National Irrigators' Council
Level 2, NFF House, 14-16 Brisbane Ave
Barton ACT 2600
Ph: 02 6273 3637
ABN:
92133308326

Review of Water Charge Rules – Draft Advice, November 2015

Submission to the ACCC

March 2016

Introduction

The National Irrigators' Council (NIC) is the national peak body representing irrigators in Australia. The Council supports twenty-seven (27) member organisations covering the Murray Darling Basin states, irrigation regions and the major agricultural commodity groups. Council members collectively hold approximately 7,000,000 mega litres of water entitlements.

The national body is the policy and political voice of those who use water for commercial agricultural purposes, producing food and fibre for local consumption as well as making a significant contribution to Australia's export income.

NIC is funded by irrigators, for the benefit of irrigated agriculture which provides jobs in rural and regional communities. Members are not individual irrigators but members of their respective representative organisations. An irrigator is defined as *'a person or body with irrigation entitlement for commercial agricultural production'.*

Member organisations are located in irrigation regions across Australia within the Murray-Darling Basin and beyond. They represent a diversity of organisations from irrigation infrastructure operators, individual irrigators, processors through to agricultural commodity groups who produce and value add food and fibre for domestic consumption and significant export income.

NIC advocates on behalf of irrigated agriculture and aims to develop projects and policies to ensure the efficiency, viability and sustainability of Australian irrigated agriculture and the security and reliability of water entitlements. The NIC advocates to governments, statutory authorities and other relevant organisations for their adoption.

Irrigated agriculture contributes to the social and economic wellbeing of rural and regional communities and to the national economy, producing goods such as milk, fruit, vegetables, rice, grains, sugar, nuts, meat and other commodities like cotton.

In 2013-14 the total Gross Value of Irrigated Agricultural Production (GVIAP) for Australia was $14.6 billion, an increase of 9% from 2012-13. In 2011-12 the total gross value of GVIAP in the Murray Darling Basin (MDB) region rose by 13% to $6.7 billion *(accounting for 49% of the total GVIAP for Australia)*, *{Australian Bureau of Statistics}* with the volume of water applied in the same period, 5.9 million megalitres.

NIC Guiding Principles

The objective of the National Irrigators' Council is to protect or enhance water as a property right and to champion a vibrant sustainable irrigation industry.

The Council's policy positions are guided by the following principles:

- A healthy environment is paramount
    - Sustainable communities and industries depend on it
- Protect or enhance water property rights
    - Characteristics of water entitlements should not be altered by ownership
- No negative third party impacts on reliability or availability
    - Potential negative impacts must be compensated or mitigated through negotiation with affected parties
- Irrigators must be fully and effectively engaged in the development of relevant policy
- Irrigators expect an efficient, open, fair and transparent water market
- Irrigators require a consistent national approach to water management subject to relevant geographical and hydrological characteristics
- Irrigators expect Government policy to deliver triple bottom line outcomes
- Regulatory and cost burdens of reform must be minimised and apportioned equitably.

Contacts

Gavin McMahon
Central Irrigation Trust
Chief Executive Officer
08 85807100
email gavin.mcmahon@cit.org.au

Anthony Couroupis
Western Murray Irrigation Limited
Interim General Manager
(03) 5027 4953
Anthony.Couroupis@westernmurray.com.au

Barry Schier
General Manager
Renmark Irrigation Trust
(08) 8586 6911
bschier@rit.org.au

Perin Davey
Murray Irrigation Limited
Water Policy & Communications
(03) 5898 3347
perin.davey@murrayirrigation.com.au

John Culleton
Chief Executive Officer
Coleambally Irrigation Co-operative Limited (CICL)
(02) 69544003
JCulleton@colyirr.com.au

Paul Shanks
General Manager
Barossa Infrastructure Ltd
(08) 8563 2300
paulshanks@barossainfrastructure.com.au

Karen Hutchinson
MI Murrumbidgee Irrigation
Customer Services Manager
(02) 6962 0200 :
karen.hutchinson@mirrigation.com.au

Tom Chesson
Chief Executive Officer
National Irrigators' Council
(02) 6273 3637
tom.chesson@irrigators.org.au

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1. Overview

1.1 We are pleased to make this submission on behalf of our members in response to the ACCC's Water Charge Rules Review: Draft Advice dated November 2015.

1.2 We disagree with the Draft Advice and we strongly oppose the ACCC's proposed new Water Charge Rules. The existing Water Charge Rules are far preferable.

1.3 Our members are very concerned that the changes to the Water Charge Rules proposed by the ACCC's Draft Advice represent a very substantial increase in the regulatory burden on member-owned irrigation infrastructure operators and there are many examples of new regulations that have been poorly considered and drafted which will lead to unintended or absurd results. The changes proposed are not well considered and will exacerbate the impact of a decade of regulatory change in the Murray-Darling Basin which has had a major impact on all water users.

1.4 With respect to member-owned operators, the ACCC has not complied with the specific requirements of subsection 93(3) of the *Water Act 2007* (Cth) which requires that the ACCC, when advising the Minister on the Water Charge Rules, or proposed amendments to them, must have regard to:

(a) the governance arrangements of infrastructure operators;

(b) the current charging arrangements of those operators; and

(c) the history of the charging arrangements of those operators.

