

Audit of strategic water purchases

Submission to Joint Committee of Public Accounts and Audit

The Australian National Audit Office (ANAO) report on strategic water purchases found that the Department of Agriculture and Water Resources' processes were poor, could not ensure value for money or that conflicts of interest were eliminated. Despite these findings, the audit did not ask if the public actually got value for money and real environmental benefit. The audit relies on evidence that does not meet relevant audit standards, breaching ANAO legislation.

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Summary

The Australian National Audit Office (ANAO) report into strategic water purchases found poor processes and no framework to ensure value for money or eliminate conflicts of interest. It did not, however, ask the obvious questions about the consequences of the poor process. For example:

- Did all the strategic purchases achieve value for money?
- Did all the purchases meet Commonwealth procurement guidelines?
- Were the conditions of all purchases met and met within the timeframes set out in the contractual agreements?
- Will all of the water purchased contribute to environmental goals?
- Do all of the environmental water licences purchased have appropriate legal status or statutory protection?
- Were there any actual conflicts of interest?

These questions are fundamental to the public interest and the public's trust in water recovery in the Murray Darling Basin. These questions are not answered by the ANAO's finding that the purchases "contribute to" government policy of obtaining water for the environment, or in water jargon that they contributed to 'Bridging the Gap'. The ANAO provide no evidence to support that conclusion, despite ample evidence to the contrary.

Still more problematic is the ANAO finding that prices paid were "equal to or less than the maximum price determined by valuations." This statement is demonstrably false, with examples and evidence readily available.

One reason the ANAO has produced these problematic findings and not answered key questions of public interest is the narrow scope of audit evidence used. The sources the ANAO relies on, particularly water valuation reports, do not comply with the ANAO's audit standards, particularly *Auditing Standard ASA 500: Audit Evidence*.

One example is the reliance on a valuation commissioned by the Department of Agriculture and Water Resources (the Department) for water in the Condamine-Balonne. Departmental and ANAO claims that this valuation supports the price paid have been contradicted by the report itself, which was only recently released in unredacted form. At time of writing the ANAO had not answered questions on notice relating to this issue.

Another example is valuation reports relied on to justify the Lower Darling/Baaka purchase of water rights from Tandou Station. These valuations exclude an additional \$40 million paid by the Department in this purchase. Inclusion of this \$40 million

makes the price paid far in excess of all valuations. The valuations themselves are based on various implausible or unjustified assumptions and all omit the gifting of a further water allocation for the year after the purchase, which enabled harvest of a \$35 million cotton crop. The ANAO report ignores NSW ICAC findings relating to this purchase.

Similar problems exist with the Warrego purchase, where valuation appears to be based on water in a different valley, and the Murrumbidgee purchases, where valuations were based on a different, and inferior, kind of water entitlement.

ANAO findings around 'bridging the gap' are equally problematic. The Condamine-Balonne purchase included licences not included in original baseline estimates, so cannot contribute to water recovery. The Lower Darling/Baaka purchase enabled reduced reliability of the entitlement, meaning it also cannot contribute fully to bridging the gap. The Warrego valley had no gap to bridge, as emphasised by the Commonwealth Environmental Water Holder. The purchase of Lowbidgee water entitlements also does not contribute to bridging any gap in the Murrumbidgee at the time of the purchase.

ANAO appears to have made no investigation into many potential conflicts of interest around valuations, water modelling and people involved in different aspects of these purchases.

Decommissioning works was a condition of the Condamine-Balonne purchase. The ANAO notes the paucity of documentation that the Department provided to confirm decommissioning, yet itself relies on nothing more than a Senate Estimates answer ten months after television footage showed conditions had not been met.

An interesting contrast with the audit of strategic water purchases is the Auditor-General's Leppington Triangle audit, triggered by a revaluation of \$27 million. If a similar revaluation was carried out, the strategic purchases would leave the Leppington Triangle in the shade.

The Leppington Triangle audit included interviews with external valuers. The strategic purchase audit cost taxpayers more than twice as much (almost \$700,000 compared to \$330,000) yet interviewed no one outside of the Department of Agriculture and Water Resources. The Auditor-General should reexamine each of the key strategic purchases with a similar level of rigour.

