

## **CENTRAL IRRIGATION TRUST**

Trustee: Central Irrigation Pty. Ltd. ACN 075 446 810  
4 Fowles Street PO Box 34  
Barmera SA 5345  
Telephone 08 8580 7100  
Fax 08 8588 2001



### **CIT SUBMISSION**

ACCC inquiry into water markets in the Murray Darling Basin  
Interim Report  
Australian Competition and Consumer Commission  
GPO Box 3131  
Canberra  
ACT 2601  
28/08/2020

To whom it may concern,

Thank you for the opportunity to provide a submission to the inquiry.

CIT is an Irrigation Infrastructure Operator ("IIO") in the Riverland of South Australia supplying irrigation water to approximately 1200 irrigators, 3000 non drinking water customers and 16 industrial customers. Our customers use between 100 and 120 GL in average years on permanent horticulture and trade approximately 60 GL of water allocation per year directly or through various intermediaries.

As an IIO we are subject to the current Water Act regulations such as the Water Charge Rules and the Water Charge (Termination Fee) Rules. We are also required by legislation to supply the relevant trade information to the BOM (Bureau of Meteorology).

Being a large energy user we are also a participant in the energy market and understand the regulatory framework of the National Electricity Market (NEM)

CIT financial reserves are invested in a diversified portfolio of shares, bonds and property.

As a result of above listed experience we believe that our submission is based on experience rather than being hypothetical or theoretical.

### **General Comments on the Interim Report**

It is very difficult to read a 542 page report and prepare a submission within the time frame provided. In fact the average irrigator described on page 158 of the report (age 60, 35+ years farming experience) in our view would not be inclined to read such a lengthy report or provide a submission.

We note that the interim report confirms the principle that water will move to the highest value and that the high prices experienced in 2019 were a result principally of supply and demand. Aither Water Markets presentation in August 2020 reaffirmed ACCC's comments noting that the 2019/2020 water prices were not surprising and in fact, a market functioning.

Policy makers and regulators need to articulate this to the market participants, a number of whom believe that the high water allocation prices of 2019/2020 were a result of market failure and corruption and that the adoption of ACCC recommendations will ensure there is not a repetition of 2019 market prices and conditions again.

### **No Evidence of Market Failure or Inappropriate Behaviour**

The report lacks evidence or facts and revolves around conjecture, "this could occur". Page 200 of the interim report states that "In recent years the ACCC has only received a small number of complaints concerning Brokers and other Water Market Intermediaries"; page 213 "At this stage the ACCC does not have specific evidence of Brokers deliberately providing misleading price or other market information to their clients" which would tend to indicate that the water market functions well in its current format and does not require significant or costly change for improvement. Perhaps we should

take stock and applaud the hard work many of the water market participants that make the market function for the benefit of many. A Federal Senator recently described to me that the ACCC report implies the Water Market is the “wild west”. This description I find far from the truth and one that erodes market confidence more than any activities of market participants.

We are also aware of recent court action brought against a South Australian water broker which shows that where transactions fail civil recourse is available. In such a small market the rapid spread of such news will quickly influence the decisions of which market intermediaries are used into the future.

### **State Based Market Architecture**

In the establishment of the Commonwealth Water Act and the subsequent Murray Darling Basin Plan the MDB States did not cede all of their powers to the Commonwealth and are unlikely to do so in the future. The system is now entrenched as a cooperative model with MDBA overseeing the states implementation.

The National Water Market Systems and The Bureau of Metrology Water Market Information have seen significant expenditure (\$100 million) but not provided the outcome sought by many, a single source of information.

Likewise the NEM (National Electricity Market) is in name a National Market but in reality is still a collective of State based markets and operators. The regulated businesses and the contested market are all state based. The prices reported on the NEM ASX site are a guide only and not a reflection of the price any business will pay as they have their energy prices demand load shaped and risk assessed as well as locational charges such as MLF (Marginal Loss Factors) applied.