1.5 The Draft Advice does not reflect the Terms of Reference. This whole exercise arises out of Recommendation 11 of the Report of the Independent Review of the *Water Act 2007*. Recommendation 11, which was accepted by the government, was that the ACCC undertake a review of the Water Charge Rules and "*focus on reducing the cost to industry and governments*". Accordingly, the Terms of Reference specifically required that:

(a) "*The advice should address the merits of amending the rules in response to matters raised in the Report of the Independent Review of the Water 2007, as tabled on 19 December 2014; specifically, recommendation 11 in the report, proposing that the rules be reviewed* ***to assess opportunities to reduce cost to industry and governments***."

(b) "*The ACCC's advice is also requested on other opportunities for amending the rules to improve regulatory clarity or efficiency, or* ***to reduce regulatory burdens*** *while maintaining effective standards.*"

Seven particular matters for the ACCC to consider were listed under the overarching instruction to assess opportunities to reduce cost to industry and governments.

Contrary to the Terms of Reference, what the ACCC has done in its Draft Advice is to propose a burdensome increase in regulation, including a host of complex new rules, which would significantly increase cost to industry and governments.

1.6 In discussions with the ACCC's representatives, our members have been advised that the additional non-discrimination regulations advocated by the ACCC are desirable to enforce a principle of equitable treatment of customers. There are, however, examples – such as the prices charged by electricity retailers, urban water utilities or local governments (for rates) – which are not subject to non-discrimination requirements as extensive as those advocated in the ACCC's Draft Advice. There is no persuasive evidence that the irrigation sector ought to be treated in such a radically different way from other infrastructure service providers.

1.7 It should be noted that reviewing and preparing submissions in response to the ACCC's Draft Advice and the draft new Water Charge Rules is itself a significant exercise, and one which not all operators are equipped to undertake. Not all operators have been effectively engaged by the ACCC in this process and many of the smaller operators are either unaware of the existence of the ACCC's Draft Advice or do not understand it.

1.8 The only significant part of the Draft Advice which responds appropriately to the Terms of Reference to reduce regulatory burdens and costs to industry and governments is the proposal to repeal the requirement for Part 5 operators to produce Network Service Plans. These five-year plans are expensive to produce but do not contain information valued by customers, as reflected by the direct feedback provided by customers in response to these plans. The repeal of this requirement would bring a welcome reduction in regulation and cost. If the repeal of Part 5 (Network Service Plans) were a stand-alone reform, we would support it. The ACCC, however, links it to the introduction of swathes of new regulations on unrelated topics (ie non-discrimination and other pricing regulations). Ongoing compliance with all these complex, new regulations would be more burdensome and costly than the requirement to produce a Network Service Plan once every five years. Accordingly, we would not support the repeal of Part 5 (Network Service Plans) if this were conditional upon the introduction of the ACCC's proposed new regulations. In that case, the status quo would be preferable.

1.9 Given the scope and complexity of the ACCC's Draft Advice, this submission is necessarily focused on key concerns only. A great deal more could be said about how the ACCC's various specific proposals would adversely affect individual operators.

2. Structure of this submission

2.1 Our submission first summarises some high-level observations about the approach which the ACCC has taken in the Draft Advice.

2.2 We then turn to some specific comments on new regulations or changes proposed by the ACCC which we expect would be particularly disruptive or concerning for our members and their customers, in particular:

(a) the new non-discrimination regulations (rule 10);

(b) the new prohibition of certain charges (rule 10A);

(c) the new regulations concerning schedules of charges (rule 11) and pass-through of costs (rule 9A);

(d) the new regulations concerning distributions (rule 45); and

(e) the new regulations concerning termination fees (rules 70 to 75).

2.3 Finally, we explain why the ACCC's assessment of compliance costs is deficient and significantly understates the compliance costs to be borne by operators. We also note that, contrary to the express instruction in the Terms of Reference to "*assess opportunities to reduce cost to industry **and governments***", the ACCC ignores the increased cost to governments of all the new regulations the ACCC is advocating.

3. High-level observations

3.1 **Non-compliance with the *Water Act 2007* (Cth)** – With respect to member-owned operators, the ACCC has not complied with the specific requirements of subsection 93(3) of the *Water Act 2007* (Cth) which requires that the ACCC, when advising the Minister on the Water Charge Rules, or proposed amendments to them, must have regard to:

(a) the governance arrangements of infrastructure operators;

(b) the current charging arrangements of those operators; and

(c) the history of the charging arrangements of those operators.

The details and implications of the ACCC's non-compliance are explained in paragraph 3.2.

3.2 **Member-owned operators should be less heavily regulated** – The starting point is that the public policy position has always been that member-owned operators (being those infrastructure operators that are owned and therefore controlled by their customers) should be less heavily regulated. It is a specific requirement under paragraph 93(3)(a) of the *Water Act 2007* (Cth) that the ACCC, when advising the Minister on the rules, must have regard to the governance arrangements of infrastructure operators. In light of this, and because member-owned operators are controlled by their customers, under the existing Water Charge Rules, their pricing decisions are generally unregulated (with just a couple of exceptions, such as termination fees and the simple requirement not to price-discriminate against customers who have transformed their irrigation rights).

Furthermore, the ACCC has not had regard to member-owned operators' current charging arrangements and their history, despite the specific requirements of paragraphs 93(3)(b) and (c) of the *Water Act 2007* (Cth). Operators' charging arrangements have been developed and refined over long periods by elected representatives of each operator's customers. The ABARES survey commissioned by the ACCC (and referred to in the Draft Advice) found that:

(a) over 90% of customers say that their current schedule of charges clearly sets out the difference between charges payable for holding or using water and charges payable for accessing the operator's infrastructure;

(b) over 80% of customers say that their current schedule of charges clearly sets out the differences between charges payable for access to the operator's infrastructure and charges incurred by the operator and passed on to the customer (bulk water charges); and

(c) around two-thirds of customers say that the current schedule of charges provides sufficient information for them to calculate the charges payable to terminate some or all of their water delivery rights.

