operators to comply with the rules.<sup>324</sup>

Several stakeholders submitted that a reasonable transition period would be required to give all operators time to comply with the water market rules, to ensure compliance with and successful implementation of the rules.<sup>325</sup> Western Murray Irrigation suggested that 12 months would be a reasonable period.<sup>326</sup>

Several stakeholders submitted that the water market rules should have limited application to agreements already in place between operators and their irrigators.<sup>327</sup> The Bondi Group suggested that the water market rules should recognise pre-existing contracts—for example, when both parties to a contract agree that if it had been entered into in good faith, it should be allowed to run until it expires. The Bondi Group also suggested a minimum five-year period before contracts can be varied.<sup>328</sup>

Western Murray Irrigation noted that current agreements do not have a scheduled end date<sup>329</sup>, although it noted that there is provision for these to be amended.<sup>330</sup> However, there may be minimum timeframes in which these amendments can be completed. Murray Irrigation Limited gave an example of this—where the rules require changes to its company constitution, its company constitution specifies (consistent with the Corporations Act) minimum times in which to notify members of proposed changes.<sup>331</sup>

A few stakeholders noted that irrigation rights are contractual in nature and operators should not be penalised for a change in law or policy.<sup>332</sup> Western Murray Irrigation noted that in all instances operators must be given the opportunity to take appropriate action to honour infrastructure loans and land and water management plans entered into with the New South Wales Government under the terms of its bulk water licence.<sup>333</sup>

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<sup>323</sup> Mourquong Co-operative, submission 14, p. 6; Bondi Group, submission 32, p. 18; West Corrgan Board of Management, submission 50, p. 5; Gol Gol Creek Growers Association, submission 55, p. 1; Trangie Nvertire Irrigation Scheme, submission 56, p. 3; Sunraysia Citrus Growers, submission 17 p. 7; Narromine Irrigation Board of Management, submission 33, p. 14.

<sup>324</sup> Ricegrowers' Association of Australia, submission 26, p. 7; Murrumbidgee Irrigation, submission 44, p. 10; Waterexchange, submission 46, p. 11.

<sup>325</sup> Murrumbidgee Irrigation, submission 44, p. 10; Western Murray Irrigation, submission 11, p. 5; Moira Private Irrigation District, submission 52, p. 2.

<sup>326</sup> Western Murray Irrigation, submission 11, p. 42.

<sup>327</sup> New South Wales Irrigators' Council, submission 31, p. 12.

<sup>328</sup> Bondi Group, submission 32, p. 18.

<sup>329</sup> Western Murray Irrigation, submission 11, p. 42.

<sup>330</sup> Macquarie River Food and Fibre, submission 53, p. 16.

<sup>331</sup> Murray Irrigation Limited, submission 40, p. 43.

<sup>332</sup> Western Murray Irrigation, submission 11, p. 42; Murrumbidgee Irrigation, submission 44, p. 10.

<sup>333</sup> Western Murray Irrigation, submission 11, p. 9.

Several stakeholders noted that the administrative costs associated with transition should be met by the government in the form of funding assistance for all operators<sup>334</sup> and that this should not be subject to cost-recovery provisions.<sup>335</sup>

### **8.2.2 Preliminary position**

Several stakeholders submitted that to provide a level of certainty for participants, current contracts should be permitted to continue. These stakeholders also noted that when both parties to the contract agree to continue the contract, that should be sufficient to exempt the application of the water market rules.

In some circumstances, contracts may have been negotiated between operators and irrigators in good faith and the written contracts reflect this. Even in situations where a formal written contract has been executed, these contracts may contain provisions inconsistent with the water market rules and the objectives and principles of the Act. The ACCC does not support the continued operation of contracts that contain such inconsistencies. Any current contract should continue to operate only to the extent that the contract is formally recognised by both parties in writing and is drafted in compliance with the water market rules. This will provide a significant degree of certainty for market participants and prevent operators from exploiting potential loopholes created if contracts are exempt from the water market rules on the basis that parties have agreed to 'opt out' of the rules application.

All operators will need time in which to implement and give effect to the water market rules. The ACCC proposes transitional arrangements to give operators time to amend terms and conditions and make other necessary changes to comply with the water market rules. These timeframes should be sufficient for both large and small operators. The water market rules are being drafted with significant consideration being given to the issue of compliance burden and should not be unduly onerous on any particular operator to implement.

The ACCC proposes that the first stage of implementation would consist of a transitional period that would run from the tabling of the rules to September 2009 (for commencement in the next irrigation season).

During stage 1, operators must use their best endeavours to ensure that they do not prevent or unreasonably delay transformation and/or trade. The transition period will allow operators time to make necessary amendments to documents such as their constitution, contracts or application forms. Operators should give priority to addressing compliance with the water market rules where current actions or inactions of operators are directly preventing or hindering transformation and trade. In particular, prohibited restrictions within operators' governing documentation and supply contracts should be promptly addressed.

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<sup>334</sup> Western Murray Irrigation, submission 11, p. 42; New South Wales Irrigators' Council, submission 31, p. 14; West Corugan Board of Management, submission 50, p. 5; Gol Gol Creek Growers Association, submission 55, p. 1.

<sup>335</sup> New South Wales Irrigators' Council, submission 31, p. 14.

From September 2009, the water market rules should apply in full. Monitoring will be required to assess their effectiveness and to assist in identifying instances of potential breaches.

