



AUSTRALIAN COMPETITION
& CONSUMER COMMISSION

Productivity Commission Inquiry into National Water Reform

ACCC Submission on the Draft Report

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1. Introduction

This submission provides comments from the ACCC on the Productivity Commission's (PC) *Inquiry into National Water Reform Draft Report* (draft report), released for public comment on 15 September.

Section 2 sets out our high level comments relevant to the broad directions of water market reform and to the development of any renewed Intergovernmental Agreement on a National Water Initiative (NWI).

Section 3 provides our specific responses to the draft report's findings and recommendations.

Section 4 provides comment on selected issues discussed in the draft report but not addressed in the PC's draft recommendations or findings.

In summary, the ACCC:

- strongly supports or supports the PC's recommendations on:
 - removing remaining unwarranted trade barriers, including trade between the urban and rural sectors
 - government provision of grant funding for irrigation infrastructure, or that part of infrastructure, that is for the private benefit of irrigators
 - incorporating all entitlements (such as extractive industries) into the entitlement framework.
- provides qualified support for, and encourages further consideration of:
 - the PC's draft finding that the government's role in water market information should be limited to providing "basic" trade data
 - opportunities to reinvigorate NWI parties' progress on cost recovery for water planning and management
 - the development of pricing principles to avoid discouraging the development of integrated water cycle management.
- sounds a cautionary note on:
 - the need to avoid the risk of anti-competitive or collusive behaviour when developing proposals for "collaboration" between local water utilities
 - the PC's assessment of the effectiveness of rules currently in place to limit monopoly power of irrigation infrastructure operators (IIOs) in the Murray-Darling Basin (MDB)
 - some additional areas where further consideration or detailed oversight is warranted.

In addition, the ACCC provides some thoughts relevant to development of a new NWI framework.

We would be happy to elaborate on any of these matters with the Inquiry team.

2. Overarching comments

Overall, the ACCC agrees with the PC's overarching assessment that water reform has brought significant benefits to irrigators and other stakeholders, and with the conclusion that there is more work to be done.

To enable further rigorous assessment of the outcomes achieved under the existing policy framework and to better identify areas for future reform or further work, we consider that the PC could provide additional useful commentary in its final report on the following matters:

The adequacy and capacity of existing institutions

Many of the draft recommendations depend upon more robust and independent oversight of the proposed arrangements. The PC could more explicitly identify the gaps in or inadequacy of current oversight arrangements, and provide more guidance on what improved institutional arrangements would look like. It may be helpful to the PC to refer to the reports and recommendations that result from the various Commonwealth and State government inquiries currently underway investigating governance and strategic compliance issues within the MDB.¹

The ongoing role of water use efficiency as a cornerstone of the NWI

The NWI is underpinned by the objective of improving water use efficiency.² Water use efficiency is not defined in the NWI. There are many possible definitions, each measuring a somewhat different concept, and which, if pursued as a reform objective, will drive outcomes in particular directions.

The PC does not address how water use efficiency should be defined or what priority should be given to water use efficiency in the NWI, having regard to the NWI's overarching objectives to optimise economic, social and environmental outcomes (cl.23). This is significant because there are clear tensions between these goals. Further, as the 'low hanging fruit' to achieve water use efficiency has been largely obtained, the gains from further improvements may be difficult to achieve and potentially work against other goals, including that of overall economic efficiency (see below).

The PC urges benefit cost assessments to be completed for business cases to invest public funds in infrastructure, and we strongly support this call, but suggest that the PC could clarify that water use efficiency should not be prioritised over achieving more efficient and effective overall resource use. This is particularly important if the shift in policy from water purchase to water infrastructure upgrades as the major mechanism for recovering water for environmental purposes is ongoing.

Water use efficiency in the context of more efficient and effective overall resource use

The PC should consider further the interaction between all input costs, including, for example, energy, water and labour. Irrigators optimize across all farm inputs, not just water. Increasing energy costs may result in irrigators moving away from (or not adopting) water efficient systems. High energy requirements for water efficient infrastructure, for example, may slow or even reverse the uptake of water efficient infrastructure, thus acting against achievement of the NWI's goal. Improving energy efficiency in irrigation could contribute to productivity gains across both energy and water. The PC should note that providing

¹ These inquiries include the MDBA's Basin-wide Compliance Review, the Ken Matthews' Review of Water Issues in NSW, the Australian National Audit Office's Expanded National Partnerships Agreement Audit, the Senate Inquiry into the Integrity of the water market in the Murray Darling Basin, and several investigations underway by the NSW Independent Commission Against Corruption.

² COAG (2004), *Intergovernmental Agreement on a National Water Initiative (NWI)*, cl.23viii

government subsidies for energy intensive infrastructure upgrades to enhance water use efficiency may increase risk to irrigators and harm their ability to respond to changes or 'shocks' such as droughts (see Anderson, Loch, Wheeler and Connor, 2017³).

Monitoring and public reporting of the impacts of infrastructure on return flows

Given the focus on water use efficiency and the deficiencies of benefit cost analysis of business cases for improving water use efficiency on farm and delivery efficiency off farm, it is not surprising that return flows often have not been appropriately considered. The PC's Draft Report provides little evidence about the extent to which these returns are being achieved. There is a substantial future risk to water reliability by continuing to invest in technical efficiency on farm without adequately considering the impact on third parties, including the environment and other water users. The PC could consider whether public funding (if any is provided) should give priority to investments that address excessive evaporation and seepage into saline ground water, rather than focus on investments that largely re-distribute water among existing water users.

The economic efficiency effects of premiums paid for water 'saving' through infrastructure

The PC notes that governments have paid large premiums when recovering water⁴ via infrastructure upgrades but does not discuss the potential distortions to competition through the advantage to those water users that benefit from the funded upgrades compared to those who do not. Nor does the PC note that irrigation upgrades in terms of water use efficiency can result in increased water use (see, for example, Anderson, Loch, Wheeler and Conner, 2017⁵).

We encourage the PC to identify these effects in the final report to ensure they are broadly understood and appropriately considered in the design of infrastructure funding policy and programs.

Further detail on proposed benefit cost assessment requirements in infrastructure business cases

The PC calls for future business cases for infrastructure investment to be required to contain a benefit cost assessment. In the final report, the PC could helpfully elaborate on the standards for an assessment, the compliance and review processes to enforce those standards and arrangements to improve the transparency of assessments prior to the investment decision being made.

Guidance on the development and use of Community Service Obligations (CSOs)

The NWI allows for the provision of CSOs but does not specify when and how they should be implemented. While the PC encourages the use of CSOs in preference to capital subsidies where a need can be identified, an important gap in NWI and in the draft report is the absence of guidance on a framework for developing and applying CSOs. CSO payments could be a major issue for the water sector in future as 'gifted' public infrastructure matures, in light of the ongoing requirement to realise water savings from the infrastructure in perpetuity. The PC could usefully provide commentary on the key elements of a CSO framework.