Notably, on all three of those issues, the percentages were higher in the regions where the majority of survey respondents were customers of member-owned operators. The results indicate a high degree of understanding among customers of current charging arrangements. Many of these arrangements have long histories which explain their current structures, but none of this has been examined properly by the ACCC, despite the clear legislative obligation to do so. Charging arrangements determined by the customers' own representatives should not be disturbed lightly.

The ACCC concedes on pages 57 and 58 of the Draft Advice that member-owned operators are less likely to take advantage of their market power to the detriment of their customers. Similarly, page 187 of the Draft Advice states: "*The ACCC has not found evidence that the general price level of operators are being set to achieve monopolistic profits at the expense of irrigators*".

Furthermore, the ACCC commissioned an independent expert, Marsden Jacob Associates, to identify circumstances under which the structure of regulated charges may distort trade decisions or act as a barrier to trade. Page iii of their report states: "*Overarching Conclusion Two: We could find no evidence that Irrigation Infrastructure Operator (IIO) charges are distorting water markets*".

In light of the ACCC's own findings, and the findings of its own survey and independent expert, the logic for regulating member-owned operators less heavily remains unchanged. Indeed, there is a compelling case for reducing the regulatory burden on member-owned operators, which is what this review was supposed to be about.

3.3 **ACCC offers no evidence for increasing regulation** – Nevertheless, despite those findings of fact, the ACCC now advocates much heavier regulation of member-owned operators because they *may* have incentive to discriminate against some customers. But the ACCC does not cite

even one actual example of this having occurred. Instead, the ACCC puts forward three arguments.

(a) First, the ACCC claims that operators may have incentive to discriminate against customers who trade water out of irrigation districts – but no actual instance of such discrimination is identified.

(b) Second, the ACCC claims that operators may have incentive to discriminate against customers who have transformed their irrigation rights – but that is not a reason to introduce a series of burdensome new regulations because this type of discrimination is already unlawful under rule 10 of the *Water Charge (Infrastructure) Rules 2010* (Cth).

(c) Finally, the ACCC claims that operators may use tiered pricing structures which may benefit large users over small users in a way that is not commensurate with underlying differences in costs of service provision to these users, particularly where voting rights are based on the size of holdings. However, in both examples cited by the ACCC (Murrumbidgee Irrigation and Murray Irrigation), voting by members of the operators is one vote per landholding, which gives small users very significant voting power. The ACCC's argument is not persuasive.

In summary, the ACCC offers no actual evidence for increasing regulation of member-owned operators.

3.4 **Increased regulatory burden contrary to the Terms of Reference** – Nevertheless, the overall effect of what the ACCC is proposing is a substantial increase in the regulatory burden on member-owned operators. The terms of reference specifically required the ACCC to assess opportunities to reduce cost to industry and government. In contrast, what the ACCC has actually done is to cast aside the principle that member-owned operators should be less heavily regulated and put forward a very unorthodox view of regulatory simplification that is not supported by evidence and does not appear to be consistent with the Terms of Reference. On page 66, the ACCC claims "*Streamlining the application of the rules to apply to **all** infrastructure operators is consistent with stakeholder feedback to simplify the regulatory framework*". That is a very strange way of defining "simplification". Adding voluminous new regulations and applying them to all operators is not a simplification of the regulatory framework: it is a significant expansion of the regulatory burden borne by member-owned operators which are less heavily regulated at present. It also ignores the specific requirement under paragraph 93(3)(a) of the *Water Act 2007* (Cth) that the ACCC, when advising the Minister on the rules, must have regard to the governance arrangements of infrastructure operators.

3.5 **Effect is to tell member-owned operators how to charge** – The effect of what the ACCC is proposing is that the benefit of being a member-owned operator and having the freedom to determine one's own water charges with less regulation will be substantially removed. The proposed new non-discrimination regulations, the new pass-through regulations, the new termination fees regulations and the new regulations about permitted ways to make distributions to customers have the practical effect of requiring member-owned operators to charge for infrastructure services in the limited ways left open by the proposed new web of regulations. This will reduce pricing flexibility and stifle innovation, weakening a key plank in the Australian Government's innovation strategy.

3.6 **No relationship with what it's replacing** – One sensible proposal the ACCC has made is the abolition of Network Service Plans. This is appropriate because it responds to the requirement of the Terms of Reference to "*assess opportunities to reduce cost to industry and governments*" and to "*reduce regulatory burdens*". However, the ACCC wants to make this conditional on the introduction of swathes of expansive new regulations dealing with completely different issues. The proposed new non-discrimination regulations, for example, bear no relationship to the content of Network Service Plans, which deal with plans for works, estimates of expenditure, plans for financing, details of grants or subsidies and estimates of regulated charges. There is no logical link or proper rationale for replacing Network Service Plans with new, unrelated regulations that will create a greater regulatory burden.

The proposed new regulations would apply to all operators, regardless of size. The industry believes that the ACCC has underestimated the number of operators that will be impacted. Since the abolition of Network Service Plans would only assist the few larger operators to which Part 5 currently applies, none of the smaller operators would receive any offsetting benefit upon the introduction of the new regulations. These smaller operators would be subject to significant new regulation.

