



*Australian Dairy Industry Council Inc.*

## **Australian Dairy Industry**

Represented by

Australian Dairy Industry Council Inc.

Response to

Water Amendment Bill 2015 (Provisions)

31 July 2015

**Submission to:** Senate Standing Committees on Environment and Communications  
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## Contents

The Australian dairy industry .....	1
Contact for submission .....	1
Summary of submission and recommendations.....	2
Background.....	3
Water Amendment Bill 2015 (Provisions) .....	6
1. 1500GL cap on buybacks. ....	6
2. Socio-economic neutrality test. ....	7
3. Covering the gap to 2750GL first.....	8
4. Greater flexibility in water recovery under the Water for the Environment Special Account Act 2013.....	9
5. Greater flexibility to trade environmental water. ....	9

## The Australian dairy industry

The Australian Dairy Industry Council (ADIC) is the dairy industry's peak policy body. It co-ordinates industry's policy and represents all sectors of the industry on national and international issues through its two constituent bodies, Australian Dairy Farmers Ltd (ADF) and the Australian Dairy Products Federation (ADPF).

Australian dairy is a \$13 billion farm, manufacturing and export industry directly employing 43,000 Australians and indirectly providing a livelihood for more than 100,000 people in dairy related service industries. Australia's 6300 dairy farms produced approximately 9.6 billion litres of milk in 2014-15. The dairy industry is highly dependent on water through irrigation systems or rainfall to produce high quality fodder, provide stock drinking water and operate a dairy milking shed.

Approximately 28% of Australia's milk is produced in the Murray Darling Basin providing more than 12,000 jobs on farms, in processing and local service industries. The Basin Plan has so far reduced the total volume of water available for irrigation, trade and carryover by about 13% in the southern-connected Basin; if fully implemented, the reduction will be approximately 26% on average each year. Dairy farmers will need to boost their productivity by 20-25% if milk production is to recover to pre-drought levels.

## Contact for submission

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## Summary of submission and recommendations

The Australian Dairy Industry Council (ADIC) supports the proposed amendment to legislate the cap on water entitlement purchases at 1500GL.

We also support explicitly including off-farm water saving infrastructure projects in the socio-economic neutrality test in the Murray-Darling Basin Plan. However we do suggest further amendment to better achieve triple bottom line outcomes rather than assuming individual farmer participation in such projects means no negative socio-economic effects for the community and other businesses.

The ADIC has significant concerns about some aspects of the Bill. In particular that the 1500GL buybacks cap applies only to water recovered towards meeting the 2750GL target. This effectively enables a future Government to abandon on-farm works and irrigation efficiency programs and revert to buybacks to recover the additional 450GL under the Water Amendment (Water for the Environment Special Account) Act 2013. This is not acceptable. It is not consistent with the intent that water will be recovered in a way that has no negative social or economic impacts on Basin communities and nor does it reflect the previously stated intent that Section 86AD(2)(b) in the Special Account Act was only to allow 'flexibility' in certain circumstances.

The Water Amendment Bill 2015 also misses an important opportunity to address long-standing limitations in the Water Act 2007 and the Basin Plan in achieving the socio-economic neutrality and triple bottom line outcomes promoted so often by decision-makers. These limitations include water recovered under the Special Account not counting towards the 2750GL target first; that Section 106(2) of the Water Act does not provide flexibility in trading environmental water to raise funds for investment that contributes to environmental outcomes; and the need for flexibility in the volume recovered beyond 2750GL based on socio-economic impacts.

With more than 1160GL a year already removed from the productive pool through buybacks and farmers transferring entitlements to the environment under on-farm infrastructure projects, these limitations exacerbate the negative socio-economic effects of a reduced pool of water available for irrigated production. Irrigators and the communities that rely on them are rightly worried about what will happen if more water is removed from productive use to cover the remaining 795GL gap to the 2750GL target, much less the additional 450GL under the Water for the Environment Special Account.

A summary of our proposed legislative solutions for this Bill follows, with further detail outlined in the remainder of the submission.

**Recommendation 1:** Amend 85D(4) to ensure that the 1500GL cap on buybacks includes the 450GL in the Water for the Environment Special Account.

**Recommendation 2:** Amend 85C(4)(b) to clarify that the entitlement transfer to the Commonwealth relating to infrastructure and reconfiguration for state programs are excluded in the 1500GL cap on buybacks.