Recommendations

The Committee should require/request that the Auditor-General explain:

- Whether the following questions are answered in their audit:
 - Did all the strategic purchases achieve value for money?
 - Did all the purchases meet Commonwealth procurement guidelines?
 - Were the conditions of all purchases met and met within the timeframes set out in the contractual agreements?
 - Will all of the water purchased contribute to environmental goals?
 - Do all of the environmental water licences purchased have appropriate legal status or statutory protection?
- If not, why not and what plans the ANAO has to continue this work.
- How its finding that prices paid were below valuation maximums are consistent with the unredacted valuation by Colliers International titled *Valuation of Overland Flow licences: Condamine Balonne Water Resource Plan*.
- How the audit evidence used in relation to the Condamine-Balonne purchase, and the ANAO's efforts to understand that evidence, meet its Audit Standards.
- Whether the valuations used in the Lower Darling/Baaka purchase comply with its Audit Standards, particularly in light of the NSW ICAC report.
- Whether valuations of Lower Darling/Baaka entitlements support the prices paid in December 2019 and whether this audit can be extended to investigate these purchases.
- Why valuations of water outside the Warrego were used for this purchase and why the value of Warrego water has more than doubled to \$1,600/ML since the Department declared \$783/ML 'excessive'.
- Why Murrumbidgee supplementary valuations were used to evaluate purchase of Lowbidgee Supplementary water, and whether this approach meets ANAO audit standards.
- How it determined that all of the Condamine-Balonne overland flow licences were included in the Baseline Diversion Limit and if they can fully contribute to water recovery or 'bridging the gap'.
- How it determined the legal status of Condamine-Balonne water and ability to contribute to 'bridging the gap', and whether the sources used for this determination meet its standards for audit evidence.

- How it determined that the reliability of the Lower Darling/Baaka water purchase was not affected, whether it can contribute to 'bridging the gap' and whether the sources used in this determination meet ANAO audit standards.
- Whether it can confirm that there is no 'gap to bridge' in the Warrego, and if so, how it determined that a potential transfer to another valley would contribute to government policy on water recovery.
- Whether it can confirm that there is no 'gap to bridge' in the Lowbidgee area, and if so, how it determined that further purchases there contribute to government policy on water recovery.
- Whether it looked for actual conflicts of interest relating to the purchases from valuers, modellers and people involved in other aspects of the transactions.
- Whether it found any evidence of the Condamine-Balonne purchase conditions being met prior to March 2020 and whether the evidence relied on in the audit meets Audit Standards.

Introduction

Slattery & Johnson and The Australia Institute welcome the opportunity to make a submission to the Joint Committee of Public Accounts and Audit and its *Inquiry into Auditor-General's Reports 33, 47, 48 (2019-20) and 5 and 8 (2020-21)*. This submission relates to the Auditor-General's Report No. 2 (2020-21) Procurement of Strategic Water Entitlements (strategic purchases).

We have a particular interest in this audit because it was our research in 2018 that prompted the investigation into so-called strategic water purchases. Led by Senator Rex Patrick, a request was made for this audit in April 2018, referring to our research and signed by senators and members of parliament from across the political spectrum. Then Water Minister, David Littleproud also requested that the Auditor-General bring forward an audit of water purchases in April 2019. A response confirming that the audit would take place was sent by the Auditor-General to the senators and members in April 2019.¹ The audit was published in July 2020.