3.7 **Combining the rules is of little benefit** – The ACCC recommends combining the *Water Charge (Infrastructure) Rules 2010*, *Water Charge (Termination Fees) Rules 2009* and the *Water Charge Planning and Management Rules 2010* in one instrument (page 46). The benefits from combining the three instruments into one are marginal, and it appears that the ACCC is instead taking the opportunity to rewrite and expand the rules significantly.

4. Non-discrimination regulations (rule 10)

4.1 **Increased regulatory burden** – The ACCC proposes a significant expansion of the current non-discrimination rule, which amounts to six lines in rule 10 of the *Water Charge (Infrastructure) Rules 2010* (Cth). The ACCC proposes to replace this simple rule with over two pages of complex new regulations. We describe below some of the difficulties which are likely to be caused by the new non-discrimination regulations. Paragraph 4.6 discusses what is one of the most potentially damaging of the proposed new regulations: the new 'limited availability of service' regulation, which prohibits operators from charging any fees at all in certain circumstances.

Smaller operators would be burdened by all these new regulations and would not benefit from the abolition of Network Service Plans (which they are not currently required to prepare).

4.2 **Discrimination based on the purpose for which water has been or will be used (rule 10(1)(a)(i))** – This proposed new regulation will require every operator to scrutinise their schedule of charges and consider a range of commonplace arrangements. To take one example, some operators have different charges for differently-sized outlets, which reflect different levels of service and are often associated with the different purposes for which water is used. This may inadvertently be regarded as discrimination under these regulations.

This new regulation may also affect the pricing of arrangements between operators and non-member customers, such as on-river operators, for the use of the operator's infrastructure for the delivery of water, whether for environmental or other purposes. For example, it may be advantageous to operators to charge a lower price per megalitre for the bulk delivery of environmental water at times when their systems would otherwise remain unused, rather than the price per megalitre charged by operators for the delivery of smaller volumes of irrigation water. This mutually beneficial arrangement could, however, fall foul of the new regulation and result in a perverse outcome for both parties.

In order to maintain the arrangements described above, the operator would have to satisfy the ACCC that either these are different classes of infrastructure service or the price differences reflect differences in actual costs. Based on our members' experiences with the ACCC, either option could be a time-consuming and expensive exercise (requiring legal advice and personnel to be dedicated to the task), and even if the operator were to persuade the ACCC, the operator could still fall foul of the new 'limited availability of service' regulations, referred to in paragraph 4.6 below.

4.3 **Discrimination based on whether a tradeable water right has been traded or transformed (rule 10(1)(a)(ii))** – The difficulty with the proposed new regulation is that it does not expressly permit an operator to charge a transformed customer for the operator's administrative costs incurred when the customer trades water allocation back onto the operator's water access right. Unless such charges can be levied, customers who do not choose to transform bear these administrative costs.

4.4 **Discrimination based on the holding, volume or use of a tradeable water right (rule 10(1)(a)(iii))** – This raises a number of issues:

(a) Some operators have different charges for different categories of water delivery right. If the ACCC queries these arrangements, the operators would have to satisfy the ACCC that either these are different classes of infrastructure services, or the price differences reflect differences in actual costs. Either would be a time-consuming and expensive exercise involving legal advice and requiring personnel to be dedicated to the task, and even if the operator were to persuade the ACCC, the operator could still fall foul of the new 'limited availability of service' regulations, referred to in paragraph 4.6 below.

(b) Some operators use tiered charging structures. The ACCC states on page 58 of the Draft Advice: " *… the use of tiered regulatory structures may benefit large users over small users in a way that is not commensurate with underlying differences in costs of service provision to these users*" and on page 63: "*When the purpose of the tiered tariff structure is not related to economies of scale, and therefore cannot be justified by reference to cost differentials, it can mean that customers with smaller water holdings effectively subsidise customers with larger water holdings*".

Accordingly, it appears highly like that, if the new regulations were introduced, these operators would have to satisfy the ACCC that either the tiers represent different classes of infrastructure services, or the price differences reflect differences in actual costs (for example, through economies of scale). Either would be a time-consuming and expensive exercise involving legal advice and requiring personnel to be dedicated to the task. However, tiered pricing structures are not uncommon in consumption-based pricing by service providers in other industries.

The ACCC states, on page 64, that it is concerned that governance arrangements where voting is based on the size of irrigation right or water delivery right holdings may produce a situation where smaller customers are disadvantaged in favour of larger customers. However, in both of the cases of tiered pricing structures cited by the ACCC – Murrumbidgee Irrigation and Murray Irrigation – shareholders have one vote per landholding, providing small users with very significant voting power (indeed, disproportionately large voting power in comparison to their shareholdings and tradeable water right holdings) and the ACCC's stated concern does not apply.

(c) This new regulation would also affect WaterNSW's discounts to operators unless WaterNSW can show that these operators receive a different class of infrastructure service or the discount reflects the difference in the actual cost of providing the service. If WaterNSW does not do so, then many customers of NSW operators will have to pay more as a result of the ACCC's new regulations. This would represent a perverse economic outcome for the customers of irrigation operators.

4.5 **Discrimination based on the area of land owned, occupied or irrigated, including where land is not owned, occupied or irrigated (rule 10(1)(a)(v))** – Some operators have separate charges for 'inactive' customers or non-landholders, and all of these charges would need to be assessed to determine whether either these are different classes of infrastructure services or the price differences reflect differences in actual costs.

