

# **Response to Productivity Commission**

## **Inquiry into Government**

### **Drought Support**

#### **080822**

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## **Introduction**

NSW Irrigators' Council (NSWIC) represents more than 12,000 irrigation farmers across NSW. These irrigators are on regulated, unregulated and groundwater systems. Our members include valley water user associations, food and fibre groups, irrigation corporations and commodity groups from the rice, cotton, dairy and horticultural industries.

In responding to the Productivity Commission, NSWIC is responding with the views of its members. However each member reserves the right to make independent submissions on issues that directly relate to their areas of operation, or expertise, or any other issues that they may deem relevant.

## **Introductory Comments**

Whilst irrigated agriculture is a sector of agriculture as a whole and is certainly not immune from the threats and opportunities that agriculture faces, it is an entirely different sector to dry land farming. Irrigated agriculture is characterised by significant investment in infrastructure aside from land.

To date, drought support measures have not recognised this distinct difference.

Irrigated agriculture, by its very nature, attempts to overcome the cyclical nature of agriculture with respect to weather patterns. Irrigators rely on stored water, be that from rivers (regulated or otherwise), groundwater aquifers or on farm storages, rather than rainfall. As a result, irrigators are far more self-reliant in respect of short term droughts.

When longer term drought occurs, such as is the case at the moment, and there is no availability of stored water, irrigators suffer a crushing blow. Water is our primary asset. Without it, we have no opportunity to create revenue. At the same time, the costs of servicing and maintaining our infrastructure does not decrease.

For this reason, NSWIC submits that a drought support policy tailored specifically for irrigated agriculture is appropriate and should be recommended by the Productivity Commission.

## **Responses to Paper**

### **Section 1**

NSWIC supports the Terms of Reference of this Inquiry, particularly the fact that it will consider both State and Commonwealth Government programmes. As a cross border market for water develops, it is inappropriate that levels of government support across states is not at least moving toward equivalency.

Irrigated agriculture, as noted in our introductory comments, by its very nature approaches self-reliance in all but the worst drought scenarios.

### **Section 2**

NSWIC recognises the data presented by the BOM, the CSIRO and other climate change scientists.

Whilst we recognise that prolonged droughts may occur more frequently, we equally note that more severe weather events are likely to occur. The impact on irrigated agriculture is likely to be less severe than on dry land agriculture provided that the severe events occur in catchment areas and the water is properly managed.

### Section 3

NSWIC recognises the distinction between “normal” and “severe” drought. To a great extent, irrigated agriculture is self-reliant in terms of normal drought as it relies on stored water rather than rainfall events.

At the same time, irrigated agriculture is impacted dramatically during extended (severe) drought when allocations plunge rapidly. In current circumstances, irrigators on the NSW Murray River with General Security entitlement are facing a third consecutive year of zero allocations. That is, three years without water. Given the critical nature of water as an input, this means three years without revenue.

The nature of irrigated agriculture and the clear indicator of water availability ought make it far simpler to determine what is an exceptional circumstance for the sector. Pursuant to our earlier comment, a separately defined drought support policy for irrigated agriculture is not only warranted, but will be far simpler to operate.

NSWIC notes the three key objectives of National Drought Policy (NDP):

- Encourage adoption of self-reliant approaches for managing climatic variability;
- Maintain and protect agricultural and environmental resource bases; and
- Ensure early recovery consistent with long term sustainable levels.

The first two of these points are dealt with elsewhere in this submission. It is the third that NSWIC wishes to draw particular attention to.

As noted earlier, irrigated agriculture is characterised by significant levels of infrastructure, be that in the form of drip irrigation, overhead irrigation, lateral move, centre pivot, sub-surface and/or delivery channels and land forming. This major asset base must not only be maintained, but in many instances financed regardless of its income producing capacity based on water availability.

In the event that the cash flow of irrigators is drawn on to the extent that they are unable to maintain these assets, their capacity to quickly recover is seriously undermined. In this context, NSWIC wishes to draw attention to the situation of fixed charges in NSW.