³ Anderson, Loch, Wheeler, O'Connor (2017), *Submission to Senate Inquiry into Water Use Efficiency in Australian Agriculture* (Senate Inquiry Submission), Canberra. Available at: https://www.aph.gov.au/Parliamentary_Business/Committees/House/Standing_Committee_on_Agriculture_and_Water_Resources/Wateruseefficiency/Submissions

⁴ Productivity Commission (2017), *National Water Reform*, Draft Report, Canberra, p. 238. (Draft Report)

⁵ Anderson, Loch, Wheeler, O'Connor (2017), Senate Inquiry Submission.

Assessing treatment of gifted assets and CSOs in a regulated asset base

We support the PC's approach to funding of future infrastructure assets, and further highlight the difficulties that past gifting of infrastructure may create for future renewal of assets.

As the PC acknowledges,⁶ substantial public funds have been invested in new or upgraded water efficient irrigation infrastructure with the intention of recovering water for the environment. For those investments to provide the intended public benefit (that is, to achieve their objective of providing water for the environment) the associated water savings resulting from the new or upgraded infrastructure must be assured in perpetuity. This requires expenditure on maintenance and on replacement or refurbishment as the infrastructure matures.

The Intergovernmental Agreement on NWI called for rural water systems to achieve at least *lower bound pricing*, which includes provision for future asset replacement or refurbishment, as well as the recovery of operating and maintenance costs. If this principle is followed, operators should be charging sufficient amounts to customers to fund the renewal of previously gifted assets.

The NWI Pricing Principles (clause 23) provide for contributed assets (gifted by government) to be excluded from the regulated asset base so that users are not asked to pay charges to finance the *original* contributed cost of the assets. However, an annuity charge may be applied to recover the future costs of the replacement or refurbishment of contributed assets.

The NWI also calls for:

- continued movement towards upper bound pricing (which includes the full cost of asset consumption) for all rural systems, where practicable; and
- where full cost recovery is unlikely to be achieved in the long term and a Community Service Obligation (CSO) is deemed necessary, the size of the subsidy is to be reported publicly and, where practicable, jurisdictions to consider alternative management arrangements aimed at removing the need for an ongoing CSO.

However, as the ACCC noted in its previous submission, benchmarking of performance efficiency has lapsed in recent years and so it is difficult to assess the extent of implementation of the goals of lower or upper bound pricing.⁷ Together with lighter-handed regulation of charges for most irrigation infrastructure operators, this creates the risk that charges will not adequately provide for the future replacement or refurbishment of these previously-gifted assets, and will result in claims upon government to fund these costs when the need to undertake renewal arises.

The question of who will pay for the ongoing requirements to provide water savings obtained through past provision of water infrastructure should be clarified well in advance of the need to refurbish or replace that infrastructure. We note preferences for the standard of refurbishment or asset replacement may differ between water users, and may exceed that needed to provide the water savings for environmental purposes. The standard chosen will influence costs and charges payable by the users, and expenditure on any upgrades for private benefit would need to be fully cost-recovered from users. The NWI pricing principles could be reviewed to clarify the treatment of these issues.

⁶ PC Draft Report, p.216.

⁷ ACCC submission to PC issues paper, pp.33-35.

3. Specific responses to draft findings and recommendations

This section sets out in detail the ACCC's responses to the draft report findings and recommendations.

DRAFT FINDING 2.1

Water reform has brought about **significant benefits** to communities and stakeholders; however, there is **further work** to do. There is **unfinished business** in some areas of the National Water Initiative, and in some jurisdictions, that should be progressed. There is also a range of **future challenges** facing the water sector that will require **further water reform**.

ACCC RESPONSE

The ACCC generally supports the Productivity Commission (PC)'s draft finding **2.1**, making the following three comments.

First, we consider that the reform program would benefit from governments continuing to improve their methods used to engage with and communicate the net benefits of reform to communities and stakeholders. This work would be assisted by governments developing agreed rigorous methodologies for quantifying costs and benefits and for explaining how these are distributed.

Second, in its characterisation of the future challenges facing the sector, the PC identifies three significant challenges to be addressed: population growth and urbanisation, climate change, and changing community expectations. The PC states that "these challenges need to be addressed in policy frameworks, including the NWI, to ensure that policy frameworks are up to date and can continue to serve the Australian population into the future" (p12). We consider that changes in the energy sector could also be explicitly included in this list.

Energy costs have a significant influence on the water sector, affecting, for example, choice of water treatment, delivery & use technologies and service providers' and water users' operating costs and charges. Water efficient irrigation systems are generally more energy intensive than less efficient systems, so high energy costs may result in irrigators moving away from (or at least not taking further steps towards) water efficient systems and this may impede achievement of the current NWI objective related to increased water use efficiency. Further, through their influence on water demand, energy costs impact on water trading and potential exit and entry into irrigated farming. The link between energy and water use will mean that the price of energy will affect farm- and industry sector-level productivity, as well as regional development.

While the PC expresses the view that "matters directly related to energy policy (including energy prices) are beyond the scope of this report" (p.230), the Inquiry's terms of reference call for the PC to consider "broader policy issues ..., in particular: the interaction of water policy with other policy areas such as energy" (p.vi). While policy recommendations to address issues in energy would be outside the scope of this Inquiry, we believe that the PC could usefully include some discussion of the nexus between energy use and water use efficiency in its final report, to signal the importance of this interrelationship to policy makers in both the water and energy sectors.

The PC could recommend further work be done to explore the links between energy use by irrigators and the current policy settings: for example, considering how, why and when irrigators / operators use energy; monitoring energy prices and the share of operating costs

that energy represents in various types of irrigation enterprises; and how energy costs can influence network operation and investment decisions and farm-level decisions on commodity choice, whether or not to irrigate, adoption of alternative technologies and water use practices. This information could be used to inform the design of government policies and programs that will achieve their goals at the least cost in the next stage of water reform.

Finally, we note the importance of the upcoming review of the effectiveness of the Murray-Darling Basin Plan (MDBP) as a key element in progressing further water reform within the Murray-Darling Basin. A review of the NWI, as recommended in this Draft Report, is unlikely to be significantly advanced by the time the MDBP review is completed. Nevertheless, some of the recommendations in this Inquiry will be relevant to the MDBP review.

DRAFT FINDING 3.1

Entitlement and planning reforms have provided economic benefits and promoted certainty through more transparent and inclusive decision making. They have also enabled a significant move towards improved environmental outcomes.

However, there are still areas where further reform and / or ongoing effort is required to meet the outcomes and objectives of the National Water Initiative. These include the failure of Western Australia and the Northern Territory to enact the legislation required to create secure, National Water Initiative consistent water access entitlements.

DRAFT RECOMMENDATION 3.1

State and Territory Governments should ensure that entitlement and planning reforms are maintained and improved.

Priorities are:

- a. Western Australia and the Northern Territory should establish statutory based entitlement and planning arrangements that provide for water access entitlements that are long term, not tied to land, and tradeable
- b. State and Territory Governments should ensure that water entitlement and planning arrangements explicitly incorporate extractive industries, such as by ensuring entitlements for extractive industries are issued under the same framework that applies to other consumptive users unless there is a compelling reason otherwise
- c. State and Territory Governments should develop a process to regularly assess the impact of climate change on water resources. Where this is considered to have been significant and detrimental, they should ensure that the next water plan review fundamentally reassesses the objectives of the plan (including environmental and consumptive) and the consequent balance between environmental and consumptive use of water, to ensure it is suited to a drier climate
- d. State and Territory Governments should ensure that, as water plans reach the end of their planning cycle, suitable review processes are undertaken that allow optimisation of water use and system operation across all users, include explicit consideration of Indigenous cultural values and involve adequate community and stakeholder engagement
- e. State and Territory Governments should ensure that their entitlement frameworks can incorporate alternative water sources, such as stormwater, wastewater, and managed aquifer recharge, so they do not present a barrier to efficient investment in these supply options.

