



**RICEGROWERS' ASSOCIATION  
OF AUSTRALIA INC**

**SUBMISSION TO THE AUSTRALIAN  
COMPETITION & CONSUMER  
COMMISSION (ACCC)**

**Murray-Darling Basin water markets inquiry**

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## 1. INTRODUCTION

The Ricegrowers' Association of Australia (RGA) welcomes the opportunity to provide our submission to the ACCC Murray-Darling Basin water markets inquiry. As the ACCC has stated in its discussion paper, the water market is intended to drive an adaptive, efficient and productive irrigated agriculture sector, while supporting a sustainable level of water diversion.

However, such a far-reaching reform will inevitably result in some unforeseen outcomes (positive and negative) due to, for example, changes in irrigator behaviour; the entry of investors who do not own land or entitlement; and, the challenges of delivering water to meet demand while also managing a living, dynamic river system to improve its environmental health.

RGA has consistently called for an adaptive management approach to water reform, including the 2012 Murray-Darling Basin Plan. Such an approach recognises that much has changed over the last 15 years since the 2004 National Water Initiative. Many free market model assumptions informing the NWI and the Basin Plan, including water market design, operation and trading rules, are in many respects driving both negative and positive outcomes.

Free market water principles assume, among other things, that when prices get too high, they will be moderated by participants refusing to pay until the price drops. The principles also assume that when prices get too high, the market will drive the creation of cheaper substitutes through innovation, and that all participants have equal access to information and equal bargaining power.

None of these apply in the water market. The market is opaque, to say the least. Those with permanent plantings who have chosen to take the risk and not to buy entitlements, have little choice but to pay in a hot temporary market or lose years of investment and returns if trees and vines die. Those consequently priced out of the market such as rice growers have little alternative but to stop producing altogether, with serious socio-economic impacts on their irrigation-dependent service industries and rural communities.

And water as a product has no substitute for what it does. Greater water use efficiency is a proxy substitute, but that option is all but exhausted after more than a decade of environmental water recovery and drought driving greater efficiency. Further efficiency gains will be incremental in terms of substituting for water use to grow food and fibre.

In this submission, the RGA will focus on the priority areas we believe require federal and State actions. We look forward to informing material changes that will instil greater confidence that the water market is working first and foremost in the best interests of all Basin stakeholders.

## **2. THE RICEGROWERS' ASSOCIATION OF AUSTRALIA**

The RGA is the collective voice of Australian rice growers, representing around 1200 voluntary members. The RGA's main objective is to provide members with strong and effective representation on issues affecting the viability of their businesses, their communities and their industry.

The RGA is made up of eight branches located across the Riverina rice growing regions of NSW and Victoria. Each branch annually elects representatives to form the RGA Central Executive. The Central Executive represents their respective branches in determining RGA policy and projects.

The RGA is a member of the National Farmers' Federation, National Irrigators' Council and NSW Irrigators' Council.

## **3. THE AUSTRALIAN RICE INDUSTRY**

The Australian rice industry is located predominantly in the Riverina region of south-west NSW, with two small industries also in the Northern Rivers region of north NSW and in Northern Queensland.

The Australian rice industry relies on irrigation, mainly sourced from the Murray and Murrumbidgee river valleys. Provided water is available, the Australian rice industry is considered one of the world's most successful, delivering significant yields while leading the world in water use efficiency.

In a typical year the Australian rice industry produces around 800,000 tonnes of paddy rice with a farm gate value of around \$350 million. About 80 per cent of this product is exported. With value adding, the total industry worth is well over \$1 billion each year.

It can be further argued that the full economic potential of the Australian rice industry has not yet been realised with rice being excluded from three recent free trade agreements: Japan, China and North Korea. These markets represent significant potential for the Australian rice.



The rice industry is a significant economic contributor to the Riverina region of NSW. The towns of Griffith, Leeton, Coleambally, Finley, Jerilderie, Deniliquin, Wakool and Moulamein are highly dependent on rice production for their social and economic wellbeing. Additionally, rice growers have individually invested more than \$2.5 billion in land, water, plant and equipment and collectively invested around \$400 million in mill storage and infrastructure through SunRice. They are also mixed farmers, using their land outside the rice season to grow winter crops.

While the Australian rice industry is very small by world standards, it remains a very competitive supplier of premium rice products into world markets.