**Recommendation 3:** That subparagraph 7.17 in the Basin Plan be further amended to broaden the socio-economic neutrality test to include collective impacts on irrigation districts, community and water market.

**Recommendation 4:** That the Basin Plan be amended to ensure that the 2750GL target is achieved first before any water recovery is counted towards the 3200GL target, and that any water recovered under the Special Account first covers any shortfall to the 2750GL target.

**Recommendation 5:** That the Water for the Environment Special Account Act 2013 and the Basin Plan 2012 be amended by inserting the words 'up to' in front of all references to the 450GL.

**Recommendation 6:** That the Water Amendment Bill 2015 include a new clause to amend Section 106(2) in the Water Act 2007 enabling environmental water trading where the proceeds can be reinvested in works and activities for environmental outcomes, and to cover the CEWH's storage and other costs.

## Background

Dairy is the largest irrigation-based livestock industry in the Murray Darling Basin, and accounts for 28% of Australia's total milk production. The Basin dairy industry's 2014-15 farm gate milk value was \$1.3 billion, with regional processing worth \$3.25 billion in value-added dairy products.

More than 12,000 people in the Basin rely on dairy for their livelihoods, including farm and factory workers, tanker drivers, dairy machinery technicians, financial services, vets, feed brokers and suppliers, farm equipment suppliers, agronomists and farm advisers.

The bulk of the industry is in the Murray Dairy region, which covers northern Victoria and the southern Riverina. This region is the largest milk producing region in Australia, accounting for 25% of national production. In 2014-15, it produced 2.3 billion litres of milk, with a farm gate value of \$1.2 billion. Nine major processing factories are located in the Murray Dairy region, along with many smaller processors. More than 9000 people living here rely on dairy for their livelihoods.

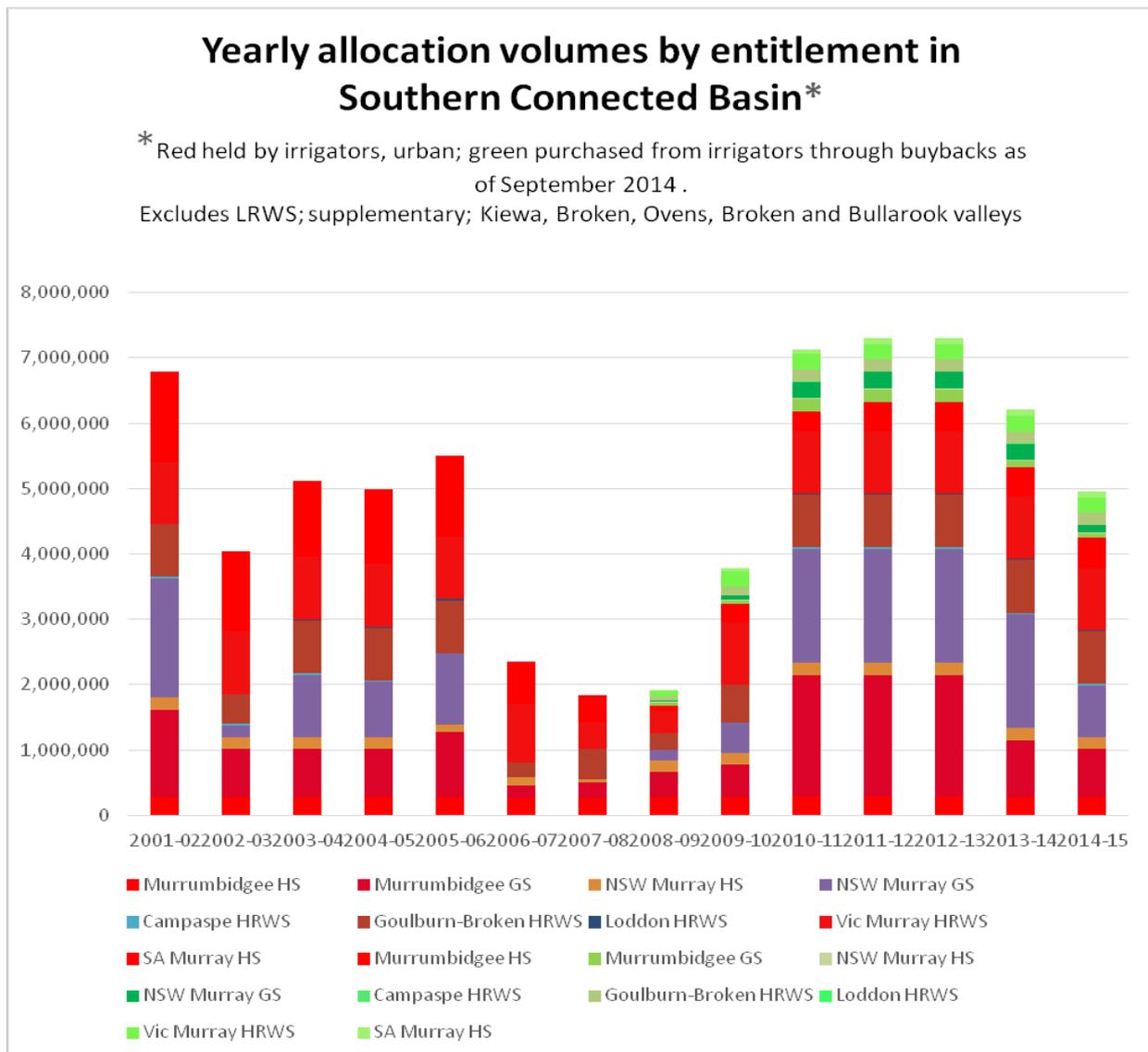
Water availability and affordability are our key issues. As it stands, more than 1160GL (long-term annual average) has been lost from the pool allocated for irrigation in the Basin. More than 950GL of this has been sourced in the southern-connected Basin, where it represents about 13% of the annual average water availability. It includes about 20% of Victoria and South Australia's high reliability entitlements, which underpin those States' high-value dairy industries.

