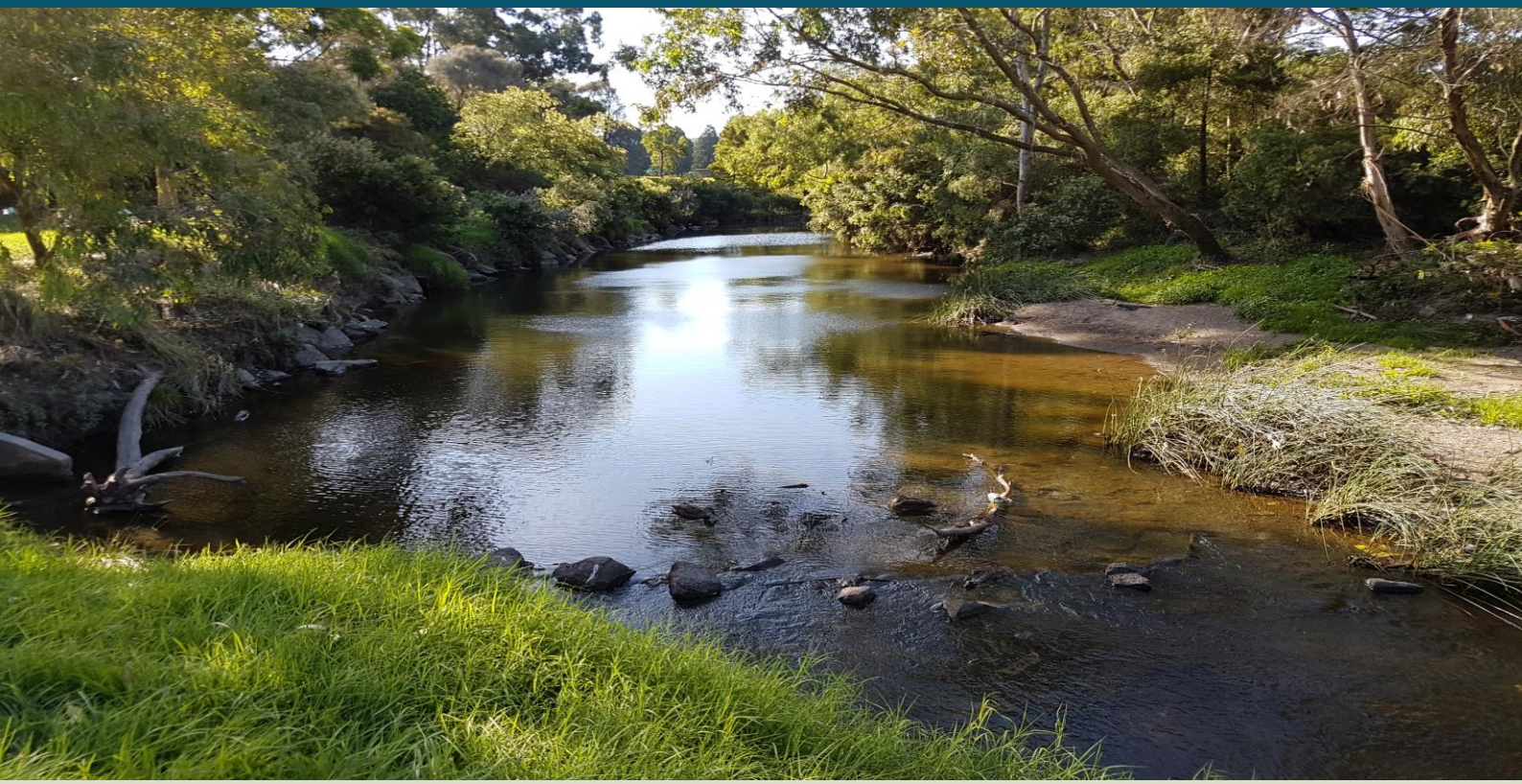
VICTORIAN WATER MARKET EFFECTIVENESS



Findings and actions from the 2017 Review

April 2018

VICTORIA State Government | Environment, Land, Water and Planning

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FOREWORD



Today, as we face increased pressure on our water supplies from climate change and changing demand from all water users, it is vital that our water markets are transparent and working effectively to give confidence to market participants and to allow water to move to where it is needed most.

Water for Victoria action 9.3 commits the government to ongoing statewide reviews of water market effectiveness. This first review has been an important first step in meeting a key government commitment to develop the water market in south central Victoria. Another key focus of this Government is building the water grid and a properly functioning market optimises the value of this infrastructure. The report of the review's findings, *Effectiveness of Victoria's Water Markets* (2018), will help guide next steps in market development in the south and across the rest of the state in regulated surface water, unregulated surface water and groundwater markets.

Through acting on the findings from this review Victoria will continue to lead the way in market development in Australia.