## 4. PRIORITY FOCUS AREAS FOR WATER MARKET REFORM

### 4.1. Market transparency

Transparency is the foundation for confidence that the water market is fair; that all participants have equal access to relevant information; and that unconscionable conduct with the potential to manipulate supply and price on the temporary market is exposed.

The temporary water price in large part determines the return on growing food and fibre. Allocation trade in the market as currently structured is the most vulnerable to anticompetitive behaviour. Rice and dairy farmers could be forced out of production based on individual circumstances under extreme dry conditions, a situation that does not generally present in a season that yields more supply. Many horticultural sectors are now reaching the limits where water costs more than the anticipated return from their high-value crops.

RGA acknowledges that water prices are a function of supply and demand, especially in dry years with extreme scarcity and warm temperatures such as 2015/16, 2018/19 and 2019/20. However, in a drought-affected market when the allocation water market is shallow, a few large traders/brokers are potentially able to influence supply on the temporary market, and therefore prices through their trading behaviour.

This risk is the subject of much speculation, but whether it is, in fact, occurring is impossible to tell. The southern Basin water market is opaque, to say the least. It is unacceptable that Basin trade data still has no single point of truth. Errors are compounded in inconsistent systems across 47 different

exchanges. Participants are left overly reliant on brokers with a better understanding of true market value, which in turn may be inconsistent with transactions recorded on the three State registers.<sup>1</sup>

Market depth is impossible to gauge when allocation parcels can be listed on multiple broker exchanges, creating a false sense of the true volume of water available to users. We acknowledge that real time price information is provided from the brokers who have registered with Waterflow, but not all brokers are registered so the information on market depth and price remains incomplete.

The reporting of trades can also be clouded by zero dollar trades and the actioning of a sale that may have occurred up to five years previously. The mixing of this data does not allow market participants to accurately understand the true market depth or pricing.

RGA supports a central online trading platform showing all available allocation and entitlement for sale in each trading zone and water system in real time. All commercial trades would be required to go through the central platform, and all buy and sell offers (without multiple listings for the same parcel) would be listed to show market depth. Full disclosure would be required, for example, whether the trade is for a forward lease product, or a spot market trade. Explanations for \$0/ML trades would be required.

In this way, people offering their water for sale would be sure they are getting a fair price compared with others, and buyers could be confident the water they buy from brokers is priced competitively. It would also be obvious if, for example, any one trader swamps the exchange to buy up all low-priced water; this alleged practice described above can go undetected when conducted across multiple private exchanges and public registers.

While a central platform may change the business models of existing water brokers, this is more than outweighed by the benefits of providing more transparent market price and depth information to water users. We emphasise that the water market's objectives amount to supporting all stakeholders that depend on the irrigated agricultural sector as the priority.

A central trade platform covering the whole southern Basin is essential, but we realise this requires agreement among the three southern Basin States. We urge the ACCC to push State Governments to expedite the required negotiations.

We also note the \$13 billion 2007 National Plan for Water Security was also intended to accelerate the implementation of the 2004 National Water Initiative, under which the creation of water markets was a priority. It is not unreasonable to expect the Commonwealth to fund the creation of a southern Basin central trade platform from the roughly \$4 billion remaining for water reforms, leaving market participants to cover only the operational costs through processing fees.

## Recommendations

1. A single exchange portal operating in real time for all entitlement trades.
2. A single exchange portal operating in real time for all allocation trades.
3. A real time, visual portal showing water flows through system, broken down by consumptive, operational, conveyance, environment, and 'other'.
4. A real time, visual portal showing water in storages, showing how much is committed to whom by State, and shortfalls to make up before allocations to high security, general security and other entitlements.
5. A public register of tagged accounts, including volume and locations.

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<sup>1</sup> MDBA Water Market Audit, May 2019.

6. The Commonwealth to fund a central water trade platform from the \$13 billion National Plan for Water Security. Project to include modelling of operational cost implications for market participants.

## 4.2. River operations

The MDBA and the States are responsible for river operations in the Murray and its tributaries. It is a complex task to ensure that enough water is where it needs to be to meet human, consumptive and environmental demand, without eroding the river systems' transmission capacity to the detriment of all water users.

The location and timing of demand for water is changing and is different to what was expected before the water market was created. Demand for water to be supplied further down a constrained river system is completely the opposite of what was originally envisaged, which was that demand for supply would move closer to its source because supply delivery would be more efficient.

The Murray-Darling Basin Plan has further complicated the challenge by creating a large environmental reserve that must also be delivered to improve environmental health in rivers, wetlands, riparian zones and floodplains from the top in the mountains to the Murray mouth. In effect, the Plan has increased demand for environmental water further down the river system.