Australian, State and Territory Governments should revise relevant provisions in the National Water Initiative to align with recommendations 3.1(b) to 3.1(e).

ACCC RESPONSE

The ACCC supports draft recommendation **3.1** to maintain and improve existing planning and entitlement reforms, in particular through the PC's calls for:

- WA and NT to introduce NWI-consistent entitlement and planning frameworks. Introducing such arrangements in the Murray-Darling Basin states has resulted in significant development of water markets and the legal recognition of water for environmental purposes, and we note that the PC expects benefits to be positive for WA and NT. The ACCC notes the importance of considering the transactions costs of changes to ensure there are net benefits.
- governments to bring entitlements for extractive industries under existing planning and entitlements frameworks. However, we note that the PC qualifies recommendation 3.1(b) by allowing for the existence of 'compelling reasons' not to remove exemptions, leaving room for case-by-case assessments and therefore the possibility of sub-optimal outcomes affecting water markets and entitlement frameworks. In its final report, the PC could provide further detail on the circumstances it believes might warrant continuing exemptions and could propose guidelines for decision-making on this matter to increase the transparency and consistency of decision-making.
- End-of-cycle water plan reviews; however, planning frameworks should generally seek to avoid the development of mechanisms accessible only by particular classes of user, and any special purpose Water Access Entitlements should be made consistent with the NWI. Water use decisions are best left to water users, but planning frameworks should – through clear and robust entitlement and trading arrangements – provide the necessary conditions for the optimisation of water use by water users (rather than seeking to make these decisions on their behalf).

DRAFT RECOMMENDATION 3.3

Where State and Territory Governments provide access to water for Indigenous economic development they should:

- a. source water within existing water entitlement frameworks, such as by purchasing water on the market or as part of transparent processes for releasing unallocated water
- b. ensure adequate supporting arrangements (such as training and business development) are in place to enable Indigenous communities to maximise the value of the resource
- c. involve Indigenous communities in program design
- d. ensure future governance arrangements are specified and implemented.

Australian, State and Territory Governments should revise relevant provisions in the National Water Initiative to align with recommendations 3.3 (a) to 3.3 (d).

ACCC RESPONSE

The ACCC supports in principle draft recommendation **3.3** on the basis that access to water for Indigenous economic development requires the potential for consumptive use of water, and consumptive water access rights should be sourced within the same frameworks and have the same characteristics and associated conditions as for existing water access rights.

The PC could consider expanding draft recommendation **3.3 (d)** to include the core elements of the governance arrangements that would support the implementation of their recommendation.

DRAFT RECOMMENDATION 4.1

Australian, State and Territory Governments should maintain trade reforms to date and improve arrangements to facilitate open and efficient water markets.

Priorities are:

- a. State and Territory Governments should remove those residual trading rules, policies (whether or not explicitly stated) and other barriers that prevent water being traded, or otherwise transferred, between the irrigation and urban sectors
- b. the Australian Government should commission an independent review of the effectiveness and efficiency of service standards for trade approvals. The review should consider whether the standards should require shorter approval times
- c. the role of governments in providing water market information should be focused on ensuring the quality and accessibility of basic trading data. In fulfilling this role, State and Territory Governments should improve the quality and accessibility of trade data in water registers.

Australian, State and Territory Governments should revise relevant provisions in the National Water Initiative to align with recommendation 4.1 (a).

ACCC RESPONSE

We strongly support the PC's overarching recommendation in **4.1** to maintain trade reforms to date and to continue to improve arrangements to facilitate open and efficient water markets.

On the specific elements of draft recommendation **4.1**, we make the following comments.

Restrictions on rural to urban trade

On draft recommendation **4.1 (a)**, the ACCC supports the PC's position which is consistent with the views expressed in our submission to the Issues Paper, and with our earlier 2010 advice,⁸ to enable rural to urban trade where feasible.

Restrictions for hydrological connections and water supply considerations or environmental impacts

In section 4.3 of the draft report, the PC describes a range of restrictions to manage hydrological connections and water supply considerations and environmental impacts, and notes the ACCC's observation that review of the Basin Plan Water Trading Rules (BPWTR) will not necessarily resolve any issues with the operation of these restrictions.⁹ The ACCC's comment reflected that constraints and restrictions of these kinds are currently permitted under cl.12.16-12.18 of the BPWTR. Changes to the operation of these classes of restriction will generally arise through review of Basin State trading rules, system operation arrangements under the MDB Agreement, Schedule D and associated protocols rather than through review of the BPWTR.

The ACCC participates as an observer in several interjurisdictional working groups that contribute to the development and review of Murray-Darling Basin trade arrangements under the Basin Plan and the Murray-Darling Basin Agreement. Work is currently being done by these groups to review trade adjustment processes.

Since the commencement of large scale interstate water trade in the mid-2000s, we have seen significant growth in interstate trade, as well as changes to trading patterns and water use. However the trade adjustment processes, which support the current trading framework in the southern Murray-Darling Basin and adjust state resources when water is traded between states, have been relatively unchanged over that time.

⁸ ACCC (2010), *Water trading rules – final advice*, Canberra, p.56.

⁹ PC, Draft Report, p.110.

The MDBA, in conjunction with Basin States, is now taking the opportunity to review these arrangements as part of good business practice and continual improvement. This review is called the trade adjustments project. The project follows a review of Schedule D of the Murray-Darling Basin Agreement (which sets out the arrangements for interstate trade) which identified some possible areas of improvement to trade adjustment processes.

The trade adjustment project will explore whether there are opportunities to improve how trade adjustments are made. In doing so, it will ensure the trading framework continues to support the efficient functioning and ongoing maturing of water markets in the River Murray system. The MDBA is also working with states on improving understanding of capacity and shortfall risks in the River Murray system and findings from this work may inform parts of the trade adjustments project. An update on the trade adjustments project will be provided to the Basin Officials Committee in mid - 2018.

Other restrictions or constraints on trade that should be reviewed

In considering other policies that may operate as barriers to trade, the PC could usefully include in its final report further discussion of the operation and effect as barriers or impediments to trade of various government policy decisions not to use trade mechanisms to meet particular needs to source water: for example, the 1,500GL cap on surface water purchases for the environment, legislated by the Australian government in 2015. While the PC comments in Appendix B (p390) that this limit is contrary to the NWI, it is not discussed in the Chapter on trade restrictions.

Reducing the transaction costs of trade

The ACCC supports the PC's call, in **4.1 (b)**, for governments to commission an independent review of the effectiveness and efficiency of service standards for trade approvals. Timeframes for trade approvals have improved but current service standards do not provide incentives for water registries and approval authorities to seek further improvements. A recurrent and independent review mechanism would provide an incentive for governments to progress improvements on register interoperability. Parties could also track the effect of any changes to governance arrangements and processes (such as the privatisation of the Land and Property Information Service – including the Water Registry – in NSW). We note that our 2010 BPWTR final advice recommended reviewing trade approval standards every two years.