Reduced water availability is constraining the dairy industry's capacity to recover milk production to the pre-drought levels in 2001, much less grow to meet growing export demand for high-quality, safe dairy products, particularly in China.

Farmers have substantially adapted production systems, and invested in on-farm water efficiencies often with welcome assistance from government programs, but our industry is now reaching the limits of economically viable further changes. And there is a limit when dairy farmers are price takers in domestic and export markets, and cannot pass on increases in water and other costs associated with adapting to a future with less water.

Many dairy farmers, along with those in other commodities, sold some or all of their water entitlements to the environment for desperately needed cash flow during the drought. They must now source some or all of their water from a much smaller pool on the temporary allocation market. In simple terms, more irrigators are now competing in a market for much less water offered for trade.

The volume of water allocated for irrigation varies from year to year depending on seasonal conditions and inflows into the storages, particularly in NSW. The volume available is now much less, because so much that was previously allocated to irrigators is now owned by the environment (Figure 1).



**Figure 1. Annual volume of water allocated against entitlements, and ownership.**

Prices are rising year-on-year (Figure 2), making it difficult to control costs and plan production with any certainty.

At the same time, the volume of entitlements held in shared irrigation districts has declined dramatically, mostly due to water recovery for the Basin Plan in recent years (Figure 3). The less water delivered in these collective systems, the less revenue to cover fixed maintenance and operating costs, and the greater the upward pressure on water charges imposed on irrigators.

In short, a significant adverse impact of adjustment is already being felt in the dairy industry, even if no more water is transferred from the consumptive pool across to the environment.