Irrigators pay to both the State Water Corporation and the NSW Department of Water and Energy a two part tariff – a variable charge (based on water consumed in a given year) and a fixed charge (based on the entitlement held). In years where no water is delivered, the fixed charge must still be met. NSWIC does not disagree with a two part pricing approach, but has called upon the NSW Government to provide relief from the fixed charge in times of severe drought where there are multiple years of extremely low allocation.

It is an appalling irony that whilst NDP encourages a capacity for early recovery, the State of NSW is removing that capacity by placing demands on cashflow.

**NSWIC submits that relief from fixed charges is a vital component of drought support for irrigated agriculture that the PC must consider.**

A policy in this respect has been prepared and advocated by NSWIC. It appears as an annexure to this submission.

NSWIC notes that the majority of EC funds (63% in 06/07) are committed to interest rate subsidies. NSWIC supports the continuation of interest rate subsidies for irrigated agriculture in severe drought circumstances (howsoever defined) on the basis that the sector is heavily reliant on significant investment on infrastructure which must be financed.

#### **Section 4**

NSWIC supports the PC in its recognition of economic, social and environmental reasons for drought support.

*Which are the more important rationales for government intervention during severe drought? Are these the same rationales for intervention in other severe events?*

NSWIC fails to understand why a ranking in importance is relevant. Each is equally important in our submission.

*What is your understanding of the meanings of preparedness and self-reliance?*

Irrigated agriculture is well equipped to deal with climate variability and short-term drought as per previous sections.

Relief for irrigated agriculture should be targeted at expense assistance in times of multiple years or negligible revenue.

#### **Section 5**

NSWIC recognises that the 1989 review of drought support directed a movement away from business related relief payments to education and training and increased funding for drought related R&D projects.

*What have been the lessons learned from the last drought and what strategies are farmers now adopting in response to those lessons?*

“The last drought” is an inappropriate description given its continuation. NSWIC assumes that the PC means “the current drought”.

The growing maturity of the water market will provide irrigators the opportunity in years of minimal allocations (that is, above zero but still low) to make choices in respect of asset management. Rather than grow a small crop as a result of low allocations – potentially not providing a marginal return – irrigators may choose to sell their allocation (“temporary trade”) to a higher value user to

create cash flow. This type of activity will continue to grow as derivatives develop in the water market. At the same time, irrigators who must have water annually (such as those with permanent plantings) will be able to access the market. Government must recognise that the market will naturally result in scarcity pricing, resulting in dramatically increased costs for irrigators who must access water annually.

Irrigators continue to be at the forefront of water conserving farming techniques. It is, however, an expensive undertaking that requires significant capital investment. The current environment for investment – both physical and political – limits the willingness of irrigators to move fully toward such investment.

Revenue for irrigated agriculture naturally moves with the availability of its key input – water. In dry years, revenue is dramatically limited. In wet years, significant revenue can be gained. As a result, tools such as Farm Management Deposits are vital financial management requirements.

*What are the impediments to individual farmers, farm businesses, farm dependent rural small businesses and rural communities becoming sufficiently self reliant to withstand drought events?*

The central consideration is the prolonged nature of drought. Multiple years of zero water allocation represent an unmanageable risk. Put simply, irrigators can maintain cashflow for a period but cannot last for multiple years. Assistance with expenses is vital – particularly those expenses levied upon irrigators by government or government controlled entities.

There remain in place significant impediments to the water market. Whilst the ACCC, at the request of the Minister, is assessing impediments in the private sector (particularly amongst infrastructure operators), very little consideration is given to the fact that the vast majority of impediments are caused by government. The ACCC seems unable (or unwilling) to deal with these impediments. They must be dealt with directly by government – and a recommendation to do so from the PC would be welcomed by NSWIC. The impediments are effectively twofold:

1. Delay in processing trades

Trades require the approval of state government entities. Whilst the ACCC position is to impose a 3 day limit on irrigation infrastructure operators (such as irrigation corporations) for approval of trades that same limit is not imposed on government departments. NSWIC is aware of some state government departments taking over 100 days to process a *temporary* transfer of water. This is clearly unacceptable and is a major barrier to the market assisting irrigated agriculture further toward self reliance.