Provision of water market information

Further to draft recommendation **4.1 (c)** we consider that the PC could usefully clarify and elaborate on what it considers to be 'basic trade data' for the purpose of defining government's role in providing water market information (we also note an inconsistency between the recommendation and the text of the Key Messages of Chapter 4, which refers to focus on *basic water resource* as well as trade data). We understand basic trade data to be all the relevant details that can be efficiently captured at the time of transaction. We consider that it is sensible where State government agencies/registries capture information to make publically available such data. We also note that data in raw form may be insufficient to support water users' and policy-makers' needs, with synthesis, interpretation and analysis required, and that the marginal cost to the collecting agencies to engage in the necessary data 'cleaning' and verification may be low. In addition, government agencies may have need for some data for their own purposes. Commonwealth government departments and agencies with responsibility for publishing different kinds of water market information are

working together to document and make more widely available the information they publish, to reduce duplication and ensure consistency/clarity across available sources of information and to make data more openly available in order to encourage its use, analysis and development in new applications by water market intermediaries and other interested parties.

DRAFT RECOMMENDATION 5.1

Australian, State and Territory Governments should ensure that their policy frameworks provide for the efficient and effective use of environmental water to maximise environmental outcomes, and where possible, provide additional community outcomes relating to water quality, Indigenous values, recreation and economic benefits.

Australian, State and Territory Governments should enhance the National Water Initiative to align with this recommendation.

ACCC RESPONSE

The ACCC supports in principle draft recommendation 5.1. We recognise that the primary purpose of environmental water is to achieve environmental outcomes and, where possible, support policy frameworks maximising other complementary outcomes from its use, noting that the policy frameworks should provide for access to trade and should avoid developing mechanisms that are uniquely available to environmental water, where such mechanisms could be of wider benefit (such as shepherding arrangements). Further, we reiterate the view expressed in our recent *Submission to the Victorian Parliamentary Inquiry into the Management, Governance and Use of Environmental Water*¹⁰ that held environmental water should be placed on the same footing as water held for other purposes and that environmental water holders should be treated like any other water user:

- be subject to the same trading and carryover rules as other users
- pay the appropriate and transparent charges for water infrastructure services provided to environmental water holders
- face the same charges as other users for the same infrastructure services.

DRAFT RECOMMENDATION 5.3

Where governments own significant environmental water holdings, they should ensure that decisions on the use of the holdings are made by independent bodies at arm's length from government.

The Australian and New South Wales Governments should review current governance arrangements for held environmental water to ensure holdings are managed:

- a. independently of government departments and political direction
- b. by statutory office holders with an appropriate range of expertise.

Australian, State and Territory Governments should enhance the National Water Initiative to align with this recommendation.

¹⁰ ACCC (2017), *Submission to the Victorian Parliamentary Inquiry into the Management, Governance and Use of Environmental Water*. Available at: <https://www.accc.gov.au/system/files/ACCC%20submission%20to%20the%20Victorian%20Parliamentary%20Inquiry%20into%20the%20Management%2C%20Governance%20and%20Use%20of%20Environmental%20Water.pdf>

ACCC RESPONSE

The ACCC supports draft recommendation **5.3**, noting that the recommendation could apply generally to all NWI parties,¹¹ and that there are currently a number of inquiries underway that are considering these issues. Final reports from several of these inquiries are due to be provided in early December 2017.

DRAFT RECOMMENDATION 5.4

Australian, State and Territory Governments should ensure there are clear roles and responsibilities for managing environmental water in shared resources, with no duplication. Consistent with this principle, The Living Murray program should be disbanded as there is no clear rationale for its continued existence in the context of the Murray-Darling Basin Plan. Each Basin jurisdiction should manage its share of former Living Murray entitlements as part of its broader portfolio of held environmental water. The Murray-Darling Basin Authority should complete the divestment of its holdings.

ACCC RESPONSE

The ACCC supports in principle the minimisation of duplication of roles and responsibilities for managing environmental water in shared resources, where possible.

If The Living Murray program is disbanded, care should be taken to preserve the knowledge and capabilities developed through the administration of that program.

DRAFT RECOMMENDATION 5.5

Where capable partners are available, Australian, State and Territory Governments should devolve the use of held environmental water to the **lowest practical** level, consistent with the principle of subsidiarity. Australian, State and Territory Governments should enhance the National Water Initiative to align with this recommendation.

ACCC RESPONSE

The ACCC notes that the principle of subsidiarity should be cautiously adopted, being appropriate in some but not all circumstances. Effective implementation of subsidiarity relies upon good governance arrangements, with clear overarching management frameworks and objectives and strong monitoring and accountability mechanisms. These elements must be in place and actively pursued to ensure achievement of cross-jurisdictional/national goals commitments.

DRAFT RECOMMENDATION 5.6

Australian, State and Territory Governments should improve **monitoring, evaluation, auditing and reporting** to demonstrate the benefit of allocating water to the environment, build public trust in its management, keep managers accountable and make better use of environmental water over time.

Priorities are:

- a. Australian, State and Territory Governments should increase their focus on monitoring

¹¹ For example, chapter 5 refers in the body text to the need to review governance arrangements in South Australia as well as New South Wales and at a Commonwealth level. PC, Draft report, p.141.

environmental and other public benefit outcomes — not just flow delivery — where additional effort would be commensurate with the risk to, and value of, those outcomes

b. monitoring and evaluation should involve collaborative and complementary partnerships, consistent methods that enable the synthesis of outcomes across different temporal and spatial scales, and long term investment. In the Murray-Darling Basin, governments should develop a strategy to coordinate monitoring and evaluation of the outcomes of environmental flows, both planned and held

c. all managers of environmental flows should publicly report on whether outcomes have been achieved or not, and the reasons why

d. Australian, State and Territory Governments should establish arrangements for independent auditing of environmental flow outcomes to support transparency

e. managers of held environmental water should use the results of monitoring, evaluation and research to improve water use as part of an adaptive management cycle. To achieve this, managers should clearly allocate responsibility and provide adequate resourcing for adaptive management.

Australian, State and Territory Governments should enhance the National Water Initiative to align with recommendation 5.6 (e).

ACCC RESPONSE

We support the priorities identified in draft recommendation 5.6 to improve monitoring, evaluation, auditing and reporting, and increase focus on achieving and measuring public benefit outcomes.

DRAFT FINDING 6.2

The New South Wales Government's definition of 'full cost recovery' is not consistent with the requirements of the National Water Initiative to achieve lower bound pricing.

ACCC RESPONSE

We agree with the PC's draft finding that the NSW definition is not consistent with the NWI as it does not provide for the recovery of capital costs, so the definition does not necessarily meet either the upper or lower bound pricing criteria.

We encourage consistent interpretation of the NWI pricing principles. Definitions of key principles and concepts could be reviewed as part of a broader review of the NWI.