We believe that the solution to improving the water market relies in the States working together and developing the cooperation needed to improve the synchronisation, harmonisation and interoperability. This is already happening with new registers being developed and allocation announcements coordinated.

### **Cost of Regulation**

Whilst a number of the short term incremental improvements suggested should be inexpensive to implement there was no data presented on the costs or benefits of the more structural changes suggested.

The Australian Government Guide to Regulatory Impact Analysis states that “regulation is never adopted as the default solution, but rather introduced as a means of last resort.” Any regulation should be founded on a rigorous cost benefit analysis.

In the report there is no evidence presented for regulation. Self-regulation is dismissed easily and no cost of regulation provided or the calculation of the benefits that accrue. There is also no direction as to who the beneficiaries are and who should bear the costs. Such information is critical to make decisions or informed opinions.

The NEM has been used as an example of regulation that could be used in the water market. The NEM has market bodies established by legislation being AEMO, AEMC and AER. The Regulator AER’s (Australian Energy Regulator) cost of operation was \$62 million last year, up substantially from 2018/2019, employs 253 staff and has 30 external contractors. The AER also imposes significant unaccounted costs on other organisations and companies such as the Transmission and Distribution Companies, generators, retailers and customers.

Development of the National Water Market System was never completed and cost \$25 million, closer to \$50 million at current value. Add to this the cost to organisations (80 Brokers, 60 IIOs, 20 Government Departments) to feed data into such a central system could easily add another \$50 million to the cost.

Hence a regulatory system could cost in excess of \$100 million to establish and a similar amount to operate. We very much doubt the benefits would outweigh the costs in light of the extremely low number of complaints received by the ACCC to date and the view that recent market conditions have been principally a result of supply and demand. There is also no indication of what a rigorous regulation system would do to number of brokers and hence competition in the market place or

whether higher charges would inhibit smaller parcels of water being placed on the market as the cost outweighs the returns. Many of our members trade parcels of less than 5 ML.

The government has also attempted to provide the information outcomes sought by the ACC through the BOM and MDBA with significant expenditure by governments of all jurisdictions and industry data owners. Market participants pay very little if anything for this information collected, however they are the biggest beneficiaries.

Market improvements are occurring all the time and in fact 2020/2021 water allocation announcements by each state are one example. The announcements are synchronised across the Southern Connected System; allocations for each valley are easy to ascertain; future projections under different scenarios are well explained and the components of the share of available water are also well set out and easy to identify.

The recent Aither Water markets report summarises data from the previous year and it is easy to formulate water strategies in the coming year based on such data.

We believe that the regulation proposed by the ACCC would not provide any significant benefits that outweigh the costs of such regulation and strongly oppose any major regulation. Best practice guidelines, self-regulation, enhancing the current BOM reporting system, improving MDBA oversighting and implementing incremental improvements we believe will provide the best outcomes for the markets.

### **Southern Connected system only**

Whilst the Murray Darling Basin is a discrete geographical unit it is not the case from a state boundary or national point of view. To implement changes only to the Murray Darling Basin is difficult and discriminatory and to quarantine changes only to the Southern Connected System would be even difficult and discriminatory.

The Murray Darling Basin catchment is only one of the catchments that are within the jurisdiction of each of the Basin States. In fact in some states such as Queensland the Murray Darling Basin is only a minor part of the state's water catchments. Consequently states have to provide services both within and outside the Murray Darling Basin catchments and are likely to operate multiple systems if changes are not made nationally.

References to the National Water Initiative permeate the report but changes are not considered on a national scale which we find incongruous and discriminatory. For example water markets outside the Murray Darling Basin may be unregulated and hence cheaper to operate in thus giving those regions a competitive advantage over those operating within the basin.

Experience with the ACCC Water Charge Rules demonstrated that a notion of Basin wide uniformity on price and regulation did not succeed and reverted back again to state based systems.