2. State legislation

One state in particular has moved to prevent water moving out of it. Victoria has imposed a legislative barrier to water being owned by entities that do not own productive land in that state. A maximum of 10% of Victorian entitlements can be owned by such entities. This is clearly an unacceptable barrier to the market assisting irrigated agriculture across state borders further toward self reliance.

Government has a role in encouraging irrigators to invest in water efficiency infrastructure. NSWIC supports the investment plan in the Water for the Future package. At the same time, we encourage governments – both state and federal – to recognise that an uncertain policy environment does not provide encouragement to engage in major infrastructure investment.

## **Section 6 – Are assistance measures effective and efficient in severe drought?**

“Policy design is important in efficiently targeting groups which are the focus of government intervention.”

NSWIC submits that drought support policy for irrigated agriculture must be targeted specifically at irrigated agriculture.

*In general, do current drought support programs provide an incentive for farmers, farm businesses and farm dependent rural small business to become more self reliant and adopt strategies that better prepare them for instances of severe drought? Do they do the opposite?*

This question lies at the classical heart of any government transfer payment – is it a “net” or a “trampoline”?

A feature of irrigated agriculture is its reliance on infrastructure – large and expensive infrastructure that cannot be diverted to alternate use. The cost of maintenance and ongoing finance of these assets is significant. The ability to use that infrastructure again once drought events conclude with minimal further expense is crucial to the sustainability of an irrigated agricultural undertaking. As a result, interest subsidies are crucial in this respect.

The ability to average earnings in respect of taxation and the existence of Farm Management Deposits allows irrigators to ensure sufficient cashflow to meet ordinary operating expenses in the event of drought. It enables them to preserve the enterprise to be ready to operate again when water is available.

*To what extent do drought support policies prevent the development of market responses to manage drought risk? For example, have drought policies impeded the development of weather insurance or other weather derivative markets?*

NSWIC is not aware of any weather insurance or derivative products, but is clearly heavily engaged in water market policy.

The water market – and derivatives in that market – will potentially deliver a significant self-reliance tool in the medium to longer term. Perhaps the greatest threat to that market, however, is government policy.

The basis of any market is the security of the property right that is being traded. Whilst political bodies continue to canvass the possibility of compulsory acquisition of water entitlements, they effectively undermine the efficient operation of the market, the possibility of further self-reliance and the future of irrigated agriculture. NSWIC recognises that the Commonwealth *Water Act 2007* rules out compulsory acquisition and acknowledges that Federal Minister Wong has stated that it is “off the agenda”, but is greatly concerned that other political bodies continue to gain political points in respect of the matter.

The other significant threat to the market is the dominance of one player – the Commonwealth Government. The Water for the Future package targets \$3.2 billion at the purchase of water entitlement – significantly more than has been traded in the entire market in the past. Government policy must ensure that other players are able to successfully operate in the market. One way of achieving this is for the Commonwealth to take steps to identify its actions. That is, it must disclose that it is the purchaser prior to the purchase being completed.

*Is the EC declaration process overly complex, long, non-transparent and open to manipulation?*

NSWIC refers to its earlier submission with respect to the significant difference between irrigated and dry land agriculture. As well as demanding different policy approaches, the declaration of EC in irrigated agriculture should be far simpler – and should be based on the level of announced allocation with certain defined trigger points for varying assistance measures.

*Do the geographical boundaries used in the EC declaration process unfairly exclude some farmers from relief payments or conversely include some that do not need assistance? Does and EC declaration influence behaviour, for example, does the potential for declaration delay the decision to adopt preparedness strategies?*

NSWIC refers to its earlier submission with respect to the differences between dry land and irrigated agriculture. Adopting a trigger specifically for irrigated agriculture would be dramatically simpler than the current approach given the regional nature of available water declarations. That is, the boundaries for inclusion and exclusion could simply be defined on the area in which a water entitlement is held.

EC declarations do not affect the decision to adopt preparedness strategies in irrigated agriculture. The value of the support is inconsequential in terms of the overall operations of the business and, in particular, the value of the primary asset – water.