4.6 **Operators cannot charge for services if their availability is limited on certain bases (rule 10(2))** – One of the most concerning parts of the new non-discrimination regulations proposed by the ACCC is the new regulation which states that operators cannot charge for a service at all if its availability is limited on certain bases. This new regulation has the potential to quickly make an operator insolvent if it were to lose a dispute over a limitation which has been in place for many years. The consequences of this new regulation could be severe.

To take one example: an operator cannot charge for a service if its availability is limited on the basis that the customer must hold a tradeable water right to receive it. This undermines the entire contractual basis on which operators deal with their customers – that is, on the basis that customers' tradeable water rights define the services which they are entitled to receive. Under the new regulation, if an operator were to limit certain water delivery services (for example, the availability of winter watering, or priority of access in times of supply limitations) to customers

who hold high security water delivery rights, the operator could not charge for those services. Surely, that cannot be what is intended, but it is what the new regulation literally says. The Draft Advice states that this new regulation is "*[t]o ensure the efficacy of [the other non-discrimination] provisions*", but we do not agree with that assessment. The penalty – that the operator must not levy any infrastructure charges in relation to a service the availability of which is limited in contravention of the new regulation – is extreme. It has the potential to make the operator insolvent if it were to lose a dispute about a limitation that has been in place for many years. The civil penalty in paragraph 10(2) is excessive in any event.

Some examples of perverse or unintended outcomes from this proposed new regulation include the following:

(a) If an operator could not limit the availability of an infrastructure service by reference to the purpose for which water will be used, then an operator could not limit the availability of irrigation outlets to irrigators but not domestic customers (and subrule 10(3) of the draft new Water Charge Rules does not assist because it only applies where the service is of a type that is limited to stock and domestic customers only). This produces the result that any customer could demand any service offered to any other customer; for example, domestic customers could demand the type of irrigation outlet that is normally only available to irrigators. To take another example, a customer whose landholding lies far distant from the nearest irrigation channel and receives domestic water through a pipe could demand the same service of water for irrigation purposes as the customers whose landholdings lie adjacent to that channel.

(b) If an operator could not limit the availability of an infrastructure service by reference to the holding of a tradeable water right, then the operator could not limit the availability of water delivery services on the basis that the customer does not hold enough water allocation to satisfy the water delivery order.

(c) If an operator cannot limit the availability of an infrastructure service by reference to the holding of a separate location-related right, then the operator could not limit the availability of water in a lake to those customers who have adjoining landholdings (with pumps); the new regulation would require the operator to offer the same service of delivery of water from the lake to customers whose landholdings were distant from the lake. Subrule 10(5) does not assist because it only permits the operator to specify different charges, not limit availability.

(d) If an operator cannot limit the availability of an infrastructure service by reference to the holding of a tradeable water right, then the operator could not limit the availability of carryover services by reference to the holding of general security water entitlements. This would undermine the entire basis of the property right represented by tradeable water rights. Subrule 10(4) does not assist because the limitation imposed on the customer is by reference to an irrigation right not a water access entitlement. It would also undermine the policy objectives of State governments with respect to carryover arrangements.

(e) If an operator cannot limit the availability of an infrastructure service by reference to the holding of a tradeable water right, then the operator could not impose water restrictions on customers holding domestic tradeable water rights. This is highly problematic for operators which are required to impose such water restrictions under State law. Subrule 10(3) is of no assistance because it applies to paragraph 10(2)(a) only but not paragraph 10(2)(c).

(f) Subrule 10(3) is flawed because it only assists with respect to "*stock and domestic*" purposes, not just one of "*stock*" purposes or "*domestic*" purposes.

5. Prohibition of certain infrastructure charges (rule 10A)

5.1 **Operators must be able to require payment of outstanding charges as a condition of approving a trade** – This is a key form of security for all member-owned operators. For example, it enables operators to ensure that they can recover unpaid charges when a bank appoints a receiver to sell a customer's water entitlements. Subrule 10A(2)(d) very strongly implies that this form of security would become unlawful. This would have a serious impact on operators' ability to recover unpaid charges, particularly from insolvent customers.

5.2 **Satisfying the ACCC that application fees are reasonable and efficient (rule 10A(2)(b))** – In the experience of our members, satisfying the ACCC that fees are reasonable and efficient involves a very detailed analysis of all the steps in the process to which the fee relates, the appropriate levels of seniority of the personnel involved at each stage, the appropriate amount of time to be spent on each stage, and the costs (and on-costs) associated with these personnel. In our members' experience, this is a time-consuming and expensive process. The imposition of this new regulation would represent an increase in the burden of regulation and cost to industry and government.

6. Schedule of charges (rule 11)

6.1 **Increased regulatory burden** – The ACCC proposes to introduce over three pages of complex new regulations regarding schedules of charges. The proposed new regulations would apply to all operators, regardless of size. Since the abolition of Network Service Plans would only assist the few larger operators to which Part 5 currently applies, none of the smaller operators would receive any offsetting benefit upon the introduction of these new regulations.

6.2 **Increased complexity** – The ACCC indicates (on page 75 for example) that irrigators' feedback was to the effect that pricing regimes are too complex but it now proposes to introduce additional complexity by:

(a) making the regulations significantly more lengthy, detailed and prescriptive about the information which must be included in a schedule of charges; and

(b) introducing new regulations about pass-through of particular charges which will need to be added to the schedule of charges.

