ACCC Review of the Water Charge Rules

Submission by MDBA, June 2015

## Introduction

The MDBA is a Commonwealth statutory authority established by the *Water Act 2007* (Cth).

The *Water Act 2007* established the MDBA as the body responsible for developing and overseeing the implementation of the Basin Plan: a planning framework for the integrated management of the Basin’s water and other natural resources in a way that optimises economic, social and environmental outcomes.

In addition to its functions under the Act, the MDBA also has significant functions under the *Murray-Darling Basin Agreement* (the Agreement), whose signatories are the Commonwealth, NSW, VIC, SA, QLD and ACT governments. These activities are known as the Joint Activities, the largest of which is River Murray Operations (RMO). RMO ensures the delivery of state water shares to New South Wales, Victoria and South Australia consistent with the Agreement. There are a number of other Joint Activities such as salinity management, monitoring and research which also contribute to management of the Basin water resources.

The policy and strategic direction of the MDBA’s activities are set by a six-member Murray‑Darling Basin Authority. The Murray–Darling Basin Ministerial Council is the decision making body for the Joint Activities. It is advised by the Basin Officials Committee which is made up of senior representatives from each partner government. River Murray Operations

River Murray Operations (RMO) involves the management and operation of assets that were built to deliver state water shares to NSW, Victoria and South Australia in the River Murray System, and to mitigate the environmental impacts of water use.

RMO does not supply water direct to water users, but supplies bulk water to the State Constructing Authorities (SCAs). The SCA’s on-deliver the water supplied through RMO to irrigators and other water users.

RMO functions include:

* Asset management - renewing and maintaining the suite of River Murray system assets;
* River operations - the operation of the assets to deliver water shares and environmental outcomes in the River Murray system; and
* Accounting for interstate water trade – including adjustments of state shares to reflect interstate entitlement and allocation trades and audits of these trades.

Other functions including hydrological modelling, river gauging and water quality monitoring.

### RMO Assets

RMO assets include the water storage and delivery assets through which state water shares are delivered, locks and weirs, barrages, salinity mitigation schemes, river bank restoration and other management works. RMO assets also include a number of new environmental works built to enable the delivery of water under the Living Murray program.

The MDBA is a service provider to the Joint governments for the delivery of state water shares and is funded through contributions from Joint governments. The RMO assets remain under the ownership of the states in which they are located but are managed and operated by the MDBA on behalf of the Commonwealth and the governments of NSW, Victoria and South Australia through an unincorporated joint venture.

Day to day management, operation, maintenance and renewal of the assets is undertaken by the State Constructing Authorities (SCAs) of NSW, Victoria and South Australia, under the direction of the MDBA. The SCAs are:

* New South Wales – Water NSW, and the NSW Office of Water;
* Victoria - Goulburn-Murray Water;
* South Australia - SA Water, as agent for the Minister for the River Murray.

The MDBA provides oversight to ensure a consistent standard of asset maintenance and risk management as well as providing head-office functions and coordinating and directing river operations.

As at June 2014, the RMO assets were valued at $2.6 billion, with a replacement cost of $4 billion. The RMO assets are divided into several categories:

#### Category 1 assets:

Key water assets essential to system-wide water delivery and management, including major water storages, the hydrometric network, and the Barrages.

#### Category 2 assets:

Locks and weirs originally built to facilitate navigation. They now also provide weir pools for the delivery of water allocations to local irrigation networks, river pumpers and for stock and domestic use, as well as supporting tourism and recreation activities. They provide significant local benefits to NSW, Victoria or South Australia, and are increasingly being used for the delivery of environmental water under the Basin Plan.

#### Other RMO assets include:

* Salt interception schemes (SIS) - built to address the impacts of rising river salinity as upstream diversions increased;
* River bank restoration and other management works to address the range of impacts on the environment of changed flow regimes, including cultural heritage impacts;
* a number of environmental works built under the Living Murray (TLM) program, which utilise weir pools to provide environmental water to nearby environmental assets. These new water management structures – channels, regulators, weirs and levees - enable large-scale watering of over 37,000ha of forests and wetlands. In addition, the Sea-to-Hume fishways enable fish migration along 2,000km of the River Murray channel.