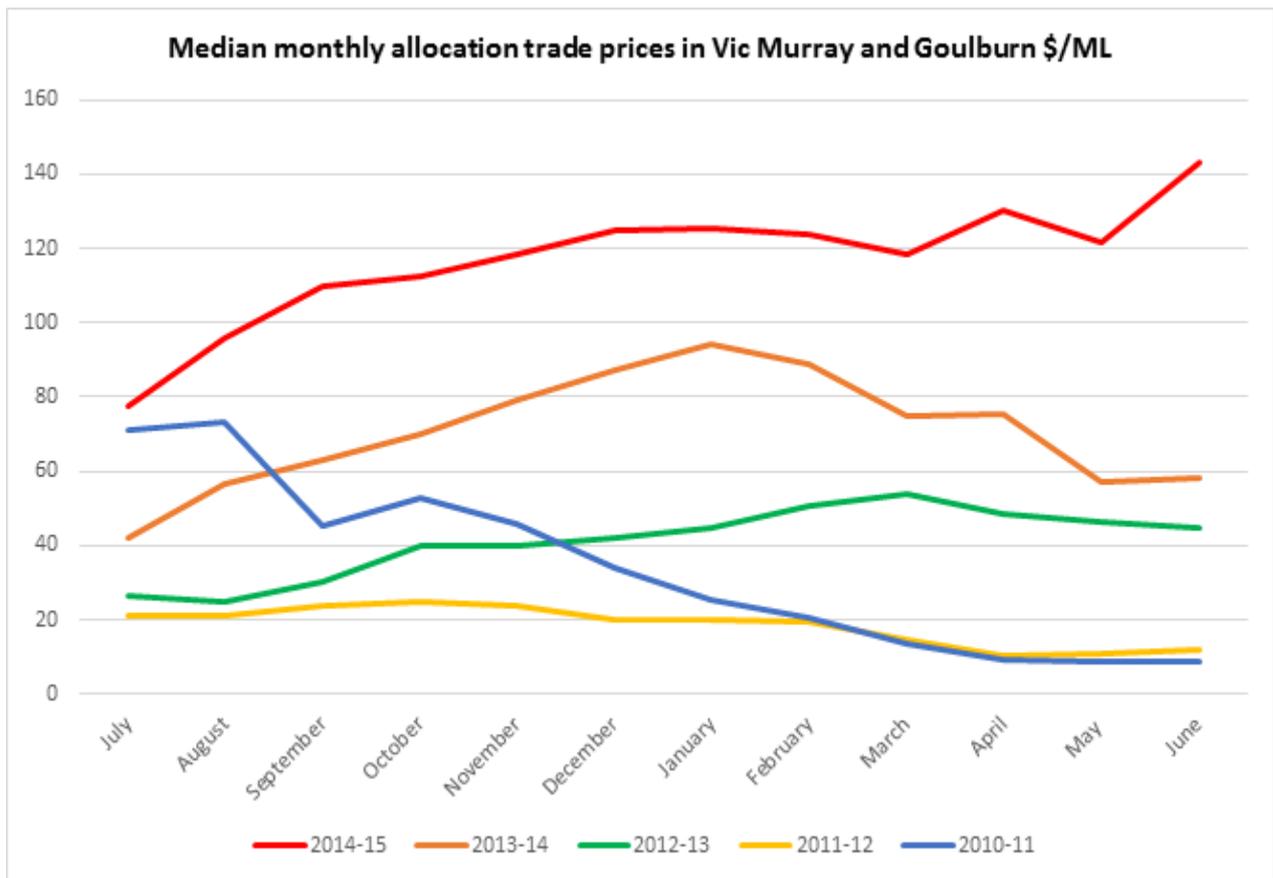


Figure 2. Median monthly price \$/ML in Victoria (source Victorian Water register).

**High reliability water shares in Northern Victoria (2000/01 to present)**

The graph below shows how the volume of high-reliability water shares in northern Victoria are divided between customers in the irrigation districts, private diverters and those who have disassociated their water shares from land<sup>1</sup>.