The assessment found the largest water market in northern Victoria was working effectively, however it needs to continue to develop to match changing demand. There has been significant change in the southern Murray-Darling Basin due to climate change, water recovered under the Basin Plan to protect the health of our rivers, and emerging water market participants like investors and brokers. The water market is now central to meeting the water needs of irrigated agriculture. The volume of water traded has increased, indicating greater understanding of, and confidence in, the market. The Victorian Government will ensure we continue to have sound market settings and is carefully managing the impacts of water movement on existing users and the environment.

This year the government will release new and more open information on the Victorian Water Register website to help people better understand trade rules and how the market works and will continue to improve confidence in Victoria's already robust compliance and enforcement system through improved transparency. We will also work with Traditional Owners to improve knowledge about their values and uses for water and provide clear information for their participation in the water market, as well as working with other groups on their cultural and social values and uses for water.

This review gives me confidence the water market is currently working as it should. However, the Government will continue to monitor the market and change settings when and where necessary to meet the needs of water users who are increasingly reliant on it, including to support the value of Victoria's irrigated agriculture. The farming landscape is constantly changing and by ensuring our water markets continue to be effective, farmers and their communities will have the flexibility to adapt to these changes.

I thank the many irrigators, urban and rural water corporation staff, water resource managers, industry representatives, environmental water managers and Traditional Owner representatives who made valuable contributions to this report. I look forward to continuing to work with them so that our government's prioritisation of market development and reporting effort meets the needs of all water users and the broader interests of the Victorian community.



The Hon. Lisa Neville
Minister for Water

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1. Introduction

The Victorian Government wants to make sure our water markets are working effectively so that water users and their communities have the flexibility to respond to changes in climate and other external factors like reduced water availability, increased demands for water and changes in commodity prices.

Victoria has the most comprehensive Water Register in the southern Murray-Darling Basin supporting the operation of our water markets. The Register is acknowledged as the national leader in reforming the registration and trade of water entitlements.

In 2017 the Victorian Government commissioned the first statewide review of the effectiveness of the Victorian water market. By acting on the findings from this review Victoria will continue to lead in the active development and monitoring of water markets to make sure that they work efficiently, with effective governance frameworks and trading rules in place to protect existing entitlement holders and the environment.

The report on the 2017 review *Effectiveness of Victoria's Water Markets* (2018) was prepared by Aither in collaboration with the Department of Environment, Land, Water and Planning (DELWP) and stakeholders including:

- Water resource managers and State and Commonwealth policy commentators (like the Productivity Commission)
- Urban and rural water corporations
- Environmental water managers
- Traditional Owner representatives
- Various industry representatives, and
- Individual irrigators.

DELWP thanks all stakeholders for their valuable contributions.

The report explains the framework used for assessment, the review's outcomes and recommendations for improving Victoria's water markets.

It covers all Victorian water markets:

- The northern regulated surface water, or northern market
- The southern regulated surface water, or southern market
- The western regulated surface, or western water market
- Unregulated surface water markets, and
- Groundwater markets.

The report comments on potential development of the south-central regulated surface water market, which includes Melbourne and other urban areas and is closely linked to the southern market dominated by irrigation. This is an example of how Victoria's water grid may provide opportunity to connect regulated surface water markets. Effective water markets can help make the case for efficient investment in infrastructure by establishing the value of water across connected systems.

This document summarises the findings from the 2017 review and the next steps the Department will take to act on the recommendations.

2. Statewide findings

The review found that overall Victorian water markets provide an equitable and efficient way to access and share our finite water resources. It found many examples of water consumers using markets to respond to changes in climate, agricultural production or environmental water demands. Economic and environmental values are fairly well-incorporated in the value of water across Victoria, but there is a need for better information on potential new participants in the market, like Traditional Owners, to improve understanding and recognition of their cultural and social values for water. There is also a need to provide new participants with clear information about how the water market works.

Water markets in Victoria are now under more pressure to efficiently distribute water between uses and users, as climate change and changing demands impact on our water supplies. This means water market frameworks and information must continue to develop to match the level of demand and sophistication in the market.

The 2017 review of water market effectiveness identified opportunities to modernise market frameworks and improve information to better meet the needs of today's more advanced participants.

3. Statewide actions

Actions recommended across the state focus on making sure market arrangements are current, to either incorporate new knowledge or technology or match growing demand.

Some actions are common across all markets, but in the less developed markets they focus on strengthening the building blocks for markets, like including up to date resource understanding to set groundwater caps where appropriate. In the more developed markets, actions focus on managing growing demand and sophistication, like improving information or monitoring the potential for anti-competitive behaviour.