### **Lack of focus on the demand side**

A focus entirely on the supply side of the market in the interim report neglects the reciprocating side of the market, the demand side. In a cap and trade market the demand side is more important than the supply side as the current and future demand is a major factor in water prices. This is evidenced by the separation of Zone 7 as a discrete market reacting differently to the other Zones within the southern connected system. However, nowhere in the interim report is there reference that demand side of the equation should be mapped or available to the market. Large corporations have a distinct advantage in the market place as they understand their demand purchase patterns, volumes of carryover, forward contracts as well as expansion plans none of which is visible to the market place until after the transactions.

If Water Market intermediaries, state governments and IIOs are expected to reveal all their internal water transactions, the same scrutiny and regulation should apply to the demand sides of the market so that all participants get a true picture of not only water supply but also water demand.

Understanding water demand requirements of current and new entrants can also provide policy makers with the information required to formulate appropriate policy for the Murray Darling Basin. In

the absence of such data, market failure in a policy vacuum occurs to a point where we see industries such as the Almond Industry calling for a moratorium development.

## **Investors**

The interim report outlines investors currently accounted for 20% by volume of water allocation trade, up from 0% a decade ago. The majority of this was accounted for by the 4 large investors noted in the report. If such a trend continues, and there are no signs of it abating as the investors continue to purchase water entitlement and allocation, investors will be the dominant water owners in the Murray Darling Basin. The Aither Water Market Reports indicates that in MDBA Zone 7 water demand from permanent plantings will outstrip supply in dry years consequently investors with significant market share certainly have potential for market manipulation. Yet no regulation or scrutiny of investors is proposed.

## **System Complexity**

The Murray Darling Basin Water system is very complex. The major supply of water is nature through rainfall and runoff. Water is then stored and delivered with storage and hydraulic constraints through multiple river systems.

Whilst this can be modelled, experience shows that the modelling is not precise and often produces erroneous results. This was demonstrated during the development of the Basin Plan.

River Operators require a certain amount of flexibility in the delivering water to all consumers throughout the system as they have to deal with many variables, many of which are not predictable. Overlaying further market based systems such as delivery capacity; storage rights further complicates an already complex system which could also result in perverse outcomes. The energy market in the transition to renewable energy is currently going through a similar process (FCAS, RERT, Demand Response) and as an informed participant in that market we are unable to keep up with the changes and understand from discussion with other users that developments of the new markets will not produce the outcomes envisaged.

We believe that the River Operators and states are best placed to manage the River System but that the rules should be clearer and based on facts.

## **Improvements and ACCC questions**

### **1 Conduct of Market Participants**

The Australian Government's Guide to Regulatory Impact Analysis states that "regulation is never adopted as the default solution, but rather introduced as a means of last resort." Any regulation should be founded on a rigorous cost benefit analysis.

In the interim report there is no evidence presented for regulation and in fact the ACCC only received 2 complaints regarding water trading in the previous year. This has also been the case in a number of previous reports. Self-regulation is dismissed easily. No estimates of the cost of regulation for each option was provided nor the calculation of the benefits that may accrue from such regulation. There is also no direction as to who the beneficiaries are and who should bear the costs. Such information is required to make informed decisions or opinions.

Much of the recent angst in regards to the water and most likely the reason behind the change in sentiment of market participants towards market intermediaries identified in the report was driven by the rapidly increasing cost of water in 2019 and this report supported by the Aither Water Market Report clearly articulates the water price was driven by supply and demand. Any regulatory changes will not change the supply/demand equation and the subsequent price impacts in coming dry years. The outcome of cheaper water that many are seeking will not eventuate from the options provided, in fact the price of water could rise significantly as a result of the increased transaction costs and possible reduced competition in the water services area. A perverse outcome could see less water available on the market as those with very small parcels find it too difficult or expensive to transact through intermediaries or on regulated platforms.

Our experience with over 1200 irrigation members is that the cost of transacting water is an important factor in their decision making especially in the times of average and low water prices. We assist many

of our members by bulking up small parcels of water into marketable parcels thereby reducing fees to all involved in a trade.