In the almost three years since the audit was requested, we have written extensively about the main strategic purchases, with our main publications listed below:

Condamine-Balonne valley

- *That's not how you haggle: Commonwealth water purchasing in the Condamine Balonne.*²
- *#Watergate's water mates: The buyers and sellers of Australia's most controversial water.*³
- *Rough Estimates: Analysis of Senate Estimates documents on Australia's most controversial water.*⁴
- *A little more valuation, a little less redaction, please: Analysis of unredacted Condamine Balonne water valuation documents.*⁵

¹ ANAO (2019) *Allegations concerning the purchases of water for environmental flows in the Murray-Darling Basin*, <https://www.anao.gov.au/work/request/allegations-concerning-the-purchases-water-environmental-flows-the-murray-darling-basin>

² Slattery & Campbell (2018) *that's not how you haggle*, <https://australiainstitute.org.au/report/thats-not-how-you-haggle/>

³ Slattery & Johnson (2019) *#Watermates*, <https://australiainstitute.org.au/report/watergates-water-mates/>

⁴ Slattery & Johnson (2020) *Rough Estimates*, <https://australiainstitute.org.au/report/rough-estimates/>

⁵ Slattery & Johnson (2020) *A little more valuation, a little less redaction please*, <https://australiainstitute.org.au/report/a-little-more-valuation-a-little-less-redaction-please/>

Lower Darling/Baaka

- *I'll have what they're having: A step-by-step guide to valuing compensation in the Lower-Darling.*⁶
- *Trickle Out Effect: Drying up money and water in the Lower Darling.*⁷

Warrego valley

- *Moving Targets: Barnaby Joyce, Warrego valley buybacks and amendments to the Murray Darling Basin Plan.*⁸

In addition, our submission to the 2020 audit included considerable detail on the Murrumbidgee purchase.⁹ Our submission and previous reports show that the main strategic purchases share similar, and undesirable, features:

- the reliability of the water is highly questionable and less than stated;
- the transaction was undertaken with minimal transparency;
- procurement via limited tender was not justified;
- key information about the transactions and valuations was withheld from the Senate;
- the price paid was excessive.

An objective of the audit was to examine whether the strategic water procurements were conducted in a manner consistent with government policy, supported by appropriate program design, were planned and executed appropriately, and achieved value for money. In our view, none of the strategic purchases are consistent with government policy. They were not supported by appropriate program design and they did not achieve value for money. As a result, we welcomed many findings of the Australian National Audit Office's (ANAO) report:

- It is not clear how the department assessed individual procurements to determine their strategic priority or considered how to encourage competition within the limited tender process.
- The department did not consistently apply approved policy, planning and guidance to the assessment of all limited tender procurements.
- The department did not consistently apply the guidelines it developed to all limited tender procurements.

⁶ Slattery & Johnson (2018) *I'll have what they're having*, <https://australiainstitute.org.au/report/ill-have-what-theyre-having/>

⁷ Slattery & Johnson (2018) *trickle Out Effect*, <https://australiainstitute.org.au/report/trickle-out-effect/>

⁸ <https://australiainstitute.org.au/report/moving-targets-barnaby-joyce-warrego-valley-buybacks-and-amendments-to-the-murray-darling-basin-plan/>

⁹ Slattery and Campbell (2019) *Strategic failure: Submission on procurement of strategic water entitlements*, <https://australiainstitute.org.au/report/strategic-failure/>

- The department did not develop a framework designed to maximise the value for money of strategic water entitlements purchased through limited tender arrangements.
- The department did not appropriately manage procurement risks. While the department identified risks associated with the broader water recovery strategy, there is limited evidence of risks being raised or managed for individual procurements.
- Conflict of interest declarations were not clearly documented.

The strategic purchases received significant public criticism that contributed to the requests for audit. Despite this controversy and the ANAO's critical findings, key questions remain unanswered:

- Did all the strategic purchases achieve value for money?
- Did all the purchases meet Commonwealth procurement guidelines?
- Were the conditions of all purchases met and met within the timeframes set out in the contractual agreements?
- Will all of the water purchased contribute to environmental goals?
- Do all of the environmental water licences purchased have appropriate legal status or statutory protection?
- Were there any actual conflicts of interest?

Recommendation: The Committee should establish with the ANAO whether these questions are answered in their audit. If not, why not and what plans the ANAO has to continue this work.

These questions are fundamental to the public interest and the public's trust in water recovery in the Murray Darling Basin. These questions are not answered by the ANAO's finding that the purchases "contribute to" government policy of obtaining water for the environment, or in water jargon that they contributed to 'Bridging the Gap'. The ANAO provides no discussion of evidence to support that conclusion, despite ample evidence to the contrary.