We note recommendations 4-A¹² and 4-B¹³ in the ACCC's 2016 advice in which the ACCC expressed its intention to provide further guidance on the Basin water charging objectives

¹² Recommendation 4-A relevantly provided that:

The ACCC will review its guidance materials and work with Basin State regulators and other industry stakeholders to develop more practical and detailed guidance on the interpretation of, and the interaction between, the Basin Water Charging Objectives and Principles. This will include:

- interpretation of key terms such as "perverse or unintended pricing outcomes";
- improved identification of and links between the infrastructure services provided and how infrastructure charges are determined to recover the costs of service provision; and
- cost allocation and the basis for determining charging areas (for example, where charging areas are based on geographic areas).

ACCC (2016), [Review of the Water Charge Rules - Final advice](#) (Final Advice), p. 21.

¹³ Recommendation 4-B relevantly provided that:

and principles in Schedule 2 of the Water Act 2007 (which adopt the NWI objectives and principles) and to revise its *Pricing principles for price approvals and determinations under the Water Charge (Infrastructure) Rules 2010*.¹⁴ These actions would be relevant to any review of the NWI pricing principles, and would ideally be developed under a consistent framework. However, action to give effect to the ACCC's recommendations has been deferred while the Minister considers the ACCC's advice.

DRAFT RECOMMENDATION 6.1

State and Territory Governments should ensure that independent economic regulation is in place for all urban water service providers of an appropriate scale, to further promote efficient service delivery.

Priorities are:

- a. extending independent price regulation to retailer distributors in south east Queensland and the Northern Territory's Power and Water Corporation
- b. establishing a standing reference for the Economic Regulation Authority in Western Australia and the Queensland Competition Authority to set or review prices.

ACCC RESPONSE

We support in principle draft recommendation 6.1. The ACCC does not have a regulatory role in urban water, but supports the application of the NWI and associated pricing principles in a consistent way across all (urban) water users so that competition for resources is on an equal footing, independent economic regulation is in place and the same general benefits of economic efficiency and consumer protection can be attained across the economy. The ACCC could usefully contribute to preparation of guidelines on this matter.

We also consider that clarity by the PC on the degree of independence required would be beneficial.

DRAFT RECOMMENDATION 6.2

To promote competition by comparison, Australian, State and Territory Governments should ensure that performance monitoring data are transparently reported for providers of all sizes and subject to independent scrutiny.

Priorities are:

- a. the Queensland Government extending the reporting of financial information to service providers with fewer than 10 000 connections
- b. the New South Wales and Queensland Governments requiring appropriately qualified independent bodies to review financial performance frameworks to ensure that the pricing practices of regional service providers are monitored for consistency with National Water Initiative pricing principles
- c. the Bureau of Meteorology, and the New South Wales and Queensland Governments, requiring providers to report a financial return metric that excludes developer charges and

The ACCC will work with Basin State economic regulators to ensure the Pricing Principles reflect regulatory best practice. The ongoing revision of the Pricing Principles can also serve as a useful platform for the development of nationally consistent approaches to regulatory issues in the rural water sector.

ACCC, Final Advice, p. 31.

¹⁴ ACCC (2011) *Pricing principles for price approvals and determinations under the Water Charge (Infrastructure) Rules 2010*. Available at: <https://www.accc.gov.au/publications/water-charge-infrastructure-rules/pricing-principles-for-price-approvals-determinations-under-the-water-charge-infrastructure-rules>

contributed assets alongside the economic real rate of return metric.

ACCC RESPONSE

We support in principle draft recommendation **6.2**, insofar as it seeks to implement consistent independent monitoring across all jurisdictions, to allow pricing practices to be assessed for compliance with the NWI Pricing Principles. However, the extent of monitoring for smaller operators should take account of their size and capacity.

In relation to **6.2 (c)**, we agree that it is useful to have both metrics, but view this issue as an example of the desirability of involving Commonwealth and state and territory economic regulators in a national review of the NWI Pricing Principles and the associated metrics to be monitored and reported on.

DRAFT FINDING 6.3

In some cases integrated water cycle management (IWCM) projects will be justified by their benefits to a single beneficiary. In other cases, the multiple potential benefits of these approaches, such as improved liveability and ecological health of urban waterways, mean that collaboration across multiple beneficiaries will be required to capture these benefits. To ensure that this complexity does not mean that cost effective IWCM opportunities are missed, governments should ensure that material barriers and distortions to the adoption of IWCM approaches are removed from the general policy framework.

ACCC RESPONSE

We note the importance of considering how legislative or regulatory criteria for determining charges may act as barriers to the adoption of IWCM.

DRAFT RECOMMENDATION 6.6

To improve service efficiency and address remaining water quality issues, funding arrangements for local water utilities in regional New South Wales and regional Queensland should be significantly reformed.

These States should replace existing capital grants to water utilities with Community Service Obligation payments that are not tied to capital expenditure, and are tightly targeted at unviable (high cost) regional and remote services.

ACCC RESPONSE

We support in principle draft recommendation **6.6** on reform of funding for local water utilities regional New South Wales and Queensland.

We also support adoption of an NWI-consistent approach to funding and Community Service Obligations (CSOs) that targets areas of need (rather than providing capital subsidies) and is limited to public benefits.

The NWI Pricing Principles give little guidance on CSOs, but appear to envisage CSOs primarily as subsidies to allow affordable prices for water services below full cost. CSOs can also be obligations to provide a service (e.g. for health reasons) beyond what would be commercially provided. If these are applied across all providers they would not necessarily justify a subsidy except in areas where the cost is considered beyond the means of

customers. Further principles for funding CSOs could be considered as part of the proposed review of the NWI (see discussion in section 2 of this submission).

DRAFT RECOMMENDATION 6.7

Local water utilities and State Governments in New South Wales and Queensland should strategically examine opportunities to improve service delivery through collaboration. Contingent Community Service Obligation payments may provide an opportunity to promote this collaboration.

ACCC RESPONSE

We support in principle draft recommendation **6.7**, with qualifications. We agree that collaboration could improve efficiency of water supply, but note that it may potentially result in parties engaging in anti-competitive conduct in breach of the *Competition and Consumer Act 2010*. The ACCC can 'authorise' businesses to engage in certain anti-competitive arrangements or conduct when it is satisfied that the public benefit outweighs the public detriment, including from any lessening of competition.¹⁵ The ACCC has authorised numerous arrangements where local councils and other small buyers collaborate on purchasing or engage in collective bargaining, where it allows the parties countervailing power against larger suppliers and provides public benefits through lower prices.¹⁶

DRAFT RECOMMENDATION 7.1

State and Territory Governments should ensure the delivery of government owned irrigation infrastructure services is underpinned by full cost recovery and economic regulation that is proportionate to the scale of the regulated service.

Priorities are:

- a. any terms of reference issued to the Queensland Competition Authority by the Queensland Government for advice on the pricing of irrigation infrastructure services should be aligned to the National Water Initiative Pricing Principles. The reason(s) for any Government decision to diverge from price recommendations based on those principles should be published
- b. the Western Australian Government should amend the role of the Economic Regulation Authority (ERA) so that irrigation bulk water customers can request the ERA to review the infrastructure prices and / or services proposed by Water Corporation (WA) as part of bulk water supply contract negotiations
- c. the Tasmanian Government should amend the role of the Office of the Tasmanian Economic Regulator (OTTER) so that irrigation bulk water and distribution customers of Tasmanian Irrigation can request OTTER to review the infrastructure prices and / or services of Tasmanian Irrigation
- d. an equitable share of the cost of any price review requested by users should be treated as a regulatory cost and passed through to users at the discretion of the bulk water supplier in Western Australia and Tasmania.