3.1. Modernising compliance frameworks

Victoria has a robust compliance and enforcement structure to support the management of our water resources. This is to protect existing entitlement holders and the environment from the illegal take and use of water. The review found that compliance with individual entitlements appeared to be well-monitored by rural water corporations and there was no evidence of major non-compliance. However, there are opportunities to modernise Victoria's compliance regime as identified in *Water for Victoria* action 8.5.

Since the water plan was published:

- Victoria is reviewing the compliance and enforcement regime in the *Water Act 1989* to reflect best practice regulation.
- Water corporations' Statement of Obligations now require them to annually report to DELWP on their various compliance and enforcement activities. Consolidated and recently updated information is available on the Department's website at www.water.vic.gov.au.

Further actions to modernise Victoria's water resource compliance arrangements will include:

- Working with water corporations to develop a consistent, risk-based approach to manage compliance and enforcement with improved oversight and reporting.
- Assisting water corporations to make better use of the existing strengths of the Victorian Water Register to improve monitoring and reporting of compliance with individual entitlements.
- Expanding the Water Register's existing capacity to strengthen DELWP's ability to monitor and report on water corporation compliance with bulk entitlements.

3.2. Improving public water market information

The review found that public water market information and communications can be improved across Victoria. It is important for water users to have a clear understanding of the value or price of water and its trends and drivers so they can be confident when making decisions and dealing with intermediaries, including water brokers. Government has a role in providing simple, understandable, easy to access and trusted information on water price, ownership, use and availability and water trade rules and processes. Detailed information about market trends can also support market communications tailored to particular audiences or sectors by private enterprise.

The information available on Victoria's Water Register is recognised as the leading water market data in the southern Murray-Darling Basin. Information recently added to www.waterregister.vic.gov.au includes:

- A report on the evolution of surface water markets in northern Victoria (Aither, 2016)
- A report on trends in groundwater trade (Aither, 2017)

This information supplements annual trade reports and the release of the *Trends in Northern Victorian Water Trade* report (Victorian Government, 2016a).

Recommendations from the 2017 review of water market effectiveness and findings from a recent analysis of users' needs are being used to develop clearer information to help people understand market trends and trade rules. This improved information will be released on the Water Register website in 2018.

The government will also work with Traditional Owners to improve knowledge about their values and uses for water and provide clear information for their participation in the water market, as well as working with other groups on their cultural and social values and uses for water.

3.3. Improving water market monitoring to inform policy

Increased pressure on water supplies and changing demands for water in recent years mean that water markets are now operating in a very different environment. It is more important than ever that the government is vigilant in monitoring water markets and understanding trends so that:

- Participants have the right information to make informed decisions about market opportunities and risks, such as different ways to access water through the market or about the level of competition.
- Policy makers have the right information to understand the current issues and to design suitable responses.

Change can be rapid and involve movement of large volumes of water in the state's largest market in northern Victoria. In 2018 the government will review its current market monitoring approach in the north to make sure the right information is being collected and reported to correctly inform the public and policy development.

Actions in 2018 will support work already done to understand northern market trends (Victorian government, 2016a, TCA, 2017). The Basin Plan has reduced the amount of water available for use by over 20% from 2008 to 2016 in the southern connected Murray-Darling Basin. Farmers using water in northern Victoria have had to adapt to climate change, a decline in water available for irrigation, more price variability and increasing demand for high-reliability water shares from outside of the Goulburn Murray Irrigation District. By using the water market to access water in different ways, many irrigators have been able to remain on their land and in their communities. Victoria's consistent aim with the Basin Plan has been to get the best outcomes for the environment with the least impact on productive water, by designing programs that recover water in a way that minimises social and economic impacts. But the full social and economic impacts of water recovery are unlikely to be understood until more time has passed and Victoria has experienced another drought.

It is important water markets work as effectively as possible to help people adjust to declining water availability and changing demand. It is also important that the government continue to work to improve the attractiveness of irrigation districts for investment. Districts remain an efficient way to deliver water and an important part of northern Victorian irrigation communities. *Water for Victoria* committed the government to ensuring that that district water delivery and pricing frameworks are effective and sustainable. Work to ensure the effectiveness of these supporting frameworks will complement and support the government's work to improve water resource markets.

3.4. Improving monitoring of anti-competitive behaviour potential and communication of current regulations

In more developed markets like the north there are more participants, including investors and water brokers offering a growing range of different services.

Since the Basin Plan water recovery, environmental water holders now hold more than a quarter of high-reliability entitlement in the north. Concerns have been raised about how these and other large water holders like urban water corporations interact in the market.

The 2017 market effectiveness review found there were generally sound arrangements and disclosure practices for government agencies involved in the market, and their trading strategies were published. There was no evidence to suggest any major examples of anti-competitive behaviour and there had been few official complaints.

But the review identified an opportunity to improve understanding of whether water brokers and new entrants to the water market - including investors whose current holdings are much less than environmental water holders'- were having any negative effect on competition.

