

Australian Dairy Industry Response to the Review of the Water Act 2007

Represented by
Australian Dairy Industry Council Inc. and
Dairy Australia

7 July 2014

Submission to:
Water Act Review Secretariat
wateractreview@environment.gov.au

Contacts

ADIC: Irene Clarke — Senior Policy Manager, Australian Dairy Farmers

DA: Claire Miller — Manager, Policy Strategy, Dairy Australia

Contents

Introduction.....	2
1. The scope and timing of the review of the Water Act.....	3
2. Assessment of the use of water for higher value uses [section 253 (2c)].....	3
3. The effectiveness of the Act in achieving its objects, as set out in Section 3	4
The triple bottom line.....	5
Optimising social, economic and environmental outcomes	5
Water recovery programs.....	5
The focus on volume, not outcomes.....	6
Too many agencies and not enough funding.....	7
4. Opportunities to reduce or simplify the regulatory and/or reporting burden while maintaining effective standards.	8

Introduction

The Australian Dairy Industry Council (ADIC) is the dairy industry's peak policy organisation. It coordinates industry policy and represents all sectors of the industry on national and international issues through its two constituent bodies, Australian Dairy Farmers (ADF) and the Australian Dairy Products Federation (ADPF). The ADIC aims to foster, promote and protect the interests of the Australian dairy industry by driving a whole of industry approach to dairy policy and the development of the dairy industry.

The ADIC is supported by Dairy Australia (DA), the national services body for dairy farmers and the industry. Its role is to help farmers adapt to a changing operating environment, and achieve a profitable, sustainable dairy industry. As the industry's research and development corporation, it is the investment arm of the industry, investing in projects that can't be done efficiently by individual farmers or companies.

The dairy industry is one of Australia's major rural industries. Based on farm gate value of production, it is ranked third behind the beef and wheat industries. There are approximately 6,400 farmers producing over 9 billion litres of milk annually. The dairy industry is the largest value added food industry, contributing \$13 billion at wholesale to the economy. It is estimated that 43,000 people are directly employed on farms and in dairy manufacturing. Dairy processing and service industries are largely based in rural areas, thus generating significant employment and economic activity in regional Australia.

The industry was closely involved in the development of the Murray Darling Basin Plan, and continues to closely monitor its implementation. We welcome the opportunity to contribute to the 2014 Review of the Water Act 2007, including the consideration of the effectiveness of the Act in achieving its objectives as set out in section 3 of the Act.

This is an opportunity to amend and clarify the Act and associated regulations and subordinate instruments to ensure this historic reform can deliver genuine triple bottom line outcomes.

The dairy industry supports improved environmental outcomes in the Murray Darling Basin. Its focus throughout this long process is how this can best be achieved while also ensuring that irrigated industries are in a strong position to adapt to and prosper in, a future with less water.

The dairy industry will focus this submission on the following aspects of this review:

1. The scope and timing of the review of the Water Act 2007
2. The effectiveness of the Act in achieving its objects, as set out in section 3 of the Act; and
3. Opportunities to reduce or simplify the regulatory and/or reporting burden while maintaining effective standards.

The dairy industry welcomes the Murray-Darling Basin Ministerial Council's separate review of the governance arrangements for joint activities in the Murray-Darling Basin. This is a very important part of the review of the Water Act, particularly in the interests of reducing red tape and therefore costs for irrigators, reducing duplication of effort across Federal and State agencies; and aligning objectives and priorities.

1. The scope and timing of the review of the Water Act

We note that the 2014 review is in many respects premature. For example, as the Basin Plan trading rules only come into effect in July 2014, it is too early to comment on the effectiveness of the Act in assisting water trading in the Murray Darling Basin.

Similarly, it is too early to judge whether the long-term Sustainable Diversion Limits (SDLs) are being met. Superficially, the SDL translates to a simple recovery of 2750GL of water by 2019 from consumptive use, through infrastructure savings and entitlement buybacks. To this extent, progress towards this target is being made with a total of 1900GL recovered so far.