## Current funding arrangements for Joint Activities

The Joint Activities are funded collectively by the partner governments under arrangements set out in the Agreement. To determine the budget for RMO, the SCAs advise the MDBA of the recommended construction, operation and maintenance activities for the coming year based on an Asset Management Plan agreed by the MDB Ministerial Council. The MDBA then prepares a draft budget which outlines the four-year RMO budget (coming financial year plus three out-years). The draft budget is incorporated into the MDBA Corporate Plan.

While not mandated, a review of RMO efficiency occurs every 5 years or so. The most recent review was in 2014 and found that the lower bound revenue requirement for RMO, based on an assessment of efficient costs, is $72.245 million. The upper bound revenue requirement was shown to be $229.486 million.[[1]](#footnote-1)

The Ministerial Council set the 2014-15 RMO budget at $54.71m, and $60.613m for 2015-16.

## Cost shares

The agreed budget for the Joint Activities is shared between the Contracting governments according to agreed cost shares. Under the 1915 River Murray Waters Agreement, the Australian Government and the states of New South Wales, Victoria and South Australia agreed to share the costs of investigation and construction of works equally, while the subsequent costs of operation and maintenance of the assets would be shared equally between the three states. Cost shares have varied slightly over the years to reflect the addition of new assets and programs, and changes in volumes of water diverted, but the fundamental principles have remained constant.

The costs of the other Joint Activities are shared equally between the Australian Government and the states of New South Wales, Victoria and South Australia once contributions by Queensland the ACT have been made.

Under the Agreement, cost shares are to be reviewed every 5 years. The 2014 Cost Share Review[[2]](#footnote-2) found that the current cost share arrangements for RMO are broadly appropriate and consistent with NWI pricing principles.

Table 1: Cost shares for joint activities

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| --- | --- | --- | --- | --- | --- |
| **Activity** | **Cost type** | **C’wlth** | **NSW** | **Vic** | **SA** |
| ***River Murray Operations (RMO) programs*** | | | | | |
| **RMO Assets** | **O&M** | 0% | Costs shared in proportions based on the cap equivalent of Murray Valley entitlements in each State, the five year average water use in the Murray Valley by each State, and the share of local beneficiary for locks and weirs.  Equal shares for salt interception schemes. | | |
| **I&C** | 25% | Balance of I&C cost shared on same basis as O&M.  RMO administration treated as I&C. | | |
| **Murray mouth dredging** | **I&C** | Costs are shared equally between all four governments | | | |
| **Environmental works and measures** | **O&M** | 0% | Equal shares | | |
| **I&C** | 25% | Balance of I&C cost shared on same basis as O&M. | | |
| ***Other activities*** | | | | | |
| **Non-RMO programs** | | Contributions from Qld and ACT are negotiated based on their interest in each programs. The balance of the costs are shared equally between the Commonwealth, NSW, Victoria and South Australia. | | | |
| **Corporate overheads** | | Joint activities pay a share of MDBA corporate overheads, which is then split between programs on the basis of the FTEs employed in each program. These costs are then shared between jurisdictions in accordance with the relevant principles for each program. | | | |

## Responses to ACCC Issues paper

*The ACCC Issues Paper asks (question #3) ‘How could the water charge rules more effectively contribute to achieving the Basin water charging objectives and principles?’*

### RMO efficiency reviews

The water charging principles of relevance to the MDBA are those that apply to water storage and delivery (the Water Charge Infrastructure Rules) and to Water Planning and Management (the Water Charge Planning and Management Information Rules).

One of the key concerns of stakeholders is the efficiency of RMO and whether water users are paying ‘over the odds’ for their bulk water. This is usually expressed as a concern in relation to MDBA costs, although the SCAs are the more significant component of RMO costs.

RMO is a bulk water service provider whose ‘customers’ are the State Constructing Authorities (SCAs). However, because the MDBA does not deliver water directly to users or impose charges, it is not a regulated entity as defined by the WCIR. Therefore, there is no scope under the current implementation of the WCIR for the ACCC to assess RMO costs against the tests for efficiency and prudency that are applied to other operators under the WCIR.

Assessments of RMO costs and efficiency have occurred historically every 5 years or so, although these are not mandated under the Agreement and no consistent approach has been taken to them. The most recent assessment – ‘The Efficiency Review of River Murray Operations (RMO)’ [[3]](#footnote-3) was completed in December 2014. It found that RMO is efficient, falling within the top ten percent of comparable bulk water operations.