¹⁵ Section 88 of the *Competition and Consumer Act 2010* provides for authorisations for conduct that may be illegal under section 45.

¹⁶ <http://registers.accc.gov.au/content/index.phtml/itemId/6031>

ACCC RESPONSE

We support the application of NWI Pricing Principles in a consistent way across all water services, as outlined in response to draft recommendation 6.1. Draft recommendation 7.1 is consistent with 2016 advice on the water charge rules and our submission to the PC's issues paper regarding charges in MDB (to be full cost recovery subject to NWI lower/upper bound criteria). We supported full price determinations under Part 6 only for bulk water service providers or cross-jurisdictional operators (generally large monopoly operators) and accept that lighter handed regulation is appropriate for smaller, generally member-owned IIOs.¹⁷

The PC's draft recommendation 7.1 (a) about the Queensland Competition Authority is consistent with our submission and our 2016 advice. The ACCC proposed in its final advice (2016) that bulk operators in Queensland be subject to Part 6 price regulation unless State legislation is changed to provide for independent price determination that uses a basic cost recovery criterion, that is:

'the regulator should be satisfied that forecast revenue from infrastructure charges is reasonably likely to meet, and will not materially exceed, the prudent and efficient costs of providing infrastructure services.'

This criterion is less comprehensive than NWI principles, but would be an acceptable basic approach.

DRAFT RECOMMENDATION 7.2

Relevant jurisdictions should ensure that the costs of River Murray Operations (RMO) are recovered from water users. RMO costs should also be subject to a periodic independent review. Specifically:

- a. South Australia should pass through RMO costs to bulk water entitlement holders
- b. RMO should be subject to transparent and independent five yearly efficiency reviews overseen by the economic regulators in New South Wales, Victoria and South Australia. The next review should be completed by 31 December 2019.

ACCC RESPONSE

We support draft recommendation 7.2 to establish periodic independent cost recovery and efficiency reviews for RMO as preferable to the existing situation where any such reviews are ad hoc. We note potential advantages of the MDBA levying charges for RMO services directly on its users (primarily other infrastructure operators, rather than private diverters).

The ACCC stated in its 2016 advice that:

Reviews of MDBA's costs and efficiency have been done and can be done further by private consultants.¹⁸

We agree that the economic regulators in New South Wales, Victoria and South Australia could oversee the proposed efficiency reviews, noting that coordination of such a review involving three separate jurisdictional regulators would be crucial. There would be benefit in the process and framework for the review being consulted on and settled ahead of the review being undertaken.

As recognised by the PC, the ACCC does not see itself assuming the role of conducting efficiency reviews for RMO. However, if the MDBA was to levy fees for service provided in performing its functions, this would trigger an ACCC role in reviewing (and possibly

¹⁷ ACCC (2017), *Submission to Productivity Commission's Issues Paper on National Water Reform*. (issues Paper Submission) pp.27-28; ACCC, Final Advice, pp. 149-151.

¹⁸ ACCC, Final Advice, p.244.

determining) those charges. Section 212 of the *Water Act 2007* provides for the ACCC to review the reasonableness of any fees for service charged by the MDBA.¹⁹ Further, where infrastructure charges are imposed, the ACCC considers that the Water Charge (Infrastructure) Rules 2010 would be likely to capture the MDBA as an operator subject to price approvals or determination under Part 6 of those rules. In its 2016 advice, the ACCC proposed that the water charge rules should more clearly provide for price determination requirements by the ACCC to apply to cross-jurisdictional operators such as the MDBA under a revised Part 6. The Minister for Agriculture and Water Resources is currently considering this advice and no amendments have been made to Part 6 at present.

There would be important advantages to the MDBA levying charges, including:

- making the funding of MDBA activities more transparent
- making cost recovery more consistent between the States
- requiring a more explicit consideration of the beneficiaries and distribution of costs
- satisfying calls for a more thorough efficiency review, and
- providing greater certainty for the MDBA's revenue flows.

NSW and Victoria have each adopted a framework for imposing charges on water users to recover a contribution towards State government funding of the MDBA. The State governments estimate the portion of their contributions that should be recovered from water users rather than general taxpayers, and require the infrastructure operators (WaterNSW and GMW) to recover that amount in additional charges on their customers. However, under this approach, the transparency of cost allocation and the opportunities for efficiency review are limited, and the MDBA's receipts still depend on annual contributions from the governments which can vary from year-to-year.

There would be establishment and administration costs in implementing a direct charging approach for RMO. Detailed consideration would have to be given to a number of issues including the treatment of existing RMO assets and the approach to financing future investments. However, the nature of the advantages listed above could be similar to those that have flowed from corporatizing and regulating the bulk water suppliers in NSW and Victoria.

DRAFT FINDING 7.2

The transfer of existing irrigation distribution networks to local ownership and management in New South Wales, South Australia, Western Australia and parts of Queensland has benefited irrigators. In exchange, irrigators have accepted responsibility for all the risks and costs associated with ownership — including the potential for, and costs of, a distribution network's financial failure.

Local ownership and management is the preferred model for any new distribution network. In contrast, the transfer of existing government owned distribution networks to local ownership needs to be considered on a case by case basis.

There are rules in place to limit the exploitation of market power by distribution networks in the Murray Darling Basin. Those rules and the approach to their enforcement:

- are proportionate to the risk posed and potential detriment
- are focused on outcomes and seek to avoid undue limits on the ability of networks to manage their business risks (such as declining water delivery volumes)
- have been subject to a transparent review process to ensure they remain fit for purpose.

¹⁹ The provision of advice is triggered by the proposal to charge the fees and the charges being prescribed in Regulations: *Water Act 2007* (Cth), s.212(2)(a).

ACCC RESPONSE

We acknowledge the advantages of local ownership as identified by the PC, but note that this ownership structure will not automatically limit exploitation of monopoly power or provide protection of customers unless strong governance arrangements are in place. Further, we note that irrigators are not the sole customers or investors – the Australian government, for example, is also a key customer of, and investor in, infrastructure operators' networks.

We believe that the rules currently in place can be improved to more effectively limit monopoly power of irrigation infrastructure operators (IIOs). While the Water Charge Rules applying within the Murray-Darling Basin have been subject to the ACCC's review and advice to the Minister, the rule changes proposed by the ACCC have not yet been implemented, apart from the removal of the requirement to prepare network service plans. Remaining proposals for rule changes include:

- broader prohibition of price discrimination and discriminatory distributions
- enhanced transparency of price schedules.

The Minister for Agriculture and Water Resources is currently considering the balance of the ACCC's advice.

DRAFT FINDING 7.4

The past failure of governments to deliver new irrigation infrastructure projects that are financially viable, environmentally sustainable and economically efficient is due to a combination of factors, including:

- prices that do not reflect the full cost of infrastructure due to governments providing grants for what is essentially private infrastructure
- poor analysis of the viability of new infrastructure projects
- an absence of robust water entitlement and planning frameworks.