These changes affect overall supply as water managers operate the system less efficiently in an attempt to meet the changed location and timing of consumptive and environmental demand.

While a constraints agreement to deliver environmental water would ease the competition for supply below the Barmah Choke and other major river system constraints, it is worth noting a market mechanism for the efficient delivery of consumptive water does not exist either. With hindsight, a cap and trade mechanism for supply demand may have averted the current challenges.

The free market model imposed on this dynamic river system does not account for the realities of conveying water vast distances. The Murray, and its major tributaries, the Goulburn and Murrumbidgee rivers, contain natural 'choke' points where the channel capacity reduces and limits the volumes that can be conveyed.

Prolonged, high flows to meet changes in the location and increased volume of commercial and environmental demand are further choking the chokes, with increased silt deposits and river banks slumping and eroding. Since February 2008, the instream deliverability of water in the Murray River has reduced by 21% or 1500ML per day, making the Barmah Choke even more prone to overflowing into the surrounding land, further increasing the risk of conveyance losses.

These losses directly affect the reliability of general security allocations in New South Wales, which are made only after all other commitments have been met. Prior commitments include covering the conveyance losses to meet increased downstream demand for water. Increased demand is in part driven by the Basin Plan market reforms enabling a rapid recent expansion in permanent plantings.

In any other market, freight costs are factored into the cost of the product. Water should be no different. A precedent has already been set with environmental water. The Commonwealth Environmental Water Holder account is debited 50 gegalitres up front and a further 20 per cent of the volumes delivered through the Murray system to cover the losses incurred in conveying that water. In effect, a megalitre of environmental water delivered from above the Barmah Choke is less than a megalitre by the time it gets to Hattah Lakes or the South Australian border.

Similarly, conveyance losses must be factored into all allocation trades downstream from their entitlement source zone in the Murray and its tributaries. The conveyance losses for commercial

trades should be based on a rigorous analysis of losses through the system, rather than relying on the environment's arbitrary 'rule of thumb' scale.

This change would help to restore the reliability of NSW Murray and Murrumbidgee general security entitlements, consistent with commitments in the Water Act 2007 and the 2012 Murray-Darling Basin Plan that the policy reforms would not erode the reliability of anyone's water property rights.

Inter-Valley Trade (IVT) is another key market-related river operations issue. IVT enables irrigators to better manage their business risks, but limits on this trade are in place for good reasons. It is essential that IVT is driven by transparent river hydrology, Snowy Hydro releases and MDBA river operations demands, and not market forces.

Allowing the market to drive IVT enables sophisticated participants to exploit arbitrage opportunities. Tagged licences are symptomatic of the problem, in that they circumvent IVT limits and move the IVT balance further from reopening in a timely manner fair for all market participants.

### Recommendations

1. Conveyance losses must be factored into allocation trades downstream from their source entitlement zone.
2. Conveyance losses must be factored into carryover water used downstream from its source entitlement zone.
3. IVTs should be driven by transparent river hydrology, Snowy Hydro releases and MDBA River Operations demands, and not market forces.
4. An analysis of the volume and location of tagged accounts, and impacts on river delivery capacity and the environment if these accounts are being used to circumvent IVTS.

### 4.3. Market-sensitive government information

As Government agencies are solely responsible for supply to the market, they need to be acutely aware of the market sensitive nature of the decisions they make. They must understand the need for full and immediate disclosure of any information that is or may be market sensitive.

With many agencies involved in determining supply, full transparency of the information is essential. For example, it is critical that timely, accurate and consistent information about supply levels is made publicly available. Similarly, environmental water trades that could open or close trade between restricted trading zones must be disclosed. This transparency is currently missing.

Market participants are constantly trying to assess future supply to the market, using publicly available information and applying the rules that Government agencies use to determine supply. But the information available is inadequate and the rules appear to be inconsistently applied. This makes it impossible for market participants to consistently and accurately determine future supply.

As a principle, market participants should be able to determine future supply to a reasonable level of accuracy, understanding of course that agencies are dealing with a dynamic system with many variables. There are just too many 'surprises' with each new fortnightly allocation announcement, affecting perceptions of future supply, with subsequent market impacts.