In reality, the actual SDLs will be determined by the SDL adjustment mechanism described in Chapter 7 in the Basin Plan; the mechanism means the final volume of water diverted from consumptive use back to the environment will be anywhere between 2100GL and 3200GL.

This volume will be determined by a complex combination of water savings, environmental offset works, the review of northern basin SDLs, and constraints management, all of which remain in flux. It will also be determined by an adjustment methodology that lacks the transparency required to engender stakeholder confidence.

It will not be possible to assess the extent to which the SDLs are being met, or will be met, until the SDL adjustment mechanism is initially applied in 2016 with a final reconciliation after 2024. Even then, the SDL reflects annual average yields in a system characterised by annual extremes so it will take some years before it becomes apparent whether the SDLs are being met consistently.

Given the Basin Plan was only signed in 2012, and is still in its very early implementation phase, it is not possible to meaningfully comment on the matters identified for review in Section 253 of the Act. However, we can provide some comment on clause 2 (c) in Section 253 of Act, which requires an assessment of the extent to which water is being used for higher value uses, as a measure of the Basin Plan's success.

2. Assessment of the use of water for higher value uses [section 253 (2c)]

The assessment under Section 253 (2) (c) of the extent to which water is being used for higher value uses, reflects market economic theory in which higher value is measured on the economic return per megalitre of water. On this basis, it is assumed that water will over time be diverted from annual cropping and pasture-based industries such as dairy, into perennial plantings such as orchards, to maximise its economic value to regional communities and Australia.

This is a highly simplistic measure and its shortcomings were all too clearly revealed in the drought. The difficulty is that each State has different water management frameworks with water products of varying reliability. These water products do not necessarily reflect the broad economic value of the use beyond return per megalitre, or the different “value” equation across different commodities, or the flexibility of different types of irrigated industries to maximise returns with the water products and irrigation infrastructure available.

Dairy operates in part on annual pastures, but it is a high value use of water returning significant economic value to the producer, local communities and Australia. This value is demonstrated not just in the type of plantings or milk production per megalitre of water used, but also in the flow on value of that milk production. For example, dairy in the Goulburn Murray Irrigation District in northern Victoria has a farmgate value of more than \$940 million in 2014, while the industry’s added value to the regional economy is worth more than \$2.350 billion due to its broad range of service industries, and through the jobs and economic activity associated with nine major dairy factories in the region.

The volume of water used does not have a direct causal link to returns. Dairy farms may use more or less irrigation water depending on factors such as rainfall and water prices. Returns are a complex combination of fluctuating factors such as global milk prices and climatic conditions affecting milk production rather than how much water is used.

Dairy’s inherent competitive advantage over other irrigation industries became evident during the drought. Dairy can use more or less water and still sustain good returns due to the flexibility in the way it can use water. For example, dairy can substitute irrigated home-grown pasture when water is short, with bought-in feed -- often paid for by selling its water allocation at high prices to orchards that may take seven years to return to full production if the trees die.

This flexibility means dairy can sustain itself in tough times and be ready to bounce production back very quickly. This was evident in the fact total milk production bounced back to pre-drought levels within two years of the drought ending, despite fewer dairy farms.

Dairy is unique in its flexibility, resilience, high return, local processing, and strong demand. This makes dairy a high value industry to regional communities, where it can be relied on to sustain jobs and production. This dynamic is not captured in simplistic higher-value measures of returns per megalitre used based on types of plantings.

Assessing the value of water use is complex. The Act needs to better reflect the broader concept of higher value and acknowledge unique factors with different commodities.

Recommendation 1. *Change the approach in the Act of water for higher value uses being linked to permanent plantings only. In its place, the Act should endorse the approach of irrigators maximising returns for the water they use, by commodity, recognising that dairy is a high value use and movement of water use to dairy is likely to be a measure of success for effective water markets.*

3. The effectiveness of the Act in achieving its objects, as set out in Section 3

The effectiveness of the Act in achieving its objectives cannot be considered in isolation of the funding and institutional capacity required to effectively deliver on the objectives.