6.3 **Pass-through requirements (rule 9A)** – The new rule 9A will require every operator of any size to:

(a) first, review every charge that the operator pays to another operator or to a State Agency, and consider whether that charge is an "*infrastructure charge*" or a "*planning and management charge*", or neither;

(b) second, classify every infrastructure charge and planning and management charge as either a "*directly attributable charge*", "*distribution loss shared charge*" or "*shared charge*", all of which are newly-defined terms in rule 9A, for a total of up to six categories of charge;

(c) third, restructure its charging arrangements so that each of the six categories of charge is passed through to customers in the way mandated by rule 9A, which, in some cases, may involve amending the operator's contract with its customers and going through the applicable contractual processes for doing so; and

(d) finally, changing its schedule of charges to reflect the updated charging structure and comply with the regulatory processes for changing the schedule of charges.

This will be a considerable undertaking for every operator and it will add complexity to the schedule of charges. This new regulation alone represents a considerable new compliance burden.

In addition, these new requirements are confusing, ambiguous and difficult to apply in practice. For example:

(a) Regarding the definition of "*directly attributable charge*":

(i) It is not clear how an operator can ever incur an infrastructure charge or a planning and management change as a direct consequence of a customer holding an irrigation right. The operator incurs such charges because it holds the water access right and this would be the case regardless of whether the customer holds an irrigation right.

(ii) Also, the market has developed a wide variety of irrigation rights and there is often no obvious relationship between an irrigation right and any particular category of water access right in the operator's portfolio.

(b) The definition of "*distribution loss shared charge*" hinges on the operator being able to prove that water is actually lost during distribution. Actual losses vary significantly as circumstances change during a water year and this new requirement would make periodic invoicing very complicated.

(c) There is no convincing explanation of why "*distribution loss shared charges*" should have to be separate from the operator's other charges for its infrastructure services.

(d) All of these separate charges will make it more complicated for a customer to determine their liability in respect of any particular period.

It is also another example of a new regulation which will stifle pricing innovation and reduce the ability of operators to differentiate themselves based on their pricing structures.

It is difficult to understand why complex new pass-through regulations are required at all given that the ABARES survey commissioned by the ACCC found that over 80% of customers say that their current schedule of charges clearly sets out the differences between charges payable for access to the operator's infrastructure and charges incurred by the operator and passed on to the customer.

6.4 **Penalty for breach of pass-through requirements (rule 72(2)(a)(ii))** – The consequence of not complying with the pass-through requirements is that the termination fee multiple is 1 rather than 10. This is an extreme outcome that bears no relationship to the nature or gravity of the non-compliance, particularly given the potential complexity of achieving compliance. The effect would be to increase the fixed costs to the remaining customers who are blameless. The civil penalties proposed in rule 9A are excessive in any event.

6.5 **Stifling innovative commercial arrangements** – Individual commercial arrangements between operators and sophisticated counterparties, such as environmental water delivery arrangements and hydroelectric power station arrangements, will need to be disclosed in public. Many commercial entities are unlikely to agree to the disclosure of such charges, and this is likely to stifle these innovative arrangements, which would otherwise help defray the costs to be recovered from irrigators. Applying to the ACCC under rule 9 for an exemption from disclosure would be unappealing because the legal test for the exemption (in subrule 9(1)) is difficult to satisfy and, even if the exemption were granted, the ACCC is proposing to add a new regulation requiring the operator to publish the name of the counterparty, the period of the arrangement and the class of infrastructure service.

6.6 **Publication on web site should be sufficient** – In the interests of reducing the costs to industry, it should be sufficient for an operator to publish its schedule of charges on its web site rather than having to send a copy (even electronically) to every customer. In many cases, operators do not possess electronic contact details for all customers.

6.7 **Electricity charges** – The proposal does not seem to have addressed the issue, which is relevant to some operators, of passing through electricity charges which are, or sometimes are, unknown at the time of publishing the schedule of charges. Electricity charges can, in some cases, only be discovered by operators retrospectively.

6.8 **Drafting** – Subrule 3(6) – The term "*send*" should be used for consistency with subrule 11(4)(a).

7. Distributions regulations (rule 45)

7.1 **No stakeholder support for increased regulation** – The ACCC acknowledges, on page 129, that the only feedback was against increased regulation: "*The only feedback the ACCC received from stakeholders on Part 7 was from Murrumbidgee Irrigation Limited (MI), Western Murray Irrigation (WMI) and Coleambally Irrigation Cooperative Limited (CICL). Both MI and WMI submitted that Part 7 should not extend to an operator that makes a distribution to some (but not all) of its members*".

7.2 **It will capture every operator which makes distributions at present** – At present, a number of member-owned operators make distributions of water allocation to their customers when they have additional water allocation available for this purpose.

Under the current rules, an operator which makes such a distribution to *all* of its members becomes a Part 7 operator, which means that its regulated water charges must be approved or determined by the ACCC or an accredited agency.

At present, no operator is caught by Part 7 because not *all* members receive the distributions.

However, the ACCC is now proposing to turn this rule on its head, without giving a proper explanation for such a significant change. The ACCC's proposal is that an operator becomes a Part 7 operator if it makes a distribution, other than a standard distribution, to *any* customer. The key standard distribution is one made to *all* customers in proportion to their right of access. That means that if any *one* customer with a right of access misses out, then it is not a standard distribution. For example, allocations would not count as standard distributions if customers with outstanding overdue charges were ineligible. Similarly, if an operator's special individual arrangements with sophisticated counterparties do not give the counterparty an entitlement to distributions of additional water allocation when it is available, then no allocation by that operator could be a standard distribution.