**Recommendation** Government agencies need to regularly (ultimately on a daily basis) provide information to the market regarding:

1. the amount of water taken by consumptive and environmental users;
2. the amount of water used for operational purposes and any variations to budget;
3. any variance to supply outside 'normal' operations (i.e. Snowy Required Annual Release (RAR)); and,

4. any change in bias to allocating or conserving increased supply.

#### 4.4. Carryover as a market driver

Carryover is an important risk management tool for irrigators to smooth out peaks and troughs in water supply between wet and dry seasons. The RGA supports the retention of carryover. However, it also recognises that carryover is influencing traders' behaviour on the water market. Large carryover volumes in storage may also be affecting the timing and volume of allocations in a given season, eroding entitlement reliability, especially of NSW general security.

Carryover operates on the principle that individuals should retain ownership of their allocation, including what they don't use. The water market extends this principle of individual rights over collective redistribution, by allowing people to buy and carryover other people's unused water.

Carryover was introduced in New South Wales and later in Victoria to help farmers better manage their business risks. Carryover helped irrigators to make an early start on production in dry years when new season allocations were delayed, and acted as a supply buffer in low allocation years.

The rules vary substantially. In NSW, high security entitlement holders cannot carry over at all. In the Murrumbidgee, general security entitlement holders can carry over 30 per cent of their entitlement volume, but cannot have more than 100 per cent in total in their account combined with new season allocations. In the NSW Murray, general security entitlement holders can carry over 50 per cent of their entitlement volumes, with a 110 per cent cap on the total in their account.

In Victoria, high security entitlement holders can carry over 100 per cent of the volume of their entitlement, and still receive 100 per cent of new season allocation. This private carryover is on top of the public carryover whereby Victorian water managers try to set aside 100 per cent of next year's allocation before they begin allocating for the current season. Victorian low security entitlement holders can also carry over 100 per cent of that entitlement's volume.

In Victoria, water carried over against low reliability entitlements is the last to spill, making this carryover product paradoxically the highest security water available to irrigators, traders and brokers. Similarly, general security entitlements with carryover capability are increasingly being used as a low-risk opportunity to underwrite the reliability of supply for some market participants.

Carryover is delivered even before NSW high security entitlement allocations, which does add value to a general security licence as their carryover is as close to guaranteed as possible. Carryover is therefore an important aspect of that entitlement. Poorly considered changes risk the erosion of a good deal of equity through loss of entitlement value.

On the other hand, while using carryover to increase security of supply may seem to be a good outcome, the practice also diminishes the likelihood and volume of allocation against general security and low reliability entitlements. In NSW and Victoria, carryover commitments must be met from storages each season before water managers can begin to allocate for the current season. Put simply, private carryover is water that in the past would have been classed as unused and returned to the collective pool for reallocation in the new season, increasing water availability for all.

It was never intended that the rights of one group of entitlement holders would be diminished to provide a market opportunity to minimise risk for others. Increased horticultural demand for water is driving increased use of carryover, which in turn ties up more water in storage leaving less for allocation; the cycle feeds off itself, further reducing supply for general security entitlement.

State authorities regularly assess likely carryover levels and their capacity to deliver that carryover when determining further supply to the market. This specifically affects general security entitlement holders and their capacity to access water through allocation. With the erosion of general security reliability (for example, from 82 per cent pre-Basin Plan in the NSW Murray down to 52 per cent now), irrigators are finding they are no longer carrying over unused water but rather being forced into the market to buy temporary water for carryover, to cover the high risk that general security allocations may be lower and later in the next season.

New water products, such as forward supply leases, are also changing the nature of carryover. Investors and brokers use carryover to meet contracted forward lease volumes. If they do not have adequate allocation against entitlements, they too must enter the market to buy carryover water, intensifying competition and putting further upward pressure on prices, particularly in dry years.

Transparency on ownership (commercial, urban, environmental), volumes and source entitlement zone is essential. In the first instance, this will test speculation accusing investors of hoarding water at the expense of water users. Secondly, it will provide insights that may inform a comprehensive review of carryover rules.

Such a review could consider the implications of options being aired in various community forums, such as changing the spill rules on carryover in Victorian low reliability accounts, and changing the permitted proportion of entitlement volume that can be carried over.

**Recommendation** Retain carryover, but undertake modelling for sensitivity testing of the impacts/reliability of general security water entitlements if permissible levels were adjusted.