This review should consider whether the Act’s objectives are in fact appropriate. Governments and agencies will always face the risk of being held to the letter of the law. That means regardless of the Basin Plan’s objectives or commitments by governments of the day, the Act as it stands dictates environmental precedence over all other considerations.

The triple bottom line

When the Water Act was being drafted, not all Basin states had agreed to hand over their Constitutional water management rights to the Federal Government. The Federal Government consequently relied on its external powers to achieve a head of power under the Constitution that would enable it to recover water to increase environmental flows.

The objectives in the Act are therefore weighted heavily in favour of achieving environmental outcomes, with a general legal consensus that the Act's objective to also manage water to optimise social and economic outcomes is a secondary consideration.

The Basin Plan five years later sought to articulate a more balanced, triple bottom line approach to managing water resources. So while its objectives echo those in the Act, they give more weight to social and economic outcomes.

At the time, the Government argued that a more balanced set of objectives in the Basin Plan would enable a triple-bottom line approach to water management. However, the dairy industry remains concerned that the Basin Plan is a subordinate instrument of the Act, and that in the event of a legal challenge, the environmental imperatives in the Act could well prevail.

Times change. The States have now all signed up to the Basin Plan and agreed to its implementation, removing much of the original reason to invoke the Commonwealth's external powers.

Now is the time to amend and align the objectives in the Act and the Basin Plan to remove the primacy of the environmental outcomes over social and economic considerations. The objectives should instead unambiguously support triple-bottom-line outcomes.

Recommendation 2. Amend and align the objectives in the Act and the Basin Plan. Remove the primacy of environmental outcomes over social and economic considerations in the Act, and instead unambiguously state triple-bottom-line outcomes.

Optimising social, economic and environmental outcomes

The Basin Plan's management objectives include optimising social, economic and environmental outcomes. It is too early to tell whether this objective will be met, but the signs are not promising.

The reasons are manifold, but most are rooted in the number of different agencies involved in the Basin Plan's implementation. There is significant overlap or duplication of responsibilities, and agencies they do not share a universal interpretation of what they are seeking to achieve under the Act and therefore the Basin Plan.

Water recovery programs

Federal programs to recover water for the environment are not properly integrated to optimise the environmental social and economic outcomes across programs and across agencies. They have been individually designed to meet their own internal program objectives, regardless of whether or not they in turn undermine the capacity to meet the triple-bottom line. They are also not properly integrated with State programs in order to provide complementary approaches in achieving outcomes.

For example, the Federal Environment Department has prioritised the Water Act's environmental objectives. It has sought to achieve those objectives by narrowly focusing on recovering 2750GL in water entitlements at least cost per megalitre, and preferably through simple buyback auctions rather than water-saving infrastructure.

A least-cost per megalitre bottom line is also applied to water entitlements recovered through the On-Farm Irrigation Efficiency Program (OFIEP). This approach ignores whether delivery partners are aligning their works with broader regional development and structural adjustment objectives.

This least cost per megalitre approach has resulted in water being randomly removed from irrigation districts, without considering the implications for that district's viability. Implications include stranded assets, while fewer farmers are left to share the fixed costs for operating their shared infrastructure.

This is compounded when farmers are being required to settle for sub-optimal upgrades to meet the least-cost per megalitre imperative. A more flexible approach that was properly integrated with regional development objectives would deliver greater economic dividends by supporting optimal farm production systems.

The current approach to water recovery is also inconsistent with the objectives of irrigation district modernisation, in which both State and Federal Governments are also heavily investing. Irrigation modernisation delivers water savings for the environment, while consolidating the infrastructure footprint to reduce shared costs and boost production through more efficient water delivery.

However, modernisation, buybacks and on-farm programs have so far largely occurred in separate 'silos' within the Environment Department.

The poor integration across programs and agencies has created a serious and growing risk of suboptimal adjustment in farming communities to the Basin Plan.