As far as we are aware, at present, there are no Part 7 operators, because among those operators who allocate distributions, at least *one* customer misses out on the distribution. For the exact same reason, these operators (of which there is a significant number) will *all* become Part 7 operators under the new regulation. There is no threshold for the operator's size or consideration of governance arrangements. Accordingly, unless they change their business models, they will *all* be required to have their water charges approved or determined by the ACCC or an accredited agency. In the Draft Advice, it is noted that WaterNSW spent $200,000 on the process of having its water charges approved. Similar additional costs could be expected for other operators, which will be passed on to customers.

7.3 **"Standard distributions" will be impossible for many operators** – The key standard distribution is one made to *all* customers in proportion to their right of access. This might be feasible if the rights of access of every customer of an operator were defined in the same way. In that case, proportionality could be achieved. In practice, however, most operators offer different types of rights of access, which can vary widely depending on each customer's particular circumstances. For example, some customers may have a right of access defined as the right to delivery of a certain volume of water within one year. Others may have a right of access defined as the right to have delivered, or to take, an unlimited volume of water when the water level in a channel or body of water reaches a certain trigger point and remains above it. Others still may have a right of access which is defined by reference to a share of the available capacity (eg a flow rate share) in a particularly constrained part of the operator's network. There is no way of comparing these different types of rights of access and determining whether a distribution to customers was made in proportion to their rights of access. The consequence is that most

operators will be unable to make "*standard distributions*" and they will therefore be likely to become Part 7 operators.

7.4 **Distributions from reserves** – The new regulations will catch a distribution of an operator's reserves, or any part of its reserves, to any customer. This would include the distribution of reserves to a customer as an incentive to close a section of channel.

7.5 **Supplementary water and off-allocation supply** – The new regulations may inadvertently catch various forms of supplementary and off-allocation distributions made by operators to their customers. Some of these types of distributions reflect long-standing and binding agreements but are not back-to-back with a water access entitlement of the operator, so sub-paragraph 45(3)(e)(i) would not apply.

7.6 **Drafting** – **Subrule 45(3)(e)(i)** – No member-owned operator holds its water access entitlement "*on behalf of the holder*". The water access entitlements are not, and never have been, held on trust. This was made clear when the operators were privatised. It is a purely contractual relationship. The drafting does not reflect this and the carve-out will be of no assistance. Indeed, there is no requirement for the operator to hold any water access entitlement at all: it could just source all of its customers' water allocation in the market. Furthermore, operators do not always promise that their irrigation rights will reflect the allocation of any particular water access entitlement. There is usually some leeway to grant more or less water allocation, and in any case, most types of water allocation are effectively fungible and operators retain the freedom to manage their water access entitlements and water allocation in various ways, so long as they honour their contractual obligations to credit the volume of water allocation to which customers are entitled.

8. Termination fees

8.1 **No general stakeholder support for increased regulation** – The ACCC acknowledges, on page 176, that the feedback generally supported the current arrangements: "*The Independent Expert Panel (the Panel) reviewing the Act received no submissions specifically on the WCTFR, which it considered indicated that the rules may be operating effectively. … Submissions to the ACCC's Issues Paper were generally supportive of the provisions currently forming the WCTFR; in particular, there were no submissions challenging the general application of the '10 times multiple' which caps the maximum amount of the termination fee an operator is permitted to charge. … Many submissions that discussed the WCTFR supported the current approach to termination fees*".

8.2 **Increased complexity** – The ACCC proposes to introduce additional complexity by adding new regulations about calculating termination fees. Among other things, the calculation relating to separate charges for exclusive infrastructure (eg outlets) in rule 72(2) will be an enormously complicated exercise that may need to be done separately for every single outlet in every single operator's irrigation network.

8.3 **Notice to terminate in the future** – The new drafting reopens the loophole whereby a customer can give notice of an intention to terminate a right of access at some point years in the future, thereby locking in the current charges for the purpose of calculating termination fees. Refer to subrule 72(5)(a).

8.4 **Prohibition on imposing a termination fee** – Subrule 71(2)(b) is to the effect that an operator cannot impose a termination fee if the operator provides a water storage service and includes the charges for storage in the charges for the right of access. The drafting of this new regulation is ambiguous as to whether it applies to an operator which permits carryover by holders of certain irrigation rights and does not charge separately for the 'storage' service. This is an important point as the consequences could be catastrophic.

8.5 **Increased costs to irrigators** – Many of the ACCC's new regulations seem calculated to reduce termination fees. The effect of this will be that, when rights of access are terminated, the remaining irrigators will be have to bear more of the ongoing fixed costs of the system than would otherwise be the case. Ultimately, this goes to the viability of the system.

8.6 **Damages** – Rule 77 has the effect of taking away an operator's common law right to claim damages for a breach. No justification for this has been offered.

9. Part 6 operators (rule 23)

9.1 **Drafting** – Paragraph 23(b)(i) is drafted ambiguously, and taken literally, would have a wider application than intended by the ACCC. This is because the literal wording of paragraph 23(b)(i) would capture all operators which have at least one customer who has transformed their irrigation rights but retained a water delivery right with the operator. This would potentially capture many operators, although the Draft Advice states that this is not the ACCC's intention; page 97 states: "*Based on current circumstances, the ACCC considers that upon the commencement of the amended rules, there will be no infrastructure operators that would immediately meet the new conditions for the application of Part 6.*"

10. Assessment of costs

10.1 **Cost to governments is being ignored** – Contrary to the express instruction in the Terms of Reference to "*assess opportunities to reduce cost to industry **and governments***", the ACCC ignores the increased cost to governments of all the new regulations the ACCC is advocating. The ACCC, among others, would incur significant new costs in monitoring, applying, investigating and enforcing all of the new non-discrimination regulations, the new pass-through regulations, the new regulations about schedules of charges, the new termination fees regulations and the new regulations about permitted ways to make distributions to customers. This cost must be factored into the analysis.