ACCC RESPONSE

The ACCC does not have a role in analysing the efficiency of infrastructure investments per se, but our earlier submission noted the difficulty of setting full-cost prices when uneconomic investments have been made.

The ACCC agrees with PC that these are factors leading to uneconomic projects, but notes such failures are likely to follow if there is a more fundamental political will for projects to proceed without great concern for economic viability.

DRAFT RECOMMENDATION 7.3

Governments should not provide grant funding for irrigation infrastructure, or that part of infrastructure, that is for the private benefit of irrigators. Rather, Australian, State and Territory Governments should ensure that:

- a. National Water Initiative-consistent water entitlements and planning are in place before any new irrigation infrastructure is considered (including infrastructure being financed under the Northern Australian Infrastructure Facility)
- b. government grant funding is limited to those projects, or parts of projects, delivering a public good. Any grant funding should be subject to an independent analysis of the project being completed and available for public comment before any government announcements on new infrastructure are made. The analyses should establish that the project will be:

- environmentally sustainable
 - economically viable and deliver public benefits that are at least commensurate with the grant funding being provided
 - c. government financing (such as loans) for infrastructure generating private benefits should only be provided after:
 - an independent assessment has confirmed the finance can be repaid on commercial terms. The assessment should be released for public comment before any announcement on new infrastructure is made
 - robust governance arrangements have been put in place to deliver merit based decision making and the ongoing monitoring of (and public reporting on) the government's investment
 - sufficient water entitlements have been sold to reduce the project's risk profile and provide assurance the finance will be repaid.
- Australian, State and Territory Governments should enhance the National Water Initiative to align with recommendations 7.3 (a) to 7.3 (c).

ACCC RESPONSE

We strongly support the PC's draft recommendation **7.3**. It is consistent with the concerns expressed by the ACCC in its submission to the issues paper over uneconomic investments and consequent difficulty of setting full-cost prices.

While we recognise that assessing the share of private versus public benefits from a project may be difficult, there are approaches to deal with this issue. The PC could usefully elaborate on such approaches in its final report.

We also suggest that PC should clarify:

- the required standards for benefit-cost analysis
- processes to review compliance and enforce those standards
- ways to improve the transparency of assessments prior to investment decisions being made and
- the role for an independent body in overseeing the analysis of options and decision-making on government investments.

DRAFT FINDING 8.1

Ongoing research and capacity building will be central to Australia's ability to deliver the sustainable management of water resources in the face of challenges from climate change, population growth and increasing community expectations.

DRAFT RECOMMENDATION 8.1

Australian, State and Territory Governments should:

- a. identify the key knowledge and capacity building priorities needed to support the ongoing implementation of the National Water Initiative (including the revisions and enhancements recommended in this report)
- b. develop mechanisms through which the jurisdictions can work cooperatively and share knowledge to build overall capability and capacity.

Australian, State and Territory Governments should update relevant provisions in the National Water Initiative to align with recommendations 8.1 (a) and 8.1 (b).

ACCC RESPONSE

We agree with the PC's position in its draft finding and draft recommendation **8.1**, but note that the PC stops short of recommending additional funding or indicating the source of these funds. In contrast, the PC does mention funding under draft recommendation **9.1** regarding renewal of NWI (p.278), where the main responsibility is considered to rest with States and Territories, but says Australian Government could provide "funding support toward activities that encourage and facilitate reform in areas of national interest". The PC may wish to express a view with regard to the funding arrangements to support capacity building.

DRAFT RECOMMENDATION 8.2

Where Governments consider there are significant and rapid adjustment issues affecting communities as a consequence of water reform, the response should:

- a. avoid industry assistance and subsidies
- b. consider all the factors impacting on the community (not just water reform)
- c. target investment to developing the capacity of the community to deal with the impacts of structural adjustment
- d. be subject to monitoring and publicly reported evaluation of outcomes.

Australian, State and Territory Governments should revise relevant provisions in the National Water Initiative to align with recommendations 8.2 (a) to 8.2 (d).

ACCC RESPONSE

While we support the principle of generally avoiding public subsidies to industry, we agree with and refer the PC to the position expressed in an earlier PC report on "Structural Adjustment – Key Policy Issues (October 2001) that noted when reforms lead to significant transitional costs, there may be a need to assess the scope for reducing those costs and how this might be best achieved. As the PC noted, "the social security and tax systems, as well as generally available adjustment measures, will usually be the most appropriate vehicles for assisting the adjustment process and moderating adverse distributional impacts. However, they are not designed to handle all contingencies and in some circumstances there is a role for additional measures to promote equitable outcomes and improve the efficiency of the adjustment process."²⁰ The 2013 Intergovernmental Agreement on National Drought Program Reform²¹ and the earlier recommendations of the PC Report on Government Drought Support (May 2009) are also relevant in the context of rural adjustment as a consequence of water reforms.

We note reference to "the community" in this draft recommendation, and observe that communities are not necessarily homogeneous in their needs and preferences, and that policy makers need to be conscious of the many different voices within communities.

DRAFT RECOMMENDATION 9.1

Australian, State and Territory Governments should recommit to a renewed National Water Initiative through COAG by 2020. This should:

- a. maintain the achievements in water entitlements and planning, water markets, water accounting, water pricing and governance, knowledge and capacity building, and community

²⁰ PC (2001), *Structural Adjustment – Key Policy Issues*, p.xviii. Available at: <http://www.pc.gov.au/research/supporting/structural-adjustment-issues>

²¹ COAG, Intergovernmental Agreement on National Drought Program Reform (2013), available at: <http://www.agriculture.gov.au/ag-farm-food/drought/drought-policy/drought-program-reform/iga-national-drought-program-reform>

engagement delivered by the current National Water Initiative as the key foundations underpinning sustainable water resource management and efficient infrastructure service delivery

b. revise a number of policy settings:

- incorporating extractive industries and alternative water sources into water entitlement frameworks
- water planning to take account of climate change and enable ongoing optimisation
- Indigenous access to water for economic purposes
- arrangements for water trading between irrigation and urban sectors
- better targeted adjustment assistance

c. significantly enhance policy settings relating to:

- urban water management to ensure innovative and efficient provision of services in the future under the combined pressures of population growth and climate change
- environmental water management to ensure maximum return on government investment in this area
- decision making on building and supporting new infrastructure for agriculture.

ACCC RESPONSE

The ACCC supports the PC's draft recommendation **9.1**, calling for renewal of the NWI by 2020. We agree that it is timely to review and refresh the NWI, recognising that there has been much change and experience since the original NWI in 2004.

The ACCC could draw on its roles and experience to contribute to the development of a renewed NWI. In particular, it could contribute to a review of the NWI pricing principles (for example, assisting with development of materials to clarify applicable standards and key concepts such as upper and lower bound pricing, capital cost recovery and the application of CSOs) as well as participate in reforming the NWI treatment of principles for cost recovery of water planning and management. The ACCC is already participating in interjurisdictional review of trade restrictions and trading rules.

The renewed framework should seek to provide greater clarity on how it prioritises its sometimes conflicting economic, social and environmental goals. In particular, it may be appropriate to consider whether the "cornerstone" of the NWI should continue to be water use efficiency, or whether that goal should be better defined and nuanced.