On the lack of evidence presented in this report our belief is that Self-Regulation should be the preferred course forward. The trade services industry can use this for product differentiation where self-regulated and accredited intermediaries can advertise the benefits to attract customers and customers have the choice of selecting and accredited broker or not. The cost and benefits of the regulation are borne the users choosing that service.

Due to the lack of evidence provided in the report and our experience in the power market we strongly oppose the Financial Regulation Framework or Independent market focussed government regulator. As stated above the cost of regulation in the energy market would be well in excess of \$100 million if you only account for the cost of the regulating bodies and such costs would be overwhelming for the water market. In fact the energy companies had to develop and subscribe to an Energy Charter in an attempt to restore "trust" in the energy system, not a good endorsement.

In such a small market as the Southern Connected system and the limited number of trade services participants we believe that the water market intermediaries should be able to service buyers and sellers with the appropriate disclosures. To do otherwise would lead to a very inefficient and non-functional market.

If regulation is imposed it should be no more than light regulation with disclosure, use of trust accounts and registration sufficient.

From broad experience in both the water and energy markets we do not see the water markets introducing more sophisticated products such as options, swaps, caps etc. in the near future. In fact forwards and carryover largely negate the need for such products.

## **2 Market trade processes and market transparency**

The suggestions made regarding validation and checking of data being sent to the BOM, catching further data on the trade forms and increased harmonisation across Basin State registers should improve the information in the water market. Much of this is already happening.

Zero dollar trades are a reality in the water market and there are many and varied reasons for such trades. Reasons could include but are not limited to:

- Trades between accounts or licences under common ownership or multiple ownerships with common entities
- Trade within families for no consideration
- Trade between community members for no consideration
- Trade across state boundaries by the same owner
- Trade for carryover or parking by the same owner
- Water donated
- Water use as a component of a barter
- Water used for environmental purposes
- Allocations traded as part of a permanent trade as permanent trades can be wet or dry (with or without allocation).

In South Australia the CHEW owns almost 50% of the irrigation consumptive pool all of which will be used or traded to sites for use for zero consideration.

Hence trades for no consideration will continue to be significant in the market place so need to be recognised and catered for whilst only trades which are underpinned by financial transactions should have the price recorded. Forcing anyone to put a value on a trade that is not underpinned by financial transactions could also distort market information.

In our experience it is interesting that market participants who are calling for greater transparency are generally the ones who fail to complete the necessary applications with all of the relevant or correct information. Generally those that provide trade services are left to correct or secure the information required from the market participant.

### 3 Efficient trade services and high quality information

The Murray Darling Basin is already awash with legislation and regulation ranging from the Water Act, Murray Darling Basin Plan, and Water Charge Rules through to various state legislation. The report states that there are already bodies and legislation covering many of the topics or suggested improvements and we should see this system improved rather than another set of legislative instruments introduced, more bureaucracies created passing costs onto market participants or associated organisations for what we believe would be marginal benefit at best.

The Australian Water Market is currently a leader in the world in both its sophistication and operation. It has developed to this state by innovation by both state governments and market participants in just over a decade and is continually improving. Attempts for national oversight such as the National Water Market System and the BOM in which there have been hundreds of millions of dollars investment have not succeeded in providing the clarity the ACCC is suggesting in this report.

The Australian Government Guide to Regulatory Impact Analysis states that “regulation is never adopted as the default solution, but rather introduced as a means of last resort.” Any regulation should be founded on a rigorous cost benefit analysis. There have been no cost benefits prepared in this report and our experience is that regulation comes with significant cost and marginal if any benefit. The regulatory impact statements also generally use bold assumptions to prove a case.

CIT are opposed to legislative changes suggested in the report as we believe they provide a bureaucratic and costly framework that will provide little advantage or improved accuracy to the water market and information for participants. Our view is that the states should work together cooperatively with a goal of improving trade services and quality of information. This is already occurring and we believe will provide superior outcomes to legislative changes. The state jurisdictions along with the current regulator (MDBA) should develop best practice guidelines that the states can work towards as they upgrade and improve systems (continuous improvement).