Recommendation 3. *Streamline, integrate and redesign all federal and state water recovery programs with a common objective to optimise social, economic and environmental outcomes.*

The focus on volume, not outcomes

The Water Act's objectives focus on achieving environmental outcomes, but this has been narrowly interpreted by the Federal agencies as translating to a minimum volume of water.

To this end, the Murray Darling Basin Authority (MDBA) and the Environment Department remain focused on recovering 2750GL of water in entitlements, regardless of whether the water can actually be delivered or used to good environmental effect. Risks include unacceptable third party effects such as flooding; scouring river banks; inability to water key sites at the height and duration needed for successful breeding events; and damage to infrastructure such as bridges, roads and culverts.

It is not a sound assumption that the Basin's environmental challenges can all be solved by merely running more water down the rivers.

The dairy industry welcomes the Federal Government's commitment to a 1500GL cap on buybacks, and a greater emphasis on recovering water through on-farm and off-farm irrigation infrastructure upgrades. However, this commitment, and what it means in practice needs to be shared by the MDBA, the Environment Department and States. We are concerned that the actions of agencies do not yet demonstrate that they will realise 650GL in environmental offsets.

Achieving 650GL in offsets is essential if the 1500GL cap on buybacks is to be sustained while still delivering the Basin Plan's 2750GL under the SDL adjustment mechanism. If the offsets are not achieved, the Plan provides for the shortfall to be covered by returning to the water market.

However, the dairy industry still does not see any serious effort to invest in environmental offset works. It seems government agencies are still assuming they can fall back on buybacks to meet shortfalls, despite the Government's commitment to the 1500GL cap. For examples, the MDBA's hydrologic modelling does not appear to recognise how environmental offsets can boost outcomes at key indicator sites. Instead, the sites are subsumed into river reaches, thereby negating the benefit of the offset works. We are concerned that the modelling may incorrectly make the case for more water to be removed from irrigation communities.

We are also concerned that a simplistic 'just add water' attitude towards achieving environmental outcomes may also be underpinning the constraints management work. For example, there seems to be an assumption that 450GL will be recovered regardless of third party impacts, even though the Act states that the recovery of an additional 450GL is subject to whether operational and physical constraints preventing delivering of the extra water can be overcome without unacceptable third-party impacts. We need a much better understanding of the socio-economic consequences and third-party effects of the Basin Plan's 2750GL target before determining that recovering another 450GL is appropriate.

The fact that the funding will be appropriated and available under Part 2AA of the Act (Water for the Environment Special Account) should in no way be driving the recovery of the 450GL. Rather, it must be informed by whether or not it can be delivered and the impacts of that delivery.

Recommendation 4. Amend and align the Act and the Basin Plan to:

- *Cap buybacks at 1500GL*
- *Deliver the 2750GL target in part through 650GL in environmental offsets, and*
- *Make it clear that the Government will not seek to recover an additional 450GL in the event that operational and physical constraints cannot be relaxed without unacceptable third-party effects.*

Too many agencies and not enough funding.

It is unlikely that the Act's environmental objectives will be met because of the number of agencies involved with too many different objectives. This adds cost and red tape, and is a highly inefficient way to optimise economic, social and environmental outcomes.

The various State and Federal agencies do not have the budgets required for the required monitoring, evaluation or reporting. In particular, the field work necessary to ground-truth whether the Basin Plan is in fact delivering its objectives is inadequate. We note that the Sustainable Rivers Audit, which at least provided a snapshot of the Basin's environmental condition, has been dumped to save money.

Instead, MDBA has indicated in its draft Basin Plan evaluation framework (20 May 2014) that it intends in future to rely almost entirely on modelling to determine whether the Basin Plan is delivering its environmental objectives, and environmental outcomes are improving. While we note that the modelling is being improved, it is still our view that modelling can only ever be a simplistic snapshot of a very complex and dynamic modified river system. We are concerned to ensure that modelling does not lead to perverse outcomes where decisions are based on the model, regardless of the evidence on the ground. This was certainly the case during the Basin Plan's development, and a source of much community anger and frustration.