While the current ad hoc approach to efficiency reviews has been of value, the MDBA considers an improved approach would involve the reviews being mandated, independent, transparent and using a standard methodology. This could be achieved if current adhoc reviews were replaced by an ACCC assessment of RMO costs using the same tests for efficiency and prudency as are currently applied to other bulk water operators. This information could be applied by the relevant pricing regulator/s in making state-based pricing determinations.

The above approach would be likely to require an amendment to the definition of water charges under the WCIR.

### Approaches to cost recovery

Through their SCAs and other irrigation infrastructure operators, state governments recover some of their RMO contributions through indirect water charges. Different levels of cost recovery are applied by each state government:

* In NSW, Water NSW cost recovers some of its contribution to RMO from irrigators and passes these revenues ‘through’ NSW Treasury to the MDBA as an identifiable cost recovery charge;
* In Victoria, Goulburn-Murray Water cost recovers from irrigators drawing from the River Murray System, but funds are paid to the Victorian government which then pays MDBA out of consolidated revenue – there is no direct link between costs to irrigators and their use of RMO services;
* In South Australia, the bulk water operations of SA Water in relation to the River Murray are not currently regulated by ESCOSA. As such, SA Water is not subject to the WCIR and MDBA costs are not included in SA Water charges for cost recovery purposes.[[4]](#footnote-4)

These different arrangements appear to be at odds with the intent of the National Water Initiative in achieving a level playing field for water users. In this context, it may be useful for the ACCC to provide explicit guidance to the joint governments on a more consistent and transparent approach to meeting their RMO costs.

### Upper vs lower bound pricing

Many of the assets in the southern MDB were built for economic development purposes, and were never intended to be cost recovered. In addition to irrigation and urban water, these assets now support extensive boating, tourism, recreational and fishing activities, and a number of communities have developed along river banks and around lake shores whose property values are directly related to the management of rivers, lakes and other RMO assets.

In this context, MDBA considers that while moving to lower bound pricing would be a sound strategy to ensure the assets operate safely into the future, the achievement of upper bound pricing for RMO infrastructure is unrealistic.

### Water trading activities

*The ACCC Issues Paper asks (questions # 41 – 44) whether differences in charging arrangements may distort a water user’s decision to trade, what measures could be taken to reduce distortions and  whether there should be a requirement for infrastructure operators’ charging arrangements to be consistent with the Basin water charging objectives and principles?*

The MDBA is committed to improving the operation of the water market across the Basin. The MDBA facilitates interstate trade under Schedule D of the Agreement (Transferring Entitlements and Allocations) and from 1 July 2014, the MDBA has been responsible for regulating water trading rules under the Basin Plan. These rules are designed to improve the efficiency and effectiveness of the market, without duplicating state rules.

The rules include provisions designed to ensure that all water users have the right to trade free of certain restrictions. These provisions prevent authorities who approve trades from imposing discriminatory conditions on trade. For example they prevent discrimination based on the use of the water after a trade, or because an individual belongs to a particular class for persons.

The MDBA considers that charging arrangements have the potential to distort the market and discriminate between water users. Differences in charging arrangements can influence a water user’s decision to trade, and the type of trade they undertake. We are considering whether the scope of the Basin Plan water trading rules may extend to charges which are discriminatory in this way.

The MDBA considers that increased charges should not be imposed on water that is traded into a state or district compared with water associated with ‘local’ entitlements, except for appropriate recognition of the marginal costs associated with administering the trade. On this point, the MDBA acknowledges that the numbers of trade in each state varies widely (approx. 500 for QLD and 14,000 for NSW/VIC in 2012-13) and therefore the marginal costs of administering a trade may be different for each trade approval authority.

1. Synergies Economics (2014) *Building Blocks Model of River Murray Operations (November 2014) tables 8 and 9.* [↑](#footnote-ref-1)
2. Buckley, Michael and Garry Smith (2014), *Review of the Cost Shares for Joint Activities – Final Report*, Report for Basin Officials Committee, April (available on the MDBA website). [↑](#footnote-ref-2)
3. Synergies Economics (2014) *Building Blocks Model of River Murray Operations (November 2014);* Cardno (2014) *Efficiency Review of River Murray Operations (8 October 2014); and* Economic Insights (2014) *River Murray Operations Economic Benchmarking Study (28 November 2014). All three reports are available on the MDBA website.* [↑](#footnote-ref-3)
4. Some of South Australia’s contributions to the MDBA were recovered through the River Murray levy. This levy is to be abolished on 1st July 2015. [↑](#footnote-ref-4)