As an example the Water Charge Rules imposed by the ACCC with an objective of uniform pricing across the Murray Darling Basin have been an abject failure with expensive bureaucratic changes imposed on companies and little change to the pricing outcomes, which were not warranted, across the Basin. The Water Charge Rules were implemented after a listening journey, on an ideology that could not be achieved due to the complex nature and diversity of the Basin’s operations and practicalities of operating across jurisdictions where catchments are within and outside the Basin.

We strongly oppose the changes suggested for IIO’s. Our water register has been developed to suit the operational need of our business and customers/members. The suggested changes would see significant cost associated with rewriting our registers to in our view marginally improve water market information. This cost would be paid for the members of our business with the benefit being water market participants most of whom are not our members.

The data provided in the report is misleading as to the quantity of internal trades that occur within our business. CIT manages 13 Trusts in South Australia which collectively account for approximately 23% of South Australia’s River Murray Entitlements. In 2019/2020, 50% of the water allocation traded by our customers was recorded on a state register as these trades were across licences. Provision of further data on internal trades, say through a state/national register as individual trades, many of which would be zero dollar trades as they trades between accounts, would not improve the accuracy of trade data but would cost our members \$500 000 in existing state authority trade fees.

We also do not support changing the Water Regulations 2008 to more clearly specify data reporting requirements for trades of Irrigation Rights. Again there is no clinical analysis to support such change and in the case of CIT the vast majority of Irrigation Right trades are considered transformations by the ACCC, recorded on the state register, submitted to the ACCC for the ACCC monitoring report, and submitted to the BOM. We fail to see the benefits or yet more regulation in this space. If enhancements are required we should work with the current bodies to improve the current systems.

The revision of trading rule 12.48 is also not supported by CIT and goes well beyond the remit of this review. There is no evidence to support such a change and the ACCC has oversimplified the complexity of hydraulic and natural systems. The ACCC continues to suggest regulation of IIOs on little to no evidence and these businesses have been operating and innovating in very tough circumstances. In fact they are recognised as the best in the world and held up as role models in other countries.

The use of a unique identifier for a trade is amicable but we believe difficult to implement. The use of an ABN will not be popular for many reasons in particular privacy. Also not all people who own water have an ABN so again there will be missing data.

The ACCC should work with the states and the regulator (MDBA) to establish best practice principles for processing and approval of water trade but this should not be mandated.

## **Digital Technologies**

Digital technologies are ever evolving, offer opportunities for efficiency and information and should be pursued by market participants but not mandated. The water market has seen two national projects pursued and/or mandated with limited or no success. The National Water Market System was an attempt by government for an overarching national system and after spending \$25 million abandoned. The BOM was also given many hundreds of millions of dollars to produce comprehensive water reporting system which has met with limited success.

However in the commercial sphere we have seen the development of many platforms that are innovative and well supported. The view of CIT is that governments should not mandate digital platforms or technologies but rather let them develop organically and provide competitive seed funding to assist with development. Successful platforms will see them self-supported into the future, tailored to customers' needs and operated efficiently.

CIT believes that this is currently occurring and that government investment or selection of platforms will be detrimental to efficient markets.

One of the suggestions in the report is implementation of a system similar to that used in the electricity industry. As a large unbundled electricity user (\$5 million annually) in the energy industry we are very familiar with the regulation and costs or benefits accruing from such regulation and believe that the cost and complexity of such a system would far outweigh any benefits if applied to water markets.

The energy market whilst touted as a national market is still a collection of state markets with limited interoperability. The ASX energy market provides very little correlation to the price we pay for energy as our costs are influence by market price, load shape, locality and risk premium. In securing our energy price and contract we firstly seek the assistance of an energy broker to tender our load to the market. The broking industry is unregulated and we use relationships to determine the broker best suited to our needs. The broker helps us navigate the complexities of the energy market including the cost of energy and all the associated costs necessary to purchase and have power delivered. We find this unregulated broking market very efficient. The broker will then tender our power to the various retail companies operating in South Australia who are interested in supplying this power. We will then develop a contract with mutually acceptable terms with the successful retailer. The retailer may or may not be involved in the generation or supply of power to our sites.