Still more problematic is the ANAO finding that prices paid were "equal to or less than the maximum price determined by valuations." This statement is demonstrably false, with examples and evidence readily available.

One reason the ANAO has produced these problematic findings and not answered key questions of public interest is the narrow scope of audit evidence used. In particular parts of the ANAO report rely on:

- Valuations commissioned by the Department;
- Valuations by independent experts, without obtaining an understanding of that expert's advice, or evaluating the appropriateness of that evidence;
- A desktop valuation prepared by the Department that was erroneous;

- A verbal response by a Department of the Environment officer in Senate Estimates relating to the fulfilment of contractual arrangements by the Department of Agriculture, some two years after the relevant transaction.

Without obtaining further wider audit evidence, the ANAO's report does not comply with Auditing and Assurance Standards Board *Auditing Standard ASA 500: Audit Evidence*, which states:

When designing and performing audit procedures, the auditor shall consider the relevance and reliability of the information to be used as audit evidence, including information obtained from an external information source.

If information to be used as audit evidence has been prepared using the work of a management's expert, the auditor shall, to the extent necessary, having regard to the significance of that expert's work for the auditor's purposes:

- Evaluate the competence, capabilities and objectivity of that expert;
- Obtain an understanding of the work of that expert; and
- Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.

When using information produced by the entity, the auditor shall evaluate whether the information is sufficiently reliable for the auditor's purposes, including as necessary in the circumstances:

- Obtaining audit evidence about the accuracy and completeness of the information; and
- Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes.¹⁰

The standards specify that where there are doubts over the reliability of information to be used as audit evidence, the audit should be redesigned and expanded to include other evidence and aspects of the subject. In not meeting the standards of the AASB, the ANAO is in breach of its own standards and legislation, which are based on those of the AASB.¹¹ Given the ANAO's critical findings and the remaining unanswered issues, we question why the ANAO did not expand the audit and obtain additional audit evidence.

¹⁰ Auditing and Assurance Standards Board (2019) *Auditing Standard ASA 500: Audit Evidence*, https://www.auasb.gov.au/admin/file/content102/c3/ASA_500_Compiled_2019-FRL.pdf

¹¹ Australian Government (2018) *Australian National Audit Office Auditing Standards 2018*, <https://www.legislation.gov.au/Details/F2018L00179>

Value for money

The ANAO made the following findings in relation to 'value for money':

- It is not clear how the department assessed individual procurements to determine their strategic priority or considered how to encourage competition within the limited tender process,
- The department's design of the limited tender approach did not appropriately consider opportunities to generate competition between sellers, and a communication strategy was not developed,
- The department did not develop a framework designed to maximise the value for money of strategic water entitlements purchased through limited tender arrangements. Rather, the department relied on a methodology of valuations where gap-bridging water was required.

These findings indicate that there is a high risk that value for money was not achieved and that the Department was driven to make these purchases by other motives, with seemingly little regard to financial cost. It is therefore surprising that the ANAO seems to rely solely on the Department's own assessment of valuations, that is:

- That the valuations were within the range of 'independent' valuations commissioned by the Department for the Condamine-Balonne, Lower-Darling/Baaka and Warrego valleys;
- That a premium of 30% was warranted for the Condamine-Balonne purchase, because the properties were of exceptional value; and
- An erroneous desktop analysis of purchases in the Murrumbidgee.

In our view, the audit failed to obtain sufficient and appropriate audit evidence by relying on the information the Department used to justify the valuations. There is sufficient alternate evidence in the public domain and reported in our research to have alerted the ANAO that there were inconsistencies in, or doubts over the reliability of, the audit evidence that was relied on. In response the audit should have been redesigned and the auditors should have sought other evidence.¹²

¹² Auditing and Assurance Standards Board (2019) *Auditing Standard ASA 500: Audit Evidence*, https://www.auasb.gov.au/admin/file/content102/c3/ASA_500_Compiled_2019-FRL.pdf

CONDAMINE-BALONNE

The Condamine-Balonne strategic purchase was of 29,159 megalitres of Overland Flow (OLF) Licences at \$2,745 per megalitre from the properties Clyde and Kia Ora owned by Eastern Australia Agriculture (EAA), a company founded by Minister Angus Taylor.