In 2018, as part of its review of current market monitoring approaches in the north, the government will improve tools for monitoring potential anti-competitive behaviour. This includes making sure that the right information is collected to understand how the distribution of water ownership and use is changing, how trade opportunities are being accessed and whether prices are responding predictably to supply and demand.

The government will work to strengthen confidence in current regulatory frameworks dealing with anti-competitive practices by:

- Improving application and communication of the audit of water brokers' use of the Victorian Water Register online trading system;
- Working with other states and agencies to improve communication of existing national fair trading legislation which governs the conduct of market participants and water brokers;
- Promoting the Australian Competition and Consumer Commission's 'know your fair trading rights' guides for people using water brokers and water exchanges;
- Working with water corporations to better collect and monitor complaints against intermediaries;
- Working with intermediary industry representatives to improve existing industry codes of conduct; and,
- Better communication of governance arrangements for government agencies acting as market participants and strengthening protocols within government for managing sensitive market information.

Improved and more open water market information will also protect against anti-competitive behavior.

3.5. Improving clarity in roles, responsibilities and review processes

As identified in chapter 8 of *Water for Victoria*, the 2017 review of market effectiveness found opportunities to improve confidence in Victoria's already robust water resource planning and governance

frameworks through streamlining and improving transparency and alignment. Opportunities include better aligning and clarifying interactions between regional and statewide water resource planning and where appropriate strengthening separation between water resource and market management functions. As identified in the water plan, the government will be seeking amendments to legislation to better align and streamline review and planning processes and is continuing to improve information on interactions between water resource management and planning functions.

3.6. Ensuring the Water Register remains contemporary

The review highlighted the Victorian Water Register's vital support for the operation of the water market. The government will continue to make sure the Register remains sound and up to date and transactions are fast and affordable.

4. Additional market-by-market findings and actions

4.1. Northern regulated surface water market

The northern regulated surface water market is the most developed with the highest level of demand. In 2016-17, 2,726 GL of water allocation was traded in the north (Victorian Government, 2018). The review recommends that improvements focus on how to best manage growing demands and sophistication in the market.

As well as carrying out the actions outlined in section 3, the government will:

- Work with other states and the Murray-Basin Authority to make sure:
  - Southern Murray-Darling Basin water trade rules stay up to date and adequately manage the impacts of water moving to different locations on the environment and the reliability of existing entitlements; and,
  - Delivery constraints, like the Barmah Choke, are well-managed.
- Produce timely and accessible water market information to help participants make informed decisions by understanding market opportunities and risks. This will include clear communications on how water availability and delivery are managed.

4.2. Southern regulated surface water market

The review assessed water markets within the southern regulated surface water irrigation systems and found they operate like those in the north and that there were similar opportunities to improve information and communications. The review also discussed areas to consider to inform south-central market development as an important first step in progressing action 9.5 in *Water for Victoria*. This work on future south-central market development will start by producing guidelines for how to trade under current arrangements.

4.3. Western regulated surface water market

The review found that the relatively small development of the western regulated surface water market may reflect historically low levels of demand for trade. Any further improvements need to be considered in the light of current and future demand for trade. In the near future the government will work to improve guidance on how to trade under current arrangements, and then work to understand demand for trade and current issues and opportunities in the western market over the longer term.

4.4. Unregulated surface water markets

The review found that unregulated surface water markets were generally operating at a reasonable level consistent with demand, but there is room to engage directly with users to improve awareness of opportunities for trade. The government will work with water corporations to communicate more about

how to trade under current processes and will consider if there is a need for further supporting reforms to entitlement or planning frameworks.

4.5. Groundwater markets

The review found that groundwater markets were generally operating at a reasonable level to meet demand, but there is likely to be greater demand than in unregulated surface water markets. There are also issues from overlap and misalignment between groundwater caps and planning arrangements, for example with transition to the Basin Plan sustainable diversion limits.

In the short term the government will make sure there is statewide alignment in the principles for setting caps and then will look at whether there is a need for further supporting reforms to entitlement or planning frameworks. The government will also work with water corporations to improve local awareness of how to trade under the current system.

5. Future reviews

This first review of water market effectiveness has established an assessment framework which can be used to monitor water markets into the future and these actions will support continued oversight of our water markets.

The review recommends repeating the 2017 assessment at three to five yearly intervals. The next review will be undertaken in 2022 which will allow the assessment to consider the outcomes of many of the actions from *Water for Victoria*.

The findings note that the contributions from water market participants and stakeholders have been essential to this review. The government intends to widen stakeholder participation in the next review and this may involve work with water corporations to collect more survey information.

The assessment framework may also be broadened in future to incorporate other aspects of the structure to support management of Victoria's water. It could also be applied in particular systems within Victoria or more broadly across the southern Murray-Darling Basin.

6. References

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