#### 4.5. Brokers

Prior to the separation of land and water title, water entitlement transactions were dealt with as a component of land sales, which were subject to the state-based regulatory regimes applying to brokers of real estate transactions. This meant the brokers handling these transactions were real estate agents and regulated as such. In NSW, under the Property, Stock and Agents Act 2002 (and associated regulations) real estate agents are required to hold the relevant licence, act in the best interests of clients, disclose all other interests to clients and hold clients' money in trust accounts.

However, these arrangements fell away when land and water titles were separated. Water brokers are unregistered and unlicensed: now anybody can broker these transactions and is not subject to the standards imposed on real estate agents. The current lack of regulatory intervention is exemplified by the fact that the number of intermediaries operating is not known.

Members of the Australian Water Brokers' Association (AWBA) are required to observe its code of ethics and standards. These standards require intermediaries to keep client funds in an account (without specifying administrative standards) and disclose conflicts of interest. But, the voluntary code carries little weight when most brokers are not AWBA members. Irrigators have no recourse if they suspect unconscionable conduct; indeed, there are no rules against insider trading and other behaviours that can potential manipulate supply and price on the temporary water market.

In this context, it is essential that brokers and associated parties are licensed and registered, to discourage insider trading and provide recourse to their clients – no different to the way that real estate agents and stock brokers are licensed, registered and bound by regulations. At a minimum, all brokers should be required to:

- Use trust accounts when handling clients' funds.
- Hold professional indemnity insurance.
- Disclose conflicts of interests.

**Recommendation** Brokers must be licensed, registered and regulated. This includes prohibitions on holding allocation accounts and trading water in their own or associates' right; and, a requirement that they hold clients' water and funds in trust accounts, hold professional indemnity insurance, and disclose conflicts of interest.

#### 4.6. Regulations and institutional settings

While water resource plans and the sustainability of extraction caps imposed under these instruments are outside the scope of the ACCC inquiry, it is important to note that in a Cap and Trade system the rules determining supply are critical to the proper function of the market.

In establishing the rules to ensure compliance with extraction caps, overreach has been demonstrated in the NSW water sharing plans. The subsequent reduction in supply has significant market impacts, particularly the disproportionate impact on general security entitlement holders.

**Recommendation** The NSW Government be directed to review water sharing plans in conjunction with water users and other stakeholders to reinstate the historic reliability of general security entitlements that has been eroded over time without consultation.

State and Commonwealth agencies process most trade transactions. Vast differences in the process and timing of these transactions leave market participants in some States at a disadvantage, especially when windows of opportunity for trade between zones open and close quite quickly.

The costs for these transactions vary significantly, and being monopoly operators there is no market for these State and Commonwealth transaction services. Government agencies are the monopoly providers of many trading transaction services and need to provide consistent fees and timely services that don't impact market participants in one jurisdiction compared to another.

**Recommendation** A single, central platform through which all trade transactions must be transacted, for consistency in fees, timing and form.

In some parts of the southern Basin market, such as South Australia, deficits are permitted to accrue in allocation accounts. The account holders only need bring their balance back to zero at the end of the quarter or at the end of the water year. This gives these accounts an unfair market advantage, as they can freely use water that is not theirs and are then able to replace it by buying water at cheaper non-peak times of the season. This is completely at odds with the NSW and Victorian systems, where allocation accounts deficits are not permitted.

**Recommendation** Consistency across all jurisdictions, prohibiting allocation accounts from going into deficit and fining account holders who use water when their account balance is zero.

## 5. CONCLUSION

Under the National Water Initiative 2004, governments agreed that water entitlement and allocation trade would have no third-party impacts on water entitlement property rights. On several fronts, this principle is being breached through unexpected and unforeseen market behavior; the way governments are managing rivers in response; and, the lack of transparency around market depth, price and market-sensitive government resource management decisions affecting supply.

This is not acceptable: water users were assured that the reliability of their entitlements would not be affected by the 2012 Murray-Darling Basin Plan and other policy reforms to facilitate water trading across the southern Basin.

Optimal operation of the southern Basin water market starts with confidence that it is fair to all participants. In this submission, the RGA has outlined several priority areas requiring further investigation and regulatory change to help build confidence that the market is indeed operating in the best interests first and foremost of a diverse and prosperous irrigated agricultural sector.

## **6. CONTACTS**

For further information please contact:

**Rob Massina**

**President**

Telephone: 0448 999 288

Email: [rmassina@rga.org.au](mailto:rmassina@rga.org.au)

**Claire Miller**

**Acting Policy Manager**

Telephone: 0409 509 677

Email: [cmiller@rga.org.au](mailto:cmiller@rga.org.au)