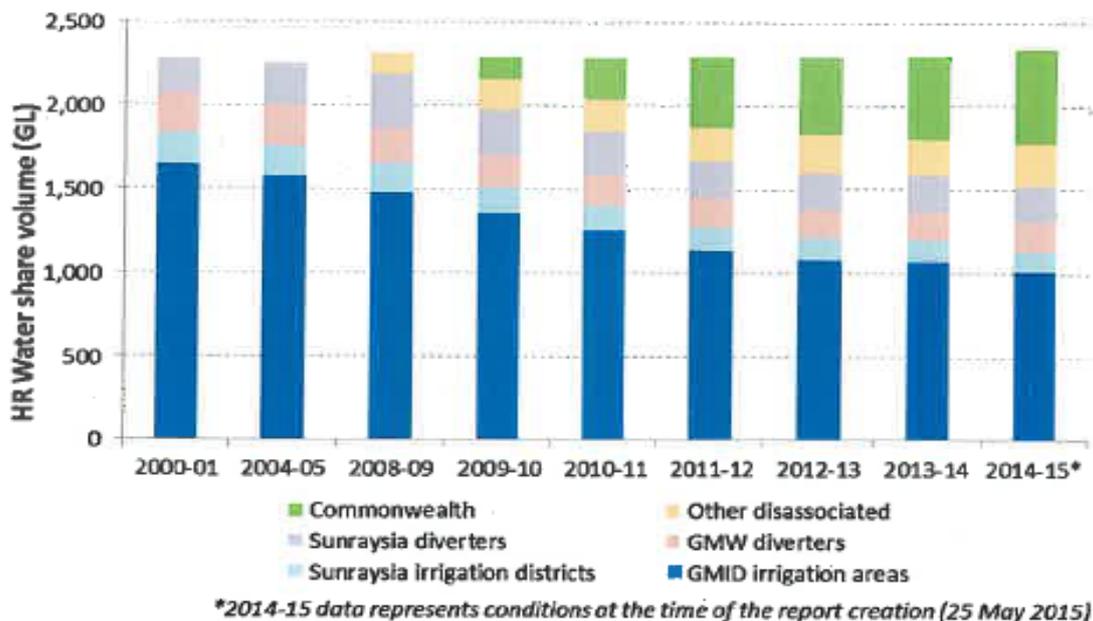


Figure 3. Ownership of high reliability water shares in northern Victoria

## Water Amendment Bill 2015 (Provisions)

### 1. 1500GL cap on buybacks.

The dairy industry has long advocated for buybacks to be capped at 1500GL, to minimise the negative socio-economic effects of reducing the volume of water available for production. We strongly support a legislated cap through amendment to the Water Act 2007.

The dairy industry supports investment in water-saving infrastructure as an alternative means of increasing the water available to the environment that also enables structural adjustment in farming systems. We also support environmental works as a means of achieving similar environmental outcomes with less water, and reducing the need to remove more water from production.

The 1500GL cap on buybacks as part of the 2750GL of recovery provides important certainty for dairy farmers about the direction and programs that will be used to implement the Basin Plan. This certainty is critical for farmers already facing a tough productivity challenge.

Case studies have shown that water buybacks have greater localised social and economic impacts on irrigation dependent communities than investment in water efficiency projects. In a 2012 study of ten dairy farms with irrigation modernisation projects, it was found that buybacks cost the Australian Government around \$2000/ML, but are associated with reduced regional farm productivity which in turn reduces regional economic activity by around \$4300 for every megalitre purchased by the Government.

Meanwhile, farm upgrades cost the Australian Government about \$3700/ ML for the environment's share of water savings. However, upgrades also delivered \$9800/ML worth of increased farm productivity (annualised capital value). Using this water to increase production generates additional regional economic activity worth \$6200/ML<sup>1</sup>.

The 1500GL cap on buybacks will increase the need for transparency and accountability in water-saving infrastructure programs and projects. The community must have greater confidence that Federal and State funds are being spent appropriately, cost-effectively, and that they will in fact achieve the stated socio-economic as well as environmental objectives. Greater transparency and accountability will give the community confidence that their interests, as well as those of the environment, are being taken into account, and that public money is not being squandered on less than optimal projects.

Spending on environmental works needs to deliver improved environmental outcomes without unintended third-party consequences. Infrastructure must be engineered correctly in consultation with landholders and community familiar with the area. For example, it is not enough for works to just get large volumes into sites and hold the water there. For the best environmental outcomes and to avoid third-party impacts, the system must use designs and technology to drain sites adequately in the event of flood conditions. Local knowledge is essential in getting the infrastructure design right. Environmental water managers must win community trust that water will be used efficiently and effectively to get the best results, just as the community expects irrigators to be water-wise.

The dairy industry does not agree with excepting the 450GL recovered under the Water for the Environment Account (new subsection 85D(4)(e)), from the 1500GL cap.

The Explanatory Memorandum to the Water Amendment Bill 2015 justifies the exclusion by citing Part 2AA in the Water Amendment (Water for the Environment Special Account) Act 2013. It claims that under this Part, the Commonwealth will not recover this additional water through open market purchase. Instead water access rights may only be obtained in conjunction with projects to improve water use efficiency, or alternative arrangement proposed by a Basin State (Section 7.17 of the Basin Plan).

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<sup>1</sup> RMCG, *Cost Benefit Analysis of Farm Irrigation Modernisation*, May 2013. Full report and fact sheet available at: <http://www.dairyaustralia.com.au/Industry-information/About-the-industry/Recent-industry-topics/Murray-Darling-Basin.aspx>

The Memorandum thus acknowledges the provisions of 86AD(2)(a) under Part 2AA, focusing on water recovery through infrastructures and other means, but ignores 86AD(2)(b), which explicitly states that water access rights may be purchased to meet the 450GL target.