*Is a trigger approach, such as EC declaration, a necessary first step to determine individual eligibility for drought relief? Could assistance be delivered on the basis of individual circumstances without an EC declaration? What administrative efficiency issues does this raise?*

This question highlights the submission of NSWIC that irrigated agriculture both can and should be treated separately from dry land agriculture. Exceptional circumstances in terms of our sector are much simpler to define – announced water allocations – and support both should and could be based on that trigger rather than the more subjective and ill-defined declaration process that currently exists.

*How effective have EC interest rate subsidies been in improving the survival of farm businesses and farm dependent rural small businesses? How are farm business decisions altered by EC interest rate subsidies? Do the current eligibility requirements create adverse outcomes, for example, by creating a disincentive for farming households to seek off-farm income? Would support based on business attributes other than debt be more effective?*

EC interest rate subsidies have been vital to the survival of a significant number of irrigated agriculture enterprises, but have been of little assistance to those that have invested in off-farm assets or income streams to protect their overall position.

At a time when both government policy and climatic circumstances are directing irrigators to invest heavily in water efficiency infrastructure, it is appropriate that a clear signal on the future of interest rate subsidies be provided.

NSWIC submits that interest rate subsidies should be maintained in exceptional circumstances, with the exceptional circumstances being determined specific to irrigated agriculture. This measure will encourage irrigators to maintain and increase investment in infrastructure, knowing that their business will be protected to a certain extent if that infrastructure cannot be used in exceptional circumstances. To aid this, the level of allowable off-farm assets and income must be increased. Failing to do so allows the perverse outcome of farmers not investing off-farm to provide protection for their overall business in dry years. For the same reason, off farm income limits should be increased.

*To what extent have farmers benefitted from other input (fodder, transport, rates and other transaction based) subsidies? Have the benefits gone to farmers or to others in the marketing chain, including financiers and farm input*

*suppliers? Do such subsidies encourage poor farm management practices, such as maintaining excessive stocking levels?*

This question again underlines the NSWIC submission that irrigated agriculture must be treated separately to dry land grazing. Fodder and transport subsidies are of limited assistance to irrigators, other than those irrigating for dairy production.

*What role do farm financial counsellors play in guiding farm business decision making prior to, during and following drought? How effective is their advice compared to that from other sources?*

This is a question for individual farmers to answer based on the quality of their individual counsellor.

NSWIC submits, however, that farmers – and irrigators in particular – must be given more recognition by governments for their own ability to manage finances. Government has a tendency to not recognise that farms are businesses – and irrigated agriculture in particular can tend toward sizeable businesses. Continued offers of counselling support may be of limited assistance.

*Should governments have structural adjustment policies which are triggered by severe drought? Why is there little use of current exit programs? Do severe droughts lead to an increase in exit from the industry? If not, why not?*

This question reflects an attitude that NSWIC perceives across many government entities – a lack of understanding that many farmers simply want to keep farming.

The first question can only be answered by a question – it depends entirely on what governments are trying to achieve. If they wish a smaller agricultural sector, a smaller export base and less regional community, then by all means embark on an expanded “structural adjustment” course. NSWIC submits that none of these outcomes is desirable for Australia.

NSWIC submits that exit from irrigated agriculture may occur in coming months due to government involvement in the market and a general impression amongst irrigators that they cannot compete with the government.

To answer the final question, NSWIC refers to its first answer – farmers want to keep farming. They don’t all want to be “retrained”, to move to cities or to work in mines.

*If governments want to maintain rural communities, what are the most transparent, effective and efficient policies? What are the effects of incorporating these policies in measures directed to the preparedness for, management of and recovery from, severe drought?*

NSWIC applauds the PC for recognising that agriculture is the basis of regional communities. Without agriculture, regional communities would face enormous challenges and in many instances would disappear. In NSW, significant towns – such as Moree, Griffith, Deniliquin and Wentworth – rely almost entirely on irrigated agriculture. Removing or seriously downgrading the level of irrigated agriculture would have devastating affect. As specific examples, consider:

- (a) The closure of processing and storage facilities for commodities, together with associated employment losses;
- (b) The economic consequences of under-utilisation of plant and equipment;
- (c) The loss of intellectual capital as research scientists, engineers and the like are forced to move away from regional areas; and
- (d) Highly skilled machinery service personnel are forced to move away – often to mines – and are unlikely to return, erecting an enormous barrier to speedy recovery;

In a broader context, these effects are felt as declining regional populations with flow on effects such as:

- (a) Reduction in numbers in schools with a consequent fall in standards;
- (b) Local government revenue decreases with a consequent fall in ability to provide and maintain infrastructure; and
- (c) The potential collapse of entire towns and/or regions.