The ACCC proposes the following timetable for transition to water market rules:

- Stage 1—from the date the rules are tabled to September 2009—implementation period for operators to amend contracts and other documents. During stage 1, operators must use their best endeavours to ensure that they do not prevent or unreasonably delay transformation and/or trade.
- Stage 2—from September 2009—full enforceability of the water market rules and monitoring.

## 8.3 Monitoring and reporting requirements

### 8.3.1 Submission by stakeholders

Some stakeholders expressed support for ACCC involvement in the water market and suggested that operators should report to, and be monitored by, the ACCC to ensure prohibition of unreasonable or unfair constraint on trade.<sup>336</sup>

Some stakeholders submitted that currently there is no or very little formal monitoring of water market transactions, particularly of small operators.<sup>337</sup> Conversely, other stakeholders suggested operators' conduct is substantially monitored under compliance reporting required under federal and state government legislation and policy.<sup>338</sup>

Some smaller operators contended that the cost of complying with any monitoring requirements will be 'horrific' and that they should not be expected to maintain the same rigorous monitoring scheme that the larger operators may adhere to.<sup>339</sup>

Western Murray Irrigation submitted that the ACCC should consider the following when developing a monitoring regime and associated information requirements:

- resource limitations of the operators (skills, time and money)
- distance and isolation of many operators from experienced legal advisers and so on
- the retention of directors and chief executive officers if monitoring is excessive and if there is a risk of penalties being imposed at an individual level

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<sup>336</sup> Minerals Council of Australia, submission 39, p. 11; South Australian Farmers' Federation, submission 42, p. 5.

<sup>337</sup> Western Murray Irrigation, submission 11, p. 42; Australian Bankers' Association, submission 25, p. 13; Waterexchange, submission 46, p. 11.

<sup>338</sup> Bondi Group, submission 32, p. 19; Murray Irrigation Limited, submission 40, p. 43; Macquarie River Food and Fibre, submission 53, p. 16.

<sup>339</sup> Murrumbidgee Private Irrigators, submission 3, p. 4; Bondi Group, submission 32, p. 19.

- private ownership versus public ownership—the performance reporting regime for publicly owned authorities are different to that applying to privately owned operators
- the frequency of and cost of monitoring to all involved
- a process to respond to individual irrigator’s complaints
- warnings and appeals processes.<sup>340</sup>

Other stakeholders noted that the ACCC should provide guidance on information required by indicating the types of monitoring it expects to implement and ensuring that compliance costs are kept low.<sup>341</sup> Additionally, Murray Irrigation Limited noted that the ACCC should avoid duplicating existing monitoring and reporting arrangements, such as those overseen by the National Water Commission.<sup>342</sup>

A few stakeholders suggested the ACCC’s compliance monitoring should be limited to assessment of complaints, given that the activities of most operators are already monitored by others, including its members and other stakeholders.<sup>343</sup>

On the objectives of monitoring, the Minerals Council of Australia submitted that performance indicators should be used and the results documented in annual reports.<sup>344</sup> Further, the South Australian Farmers’ Federation submitted that the framework for monitoring should be comprehensive, open and transparent, and that it is crucial that the Commission is given real authority to enforce compliance and impose penalties.<sup>345</sup> Macquarie River Food and Fibre went further by suggesting that there needs to be monitoring and ability for enforcement of standards across government departments, to ensure that the trading process is not hindered.<sup>346</sup>

A few stakeholders submitted that the monitoring and reporting regime should include an ongoing assessment of the social and economic impacts of trade if it is concentrated out of a specific region.<sup>347</sup>

### 8.3.2 Preliminary position

The ACCC proposes to keep reporting requirements to a minimum. However, it does not propose to exempt classes of operators from monitoring requirements. The results of monitoring will form an important base from which to assess the success and appropriateness of the water market rules. An incomplete monitoring result may occur if specific classes of operators are excluded from monitoring requirements. This could

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<sup>340</sup> Western Murray Irrigation, submission 11, p. 43.

<sup>341</sup> Murrumbidgee Private Irrigators, submission 3, p. 4; SunWater, submission 21, p. 2; Bondi Group, submission 32, p. 19.

<sup>342</sup> Murray Irrigation Limited, submission 40, p. 43.

<sup>343</sup> SunWater, submission 21, p. 2; Murrumbidgee Irrigation, submission 44, p. 10; Macquarie River Food and Fibre, submission 53, p. 16.

<sup>344</sup> Minerals Council of Australia, submission 39, p. 8.

<sup>345</sup> South Australian Farmers’ Federation, submission 42, p. 5.

<sup>346</sup> Macquarie River Food and Fibre, submission 53, p. 16.

<sup>347</sup> New South Wales Irrigators’ Council, submission 31, pp. 2, 12–13; Queensland Farmers’ Federation and Queensland Irrigators’ Council, submission 58, p. 8.

arise particularly if a specific market rule were to affect certain classes of operators differently to others.

In developing the water market rules the ACCC is considering the burden that future monitoring requirements and their administration may place on operators. The ACCC is also investigating how to eliminate any doubling-up of reporting requirements for operators. However, the ACCC requires more details about the specific information captured by other agencies and/or market participants during their current monitoring activities.

Beyond these considerations, the ACCC will not be in a position to propose any specific reporting requirements until the water market rules are more fully developed.

The ACCC proposes to keep reporting requirements to a minimum for the purposes of monitoring.

The ACCC is developing the water market rules while having regard to the potential monitoring requirements and associated administrative burden on operators.