The definition of water use efficiency is not discussed by the PC, and although there is not one 'right' definition, different interpretations can lead to different policy goals and outcomes. It is well known that increases in water use efficiency can result in consumption of more rather than less water, and in reductions in return flows to neighbouring farms and the environment. Water use efficiency schemes, as a minimum, should take into account where water was taken from and its impact – favouring water savings from reduced evaporation, or reducing return flows into saline groundwater, for example.

In addition, account needs to be taken of other inputs into decision making: increasing water use efficiency does not always increase overall productivity and profitability. It is important to take account of risk, and as water use efficiency increases, an irrigator's ability to adapt to drought can decrease, particularly if they invest in high-yield perennial crops. We note our earlier commentary (in response to draft finding **2.1**) on the need to account for relationships between water use and energy consumption, particularly in considering capital, operation and maintenance costs. Further, given much of the 'low hanging fruit' of water use efficiency has been picked, further gains are likely to come at a substantial cost, making *unconditional* ongoing pursuit of water use efficiency through government subsidies questionable.

4. Other comments

The following section provides comment on selected issues not covered in draft recommendations or findings.

CHAPTER 4 – WATER MARKET INTERMEDIARIES

The PC noted that water market participants often use water broker or exchange when trading water rights and concluded that water market intermediaries bring a number of benefits to the market, including by aiding information flow to irrigators and other water market participants. In drawing its conclusion that increased regulation of water market intermediaries was not justified at this time, the PC noted that:

- Since 2011, when the NWC considered the issue, competitive pressures are likely to have further reduced risks associated with the conduct of water intermediaries.
- Water brokers that join the AWBA are required (under the AWBA Code of Conduct), amongst other things, to have professional indemnity insurance and hold client deposits in bank accounts that are regularly audited.
- Very few stakeholders raised concerns about the water market conduct intermediaries in the course of the PC's consultations. The only submission to the PC that expressed a view about water market intermediaries (NSW Irrigators' Council) argued that 'there has not been sufficient instance of maladministration in water broking to justify a significant tightening or regulation of water brokers.' NSWIC also expressed concern that the introduction of stricter and more costly financial administration measures on brokers will tend to make small trades unviable and disadvantage smaller water brokers, and will add significantly to the cost of water trades to sellers and buyers.
- The ACCC has published guides on fair trading obligations for water brokers and exchanges, and irrigators' fair trading rights when using water brokers and exchanges.

ACCC RESPONSE

The ACCC agrees with the PC's assessment that increased regulation of Water Market Intermediaries (WMI) does not appear to be justified at this time, based on presently available information. The Australian Water Brokers Association (AWBA) voluntary code of conduct represents an effort to develop best practice industry standards. Further work could be done by the AWBA and others to raise awareness of the benefits of commitment to – and compliance with – this standard. The ACCC receives very few complaints about WMI behaviour and the costs of increased regulation can be significant. The ACCC notes, however, that the small number of complaints it receives may reflect a lack of systemic issues; alternatively, it may reflect a lack of awareness of the existing consumer protections, and the ACCC's role in investigating complaints about brokers. The ACCC will continue to take steps to raise awareness of its role and interest in WMI-related complaints within the water sector.

APPENDIX B – COST RECOVERY FOR WATER PLANNING AND MANAGEMENT ACTIVITIES

The PC concluded:

There is scope to improve cost recovery arrangements in Queensland, Western Australia, Tasmania and the Northern Territory.

.....There may be scope to improve arrangements in Victoria, South Australia and ACT whose broad based levies lack the precision of New South Wales' approach.²²

However, the PC was concerned to proceed in this direction only if the benefits would exceed the costs, and planning activities were cost-effective.

ACCC RESPONSE

We support the PC's assessment, noting that inconsistency of arrangements and progress on cost recovery for WPM across Basin States has been outlined in the ACCC's annual monitoring reports, its 2009 water charge rules advice and in its 2016 advice on amendments to the water charge rules (which recommended amending the existing regulatory approach in the MDB – not yet implemented).

Both the ACCC's 2016 advice and its submission to the PC issues paper recommended that governments reconsider the approach to WPM cost recovery through the NWI. The ACCC' submission to the PC's issues paper stated:

Noting parties' varied approaches to cost-recovery for WPM, there has been limited progress on adopting consistent approaches which give effect to the elements specified in the NWI, with no significant progress on implementing the NWI commitments since 2006, or on the associated NWI Pricing Principles since 2010. The ACCC considers that it would be appropriate for NWI parties to review their commitments in cl. 64, 67 & 68, and the associated NWI Pricing Principles, to determine the extent to which they remain committed to implementing them.²³

While the PC's draft report acknowledges the scope for improvement in some jurisdictions and with respect to some charges, it does not explicitly call for the parties to the NWI to revise and, where appropriate, recommit to cost recovery for WPM. The PC identifies that in some circumstances, the costs of implementing the current NWI commitments could outweigh the benefits. We would encourage the PC to recommend that the policy framework be revised to reflect this position and provide parties with guidance on when cost recovery approaches are appropriate.

APPENDIX B – RURAL DISTRIBUTION PRICING

The PC cited earlier views:

NWC found that lower bound price outcomes were being achieved in the MDB in 2014. However, outside the Murray–Darling, the NWC found information on, and transparency of, the extent of cost recovery to be 'generally poor' (with the exception of Harvey Water (WA) and Tasmanian Irrigation).

It is generally accepted that there are sufficient incentives for user-owned distribution networks to operate efficiently, reflect the associated costs in prices and maintain the infrastructure network (ACCC 2016).

²² PC, Draft Report, p.370-1

²³ ACCC (2017), Issues Paper submission, p.13.

Accordingly, the Commission has not directly considered the pricing outcomes in its assessment of progress for New South Wales, South Australia and Western Australia where distribution networks are user-owned. However, these networks have a degree of market power and regulation in place to limit the abuse of that market power in price setting — the Commission considers those issues in chapter 7...²⁴

ACCC RESPONSE

The ACCC's advice on WCR quoted the submissions from member-owned operators as broadly commenting that there are sufficient incentives for member-owned operators to provide outcomes that are in the interests of their members, and that there are mechanisms in place for the operators to be accountable to their members (ACCC 2016, p.51). However, the ACCC remains concerned that:

- there is the potential for member-owned operators to use their monopoly power to discriminate in favour of certain customer groups
- there may not be adequate transparency around infrastructure investment and the price setting process.²⁵

Member-owned operators can be expected to charge prices that fully cover on-going operating expenses, but the extent to which they provide for past or future asset cost recovery is less clear. The situation is clouded by periodic government grants towards infrastructure renewal and upgrade. Against this background, we suggest that the PC further consider the value of occasional monitoring²⁶ and reporting on rural IIO costs, particularly to assess provision for capital replacement and progress towards upper bound pricing. This would also implement a goal of the NWI that has lapsed in recent years. Any such monitoring should still make allowance for the size and capacity of operators.

²⁴ PC, Draft Report, p.359

²⁵ ACCC, Final Advice, pp.42, 47-48

²⁶ The ACCC monitors charges for operators (including IIOs) in the Murray-Darling Basin but does not currently monitor the degree to which such charges recover costs or provide for future asset replacement.