We further support the PC for noting that government support during drought is akin to economic support in urban centres during economic downturn.

Whilst recognising that “such expenditures do not usually take the form of grants to individual private businesses”, NSWIC does point to the numerous government grants provided to industries that provide employment, particularly in manufacturing. In any event, the nature of the support that agriculture provides in economic terms to the community that relies on it is such that only direct transfers to private businesses will be effective.

*How effective are drought relief payments in providing a safety net for farming families? Are the eligibility tests for farm family assistance suitable?*

NSWIC submits that a safety net is as important for agricultural communities as it is for any other sector of Australian society, but makes no further submission specific to drought relief payments.

*What have been the farm family welfare outcomes from the EC Relief payment? Are they satisfactory and at the level expected? For example, have farm families been able to meet their immediate health and education requirements? If not, what are some of the problems yet to be addressed in this area?*

Whilst NSWIC makes no specific submission in respect of this question, we do again draw attention to the cash flow situation of irrigators in exceptional circumstances. When faced with a range of bills and limited reserves with which to meet them, it seems absurd that no relief is available for government imposed fixed charges.

*To what extent, if any, are payments diverted to the farming business and is this a matter for policy concern.*

Refer to the above.

*What is the role for government in providing social security-type payments to self-employed farmers and rural contractors/businesses during times of drought? Who should be eligible and in what form should payments be made? Should payments be drought dependent or instead based on individual circumstances? Should equity in assets be run down to some minimal level before households are eligible?*

Rural Australia should expect a similar safety net to that afforded to urban Australia. The safety net should be extended to farming families who are technically self-employed. Further than this, NSWIC makes no submission.

*How can the environmental consequences of severe drought be minimised while providing assistance to farmers? Do current government support measures change these consequences in either a positive or negative way?*

NSWIC recognises that environmental consequences are primarily as a result of stock, which limits the involvement of irrigators.

*What role do FMDs play in helping farmers prepare for severe drought events? Is there evidence that FMDs are substantially drawn down during a drought? If not, what other "needs" are FMD's fulfilling and is this an intended policy outcome? Do the eligibility criteria of the separate relief payments encourage or discourage the use of FMD's?*

FMDs play two roles – to assist farmers to operate through times of drought and, just as importantly, to quickly recover from drought. To expect FMDs to be fully drawn prior to providing EC relief defeats the second role entirely.

NSWIC supports the continued existence of FMDs as a way of shielding agriculture and its input to the Australian economy not only from environmental shocks (including drought), but from economic shocks (commodity prices) and policy shocks.

*How has the implementation of drought support policies affected their accessibility and usefulness? Are there impediments to accessing support arrangements? Could support arrangements be delivered in a more efficient manner? For example, are the government institutions responsible for delivery of business and welfare assistance the most appropriate organisations and do state differences add to compliance costs?*

NSWIC supports drought relief delivered in the simplest terms and form possible and asks the PC to identify how this might be achieved. We reiterate our call for EC in irrigated agriculture to be separated from dry land farming.

*What is the time taken and cost incurred by farmers and farm businesses to prepare the necessary documentation and how long does it take to process these applications once submitted?*

This is a question for individual farmers.

*Should there be a uniform national approach to drought policy?*

Yes, to the extent that the problem at which the relief is targeted is national in nature. For example, interest rates subsidies are national in nature as there are no state-specific rates. Fixed charges relief, however, cannot be uniform as the charges are not uniform.

## **Section 7 – What are the alternatives?**

### *Income Contingent Loans*

NSWIC is cautious about this alternative, noting that it potentially provides a competitive advantage to one irrigators over another in the event that both need to access the water market.

### *Tax Reform*

NSWIC supports the extension of FMD arrangements to relax deposit restrictions and off-farm income.