In 2012, when the Water for the Environment Special Account Bill was drafted, the Government at the time assured stakeholders the intent of 86AD(2)(b) was only to allow 'flexibility', where some on-farm works and irrigation infrastructure efficiency programs might include a purchase component. However, the Special Account Act itself does not explicitly make this link.

Past and current governments have also repeatedly assured stakeholders that the additional 450GL of water will be recovered without negative social or economic impacts on Basin communities. Clause 86AD(2)(b) is not consistent with this intent. Neither is it consistent with the expressed intent in the Explanatory Memorandum for the Water Amendment Bill 2015, which says the Sustainable Diversion Limit can be adjusted provided environmental, social and economic outcomes are not compromised.

Future governments will not feel bound by the good intentions of those in office now. Government administrators will always be guided only by the letter of the law. Clause 86AD(2)(b) in the Special Account Act enables a future Government to abandon on-farm works and irrigation efficiency programs and revert to buybacks to recover the additional 450GL. This is not acceptable.

We are also concerned that the inclusion of 85C(4)(b) in the Water Amendment Bill 2015 may enable further recovery of water beyond the 1500GL cap through pressure on the Basin States to purchase water on behalf of the Commonwealth. This sets up a perverse incentive for the Basin States, for example to enter the permanent entitlement market to recover water to offset any State shortfalls. If the intention is that the new section 85C(4)(b) only relates to entitlements being transferred back to the Commonwealth through infrastructure reconfiguration (as per the Explanatory Document), then the wording needs to be amended to make this clear.

**Recommendation 1: Amend 85D(4) to ensure that the 1500GL cap on buybacks includes the 450GL in the Water for the Environment Special Account.**

**Recommendation 2: Amend 85C(4)(b) to clarify that the entitlement transfer to the Commonwealth relating to infrastructure and reconfiguration for state programs are excluded in the 1500GL cap on buybacks.**

## **2. Socio-economic neutrality test.**

The dairy industry welcomes amending subparagraph 7.17 in the Murray-Darling Basin Plan 2012 to explicitly include participation in off-farm water saving infrastructure projects in the socio-economic neutrality test.

We note the words of the Parliamentary Secretary to the Minister for the Environment Bob Baldwin in his second reading speech for the Water Amendment Bill 2015 on 28 May 2015:

*Our vision for water reform in Australia is very clearly founded in a triple bottom line outcome. We understand that the focus must be on the social, economic and environmental benefits equally. We will not achieve optimal outcomes through the Basin Plan without this triple bottom line focus.*

However, the socio-economic neutrality test in the Basin Plan is not consistent with achieving triple bottom line outcomes. This is because it is based only on individual participation; that is, that the mere fact a farmer decides to participate means the project has no negative socio-economic effects.

This ignores the need for comprehensive socio-economic impact assessment if more water is removed from the productive pool to meet the 2750GL target, and the additional 450GL in the Special Account.

Impacts include upward pressure on prices in the water market and fixed costs in shared irrigation districts, and effects on production and the broader community.

Determining the direct and indirect adverse impacts of the Basin Plan is a complex exercise. For example, recovering water through on-farm works has both positive and negative implications, and these need to be well understood in order to inform socio-economic neutrality assessment.

Otherwise, the Government runs a serious risk of paying to address negative impacts in future that could have been avoided in the first place, and when it may be too late to save irrigation districts and their communities from sliding into economic unviability.

By way of illustration, the Bill's support for recovering water through on-farm works is a welcome investment in regional development and increased farm productivity. As such, it is a meaningful structural adjustment payment that is paying social and economic dividends far in excess of the original investment. This is because it helps keep farmers, regional processing, and farm service industries in business, and therefore supports the overall wellbeing of the community and national economy.

However, it needs to be remembered that on-farm works have a downside. This is because farmers transfer a portion of their entitlements equal to the savings they achieved. In this way, like buybacks, on-farm works will result in a smaller collective pool of water entitlements available for irrigation overall.

This has cost implications in dry seasons, when less water is available on the temporary market to alleviate low allocations. It also has cost implications for shared irrigation districts, because less water delivered to farms means less revenue, forcing water companies to raise prices to cover the shortfall.