The retailer will then amalgamate loads to source power from generators (some of which could be supplied by their own assets) and possibly hedge their positions through caps, swaps or other options. These transactions are not visible to the customer and in South Australia many of these trades are OTC trades and may not be recorded through the exchange. We find the ASX energy exchange data for South Australia useful as a guide only for trends rather than a definitive indication of the price we will pay for power. In fact very few energy customers would contract directly through the exchange.

On the regulated side of the energy market we find it very difficult to navigate or engage with. It is incredibly complex with 3 separated entities (AEMC, AEMO and AER), expensive and has significant regulation over many companies. As a customer you have very little input into the market design and development. Nothing demonstrates this better the very limited number of successful rule changes proposed to the AEMC by energy consumers. It is also very costly with the energy regulators listed above costing in excess of \$100 million annually and the benefits of such changes to the water markets significantly less if any accrue at all.

As we currently provide the data required to the BOM our suggestion is that this system is abandoned or improved to automatically collect the data required and that the BOM's system is audited through the MDBA.

## 5. Improving Architecture

Architecture of the Murray Darling Basin system has developed over more than 100 years, spanned all climatic conditions and many challenges consequently should not be changed lightly. The Murray Darling Basin Water system is very complex. The major supply of water is nature through rainfall and runoff, water is then stored and delivered with storage and hydraulic constraints through multiple river systems. The states have developed different water sharing systems which now influence asset valuations and business models.

Whilst the river system can be modelled, experience shows that the modelling is not precise and often produces erroneous results. This was demonstrated during the development of the Basin Plan.

River Operators require a certain amount of flexibility in the delivering water to all consumers throughout the system as they have to deal with many variables, many of which are not predictable. Overlaying further market based systems such as delivery capacity and storage rights further complicates an already complex system which could also result in perverse outcomes. The energy market in the transition to renewable energy is currently going through a similar process (FCAS, RERT, Demand Curtailment) and as a participant in that market we are unable to keep up with the changes and understand that from discussions with other users that suggested new markets will not produce the outcomes envisaged.

We believe that the River Operators and states are best placed to manage the River System and do not support capacity markets or changes to the current accounting for losses. Any such changes would need significant investigation to determine if issues identified are factual, possible solutions, cost benefits, socio economic impacts and a no disadvantage test. The small amount of data presented in the report does not support any of the changes suggested. In fact broader data sets do not support the changes.

More clarity could be provided around the operating rules and some issues such as the Inter Valley Trade. The IVT transfer process needs to be more equitable to all market participants through mechanisms such as a ballot and the IVT limits and claimed environmental damage need to be clarified as to whether they are real physical limits or merely barriers to trade.

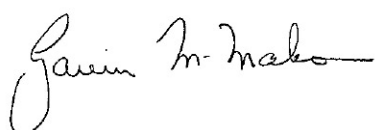
## 6 Changes to Market Governance

The Murray Darling Basin system is the most governed river system in Australia if not the world. Stakeholders operating with the Basin are already subject to a plethora of regulation and expect less not more. CIT is not in favour of improving governance by increasing bureaucracy and subsequently cost. The governance structure already exists through the MDBA, Basin States and BOM and if strengthening of governance is required it should occur within the current bodies rather than creating another body and further confusion within the Basin. In fact, the report suggests changes would be confined to the Southern Connected system which we find discriminatory and further complicating for those in this geographical region. Any changes should be national.

As a participant in both the water market at one end of the regulatory scale and the energy market at the other pole of the regulatory scale I contend the following: "When purchasing the end product in either market does the energy market provide me with greater transparency and better outcomes than the water market?" In our experience the answer is no hence our preference for self-regulation and collaborative arrangements between the states working towards best practice guidelines.

If you would like any further information please feel free to contact me.

Yours Sincerely,



Gavin McMahon  
Chief Executive Officer