### *Insurance and derivatives*

Irrigated agriculture in Australia is confined to certain regions. The vast majority is contained within the Murray Darling Basin. As a result, the opportunity for insurers to spread risk is extremely limited. NSWIC submits that the development of drought insurance products is highly unlikely for irrigated agriculture.

*Choice of assistance options*

NSWIC is concerned at the academic nature of discussions with respect to farm viability. Farm viability is not simply a measure of the assets that the farm business possesses, but the people that manage and/or operate the farm business. What might be a non-viable business for one manager might well be a viable proposition for another. NSWIC urges caution in this respect.

NSWIC needs to see further information on assistance options programs prior to making further comment.

*Are there alternatives to the current drought support policy measures that could meet the objectives of the NDP in a more effective and efficient manner, particularly in the face of significant long term climate change? What are the advantages and disadvantages of these alternative approaches?*

Throughout this submission, NSWIC has noted that irrigated agriculture differs significantly from dry land farming. We repeat our submission that a separate package of drought support measures based on separate criteria must be established for this sector.



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# Fixed Charges Relief Proposal December 2007

### Executive Summary:

- **NSW Irrigators Council seeks relief from the payment of fixed charges in extraordinary circumstances.**
- **The threshold for extraordinary circumstances should be two consecutive years of one-in-twenty-year events.**
- **If that threshold is met, government should make the fixed charges payment on behalf of irrigators.**

### Objective:

To establish the principles that would apply to trigger support from the NSW Government for irrigated agriculture during times of extreme hardship.

### Background:

Both State Water and the Department of Water and Energy levy fixed charges against water entitlements.

Fixed charges, in large part, pay for the essential maintenance of delivery infrastructure.

NSW Irrigators Council does not disagree with the levying of fixed charges.

In times of extreme hardship, however, fixed charges are a significant impost to survival. When, for a significant period, irrigators are not able to receive the benefit of the infrastructure, the payment for its maintenance should be viewed as a public service obligation to government.

In recent years, the NSW government has assisted with payment of fixed charges for irrigators in the Lachlan region. A recent Federal Government assistance package for irrigators in the Murray Darling Basin has provided a "one off" support mechanism for irrigators. Subsequent to heavy lobbying by NSWIC, this grant can be used in certain circumstances to assist with the payment of fixed charges.

The response by Governments has been a reaction to specific circumstances rather than part of a consistent policy framework to support irrigated agriculture.

Irrigators respond to drought by reducing their own operating costs. The current water pricing system requires license holders to bear the costs of running the rivers to provide water for non-paying beneficiaries, such as basic rights holders, the environment and recreational users. The relative cost of meeting this obligation rises steeply under severe drought conditions when most of the flow in the river is to meet these obligations and very little is available for license holders. In extreme

circumstances, this cost should be treated as a public service obligation for government and hence funded by Treasury.

**Proposal:**

NSWIC proposes establishing a trigger for drought relief for irrigated agriculture, based on objective indicators of the impact of drought on the irrigation sector, which can be applied to each river.

Meeting the drought threshold trigger would result in fixed charges being paid by government on behalf of irrigators.

**Trigger:**

River systems across NSW have a range of expected reliabilities. Any potential trigger for drought relief must accommodate this range, whilst distinguishing between an extraordinary drought that merits relief and the normal climatic variability that irrigators can (and should) handle through their own risk management strategies.

NSWIC recommends a drought relief trigger which is based on identifying circumstances that rarely occur. That is, support should only be expected when an event that is a remote possibility occurs.

*NSWIC recommends that the trigger be two consecutive years of 1 in 20 year low announced Available Water Determinations (AWD's).*

There are a range of indicators that could be used to indicate an exceptional drought. Water allocation reliability (yield) is recommended as the primary indicator because it is a direct and objective reflection of the impact of drought on irrigated agriculture.

The trigger would be defined as when water allocation or cumulative AWD as at 31 October in any year is within the lowest 5% of historical allocations for that valley for two consecutive years.

Meeting the trigger would result in fixed charges for that licence category being paid by government and possibly other relief measures appropriate to that valley.

The Government may apply some eligibility criteria to ensure that the assistance is targeted at those producers who earn the majority of their income from primary production.