Funding cuts announced in the 2014 Budget for the MDBA and Commonwealth Environmental Water Holder (CEWH) from 2017-18 undermines the effectiveness of the Water Act and the Basin Plan in achieving their objectives.

For example, the MDBA will go from \$45,180,000 in 2016-17 to just \$7,533,000 in 2017-18. The CEWH will go from \$34,672,000 in 2016-17, to just \$5,353,000. It should be noted that the CEWH is already liable for millions of dollars of State charges for storing its water entitlements, and managing its releases; the same charges are levied on irrigators to help cover the fixed costs for maintaining and operating the river system and its infrastructure. The CEWH will be unable to do its job to deliver improved environmental outcomes if it cannot even pay its bills.

This problem could be addressed by relaxing the environmental trade restrictions in Part 6, Section 106 of the Water Act. We suggest these restrictions be reconsidered to ensure they are not unreasonable, and do not perpetuate the flawed idea that water alone is all that is needed to improve the Basin's environmental health. For example, if the CEWH was self-funding and able to trade water to raise money to invest in activities, this may contribute to improved environmental outcomes.

The Basin Plan currently tasks the MDBA with developing environmental watering plans and strategies, and the CEWH with implementing those strategies. This seems like an unnecessary duplication that merely adds to red tape and cost.

The dairy industry also notes that two years after the Basin Plan was signed, we still do not have an agreed Basin-wide environmental watering strategy. Annual priorities are established by a range of environmental water managers at federal, state and regional level.

The CEWH has filled the void by expanding its role in annual environmental water planning, but this duplicates the MDBA's role. The CEWH, through its interaction with State environmental water holders and catchment management authorities, may have a more intimate and practical understanding of environmental water needs than the MDBA or the federal Environment Department.

Recommendation 5. Amend Part 2AA of the Act to allow for funding to optimise environmental outcomes, for example through environmental works, CEWH activities, and catchment management activities.

Recommendation 6. Reconsider Part 6, Section 106 in the Act and the potential outcomes if the CEWH was able to trade water for environmental purposes, with funds to be used to improve environmental outcomes.

Recommendation 7. Ensure responsibility for environmental watering plans and strategies rests with just one authority, preferably the CEWH, along with the capacity to plan and fund works and activities to enhance environmental outcomes.

4. Opportunities to reduce or simplify the regulatory and/or reporting burden while maintaining effective standards.

Many agencies are involved in compliance of one kind or another. This is not an optimal economic outcome given the costs are ultimately passed back to the irrigators. For example, we understand that the same or similar water information is collected, aggregated and distributed by the Bureau of Meteorology, the MDBA, State water departments, state water corporations, the ACCC, the National Water Commission, ABARES and the CEWH.

The dairy industry is particularly concerned about the onerous red tape imposed by the Environment Department on farmers involved in the On-Farm Irrigation Efficiency Program (OFIEP).

The Department is currently requiring farmers who receive funding to undertake an independent audit of their works at their own expense (\$1000-\$2000). This audit is effectively doubling up on the

requirement for the delivery partners themselves to also keep detailed records on each project to prove farmers are complying with the terms and conditions of their contracts.

This is an excessive red tape burden on farmers. Further, it does not represent best risk management practice in which random audits are the standard, with the addition of audits of any projects where there may be reason for concern such as non-compliance with terms and conditions by the farmer.

The Department's claim that the contracts with the delivery partners require all farmers to be separately audited rests on a very narrow and unreasonable interpretation of the relevant clauses.

This problem is symptomatic of the 'silos' that appear to operate inside the Department, where each water recovery program is managed independently. Integrating the different programs as discussed and recommended above will help to achieve a consistent and efficient approach to auditing and compliance.

Recommendation 8. Amend the Water Act to clearly delineate the responsibilities of the different agencies, reduce the number involved, and remove the current confusing overlap and duplication.

Recommendation 9. The Environment Department adopts standard risk management practice with random audits of individual farm projects, to complement the compliance records on each project already required of the delivery partners.