There is a real danger that a farmer may upgrade the farm to produce more with less water under the on-farm works program, only to be unable to afford to have his water delivered because of increased system charges and be therefore be unable to sustain, much less grow, production due to scarce and expensive water on the temporary market.

**Recommendation 3: That subparagraph 7.17 in the Basin Plan be further amended to broaden the socio-economic neutrality test to include collective impacts on irrigation districts, community and water market.**

### **3. Covering the gap to 2750GL first**

There is still a gap of almost 800GL to reach the 2750GL benchmark, before any attempt to recover the additional 450GL towards a 3200GL target.

The dairy industry is concerned about how Environment Department officials are interpreting Chapter 7 in the Basin Plan, 'Adjustment of SDLs'. This Chapter sets out the Sustainable Diversion Level Adjustment Mechanism, which allows the SDL to be adjusted up or down by 5%. The mechanism will be applied in 2016, taking account of water recovery measures completed or planned by 2019.

Officials appear of the view that they must recover at least a proportion of the 450GL under the Water for the Environment Special Account by 2019 commensurate with the budget schedules set out in the Special Account Act. This means recovering water counting towards the additional 450GL, at the same time as water is still being recovered to meet the 2750GL target by 2019. So we will have competing water recovery programs.

The reasoning seems to be the adjustment mechanism requires that any recovery offset through environmental works for the 2750GL target, must be balanced by recovery of water towards the 450GL target. It leaves unanswered how any shortfall to achieving the 2750GL will be covered, as Special Account Water would only count towards the 3200GL target.

The dairy industry believes the 2750GL target must be met first, and that any water recovered under the Special Account budget to 2019 must first go towards covering any shortfall to the 2750GL target. This would be consistent with the socio-economic neutrality and triple bottom line outcomes promoted so often by decision-makers.

**Recommendation 4: That the Basin Plan be amended to ensure that the 2750GL target is achieved first before any water recovery is counted towards the 3200GL target, and that any water recovered under the Special Account first covers any shortfall to the 2750GL target.**

#### **4. Greater flexibility in water recovery under the Water for the Environment Special Account Act 2013.**

The Government is legally bound to recover 450GL under the Water for the Environment Special Account Act 2013, with this absolute volume reflected in the Basin Plan Part 2, Division 1, 7.09(e) Note 1. The Act then sets out a Budget appropriation schedule to achieve this volume of water.

Our concern is that this does not, legally speaking, provide any flexibility to reduce the volume recovered in the face of negative socio-economic impacts. Rather, the Act tends to suggest any impacts will be addressed after all the water has been recovered.

**Recommendation 5: That the Water for the Environment Special Account Act 2013 and the Basin Plan 2012 be amended by inserting the words 'up to' in front of all references to the 450GL.**

#### **5. Greater flexibility to trade environmental water.**

Section 106(2) in the Water Act 2007 allows the Commonwealth Environmental Water Holder (CEWH) to trade entitlement or allocation only under very restrictive conditions. Trades can only occur if the water can't be stored or carried over, and can't be used to good environmental effect. The proceeds can only be used to acquire other water to improve environmental objectives.

These requirements set a very high bar on CEWH trades because they effectively deny the use of trading if the outcome is neutral in terms of environmental outcomes, even if the trades generate major socio-economic benefits.

It also limits the CEWH's ability to raise money to fund other highly valuable activities and works that might generate better environmental outcomes, and to pay the annual storage and other fees associated with the environmental entitlements. The environment should pay its way, when it has the means to do so through trade.

Greater flexibility in trading environmental water remains a top priority for Basin industries and communities. This was clearly articulated through the independent review of the Water Act in 2014 and also in a recent public meeting in Barham NSW with Senators involved in the current Inquiry into the Murray-Darling Basin Plan. More than 1000 people came to the meeting, endorsing among other things flexibility in environmental trading.

Not making this amendment now will be a missed opportunity to both respond to community calls for change, and to make a change that will help to alleviate concerns about water availability now and in the future.

**Recommendation 6: That the Water Amendment Bill 2015 include a new clause to amend Section 106(2) in the Water Act 2007 enabling environmental water trading where the proceeds can be reinvested in works and activities for environmental outcomes, and to cover the CEWH's storage and other costs.**