10.2 **ACCC has not included legal costs** – The ACCC has made no allowance for operators' legal costs. Taking into account our members' experiences from when the current (much simpler) Water Charge Rules were introduced, we estimate that external legal advice will be required in the order of 50% of the number of hours for the operator on each item in the ACCC's assessment in Chapter 9 of its Draft Advice at an approximate blended hourly rate of $500 plus GST. This may be substantially more where, for example, it is determined that changing the basis on which regulated water charges are imposed or calculated will necessitate amendments to an operator's contracts with its customers. Notably, external legal advice was generally not obtained with respect to the content of Network Service Plans, which focused on non-legal matters, such as levels of service, plans for works, capital and recurrent expenditure and estimates of regulated charges (so there will be no saving for Part 5 operators in that regard). By contrast, extensive legal advice will be required by every operator of any size (not just those few which are currently required to prepare Network Service Plans) in order to achieve compliance with the new regulations.

10.3 **ACCC underestimates the initial and ongoing compliance burden** – A very detailed initial review will be required to restructure each operator's charging arrangements and schedule of charges in order to comply with all the new regulations. In many cases this will involve changing the bases on which charges are levied or calculated. Reviews of an operator's charging methodology are significant exercises, which can take months of work at the highest levels in an operator's organisation, together with external professional advice. They involve significant disruptions to operators' businesses. A similar process will have to be undertaken every time any change is to be made to an operator's charging arrangements. The ACCC is seriously underestimating the initial and ongoing compliance burden.

For example, Central Irrigation Trust calculates that it has incurred costs in the vicinity of $60,000 to date simply in assessing the ACCC's Draft Advice and attempting to determine its meaning and the potential impact on the organisation. A number of other operators are also incurring significant costs in this phase. This does not include any of the actual implementation costs that would be incurred if the ACCC's proposals were to become law.

10.4 **Inconsistent treatment of publication requirements** – On page 83, the ACCC expresses the view that "*The ACCC is of the view that, while mailing of documentation may be an option used by some operators, it is not generally necessary to be compliant with the [existing] Rules*". Why then is the ACCC factoring in a reduction in printing, postage and associated staff time in connection with the schedule of charges (and Network Service Plans)? This is internally inconsistent. In any case, a number of operators cannot reliably contact all of their customers by email, and so mailing is a practical necessity.

10.5 **Cost of becoming Part 7 operators** – All infrastructure operators which make distributions are not caught, at present, because not all customers receive them. For the same reason, they will all be caught under the new regulations. Accordingly, the cost of having their charges determined by the ACCC should be added. A reasonable estimate for the costs imposed by these new rules is the costs incurred by WaterNSW in having its charges approved or determined, multiplied by the number of affected operators. WaterNSW has estimated that its costs of meeting regulatory and ACCC requirements were $200,000 (page 225 of the Draft Advice).

11. Conclusions

11.1 Our main conclusions are:

(a) with respect to member-owned operators, the ACCC has not complied with the specific requirements of subsection 93(3) of the *Water Act 2007* (Cth) which requires that the ACCC, when advising the Minister on the Water Charge Rules, or proposed amendments to them, must have regard to:

(i) the governance arrangements of operators;

(ii) the current charging arrangements of those operators; and

(iii) the history of the charging arrangements of those operators;

(b) the ACCC's argument, in meetings with our members, that additional non-discrimination regulations are desirable to enforce a principle of equitable treatment of customers is not persuasive and the ACCC has been unable to explain why the irrigation sector ought to be treated in such a radically different way from other regulated sectors which are not subject to such extensive non-discrimination requirements, such as the prices charged by electricity retailers, urban water utilities and local governments (for rates);

(c) the ACCC should not abandon the principle that member-owned operators should be less heavily regulated unless there is strong and compelling evidence that they are taking unfair advantage of their market power;

(d) the ACCC has presented no such evidence; in fact, the ACCC concedes that it is not happening; and

(e) the ACCC's proposed new regulations represent a very substantial increase in the regulatory burden on member-owned operators, and are contrary to the Terms of Reference which required the ACCC to "*assess opportunities to reduce cost to industry and governments*" and to "*reduce regulatory burdens*"; the proposed new regulations will capture sections of the industry, especially smaller operators, which the ACCC has not effectively engaged in the process;

(f) there are many examples of proposed new regulations that have been poorly considered and drafted which will lead to unintended, perverse or onerous results, which could be catastrophic for some businesses; and

(g) the ACCC is seriously underestimating the additional cost to industry and government of its proposed new regulations.

11.2 For those reasons, we disagree with the Draft Advice and we strongly oppose the ACCC's proposed new Water Charge Rules. The existing Water Charge Rules are far preferable.

11.3 The only significant part of the Draft Advice which responds appropriately to the Terms of Reference to reduce regulatory burdens and costs to industry and governments is the proposal to repeal the requirement for Part 5 operators to produce Network Service Plans. If the repeal of Part 5 (Network Service Plans) were a stand-alone reform, we would support it. However, we would not support it if it were conditional upon the introduction of the ACCC's proposed new regulations. In that case, the status quo would be preferable.