The ANAO appears to have relied solely on a valuation commissioned by the Department to infer (but not explicitly state) that the price paid was reasonable. This is despite other, readily available, lines of evidence that challenge that conclusion.

1. The purchase was well above the value recognised by the vendor, who recorded a \$52m profit on the \$80 million transaction. Both properties, including the water licences, were valued at \$107m in total, just \$27m more than the Department paid, despite EAA retaining more water than they sold - 31.6 gigalitres. On this basis alone, it appears that DAWR paid tens of millions of dollars too much.
2. The price paid exceeded the vendor's original offer, suggesting that they valued the water at less than was ultimately paid. As outlined in our report *That's not how you haggle: Commonwealth water purchasing in the Condamine-Balonne*,¹³ the price originally offered by the vendors was \$2,200 per megalitre. After negotiation, the Government paid a higher price - \$2,745 per megalitre. Prior to this purchase, the Commonwealth had purchased approximately 50 gigalitres of water in the Condamine Balonne through several open tenders and has paid an average price of between \$1,433 and \$1,795 for unsupplementary licences, which are superior to overland flow licences.
3. EAA had unsuccessfully offered to sell water to the Commonwealth eight times between 2008 and 2015. Seven of those times, the offers were rejected as 'Not Value for money'. The highest offer for overland flow water was \$1,565, a little over half of the price the Commonwealth paid in this purchase. This is outlined in our report *Rough Estimates*.
4. The NSW Irrigators Council has publicly stated that the price paid was 'grossly inflated' and nearly double the independent valuation:

¹³ Slattery & Campbell (2018) *that's not how you haggle*, <https://australiainstitute.org.au/report/thats-not-how-you-haggle/>

As for being worth \$2745 per megalitre, which the Commonwealth paid Eastern Australian Agriculture in Queensland in 2017, that was almost twice the independent valuation. It will not in any sense be the going market price.

Floodplain licences will be inherently less reliable than supplementary licences trading for \$1000 to \$1400 a megalitre in northern valleys, and the ability to trade will be restricted.¹⁴

The valuation relied on by the Department and used as evidence by the ANAO is itself problematic. The Department refused to release the valuation to the Senate without redactions even though it was publicly known that a higher price had been paid for lower security licences than in previous purchases. In answers to questions on notice the Department maintained that it had paid a price “above an estimated ‘standard market value range’, but below the maximum price the independent valuer advised we should expect to pay”.¹⁵ This claim appears to have been accepted by the ANAO, with its report similarly stating:

The price the department paid for water entitlements was equal to or less than the maximum price determined by valuations.¹⁶

However, the valuation document was eventually released after Senator Patrick submitted a Freedom of Information request and contested its refusal with the Information Commissioner. The unredacted valuation reports a central estimate of \$1,500/ML within a range of \$1,100 to \$2,300/ML.

It is now uncontested that the Department paid 20% above valuation range provided and almost double the central estimate. The Department’s claim around maximum prices refers to a separate part of the valuation report which discusses a potential premium of up to 30% for particular properties of “high standard”:

The market sentiment is considered to be improving and, for many of the above properties, if offered on the market today an improvement in value could be anticipated. By our estimate, this may range from only 10 percent to as high as 30 percent.

We have provided a value and a value range. The majority of OLF licences would be considered to be in the lower end of this range. The exception to this would be individual properties of a high standard that have achieved above average

¹⁴ Miller (2020) *So what will the licencing of floodplain harvesting mean?*,

<https://www.theland.com.au/story/6977219/floodplain-harvesting-licensing-essential/?cs=5739>

¹⁵ Department of Agriculture and Water Resources (2020) Rural and Regional Affairs and Transport Committee, Question on Notice 197, 2018-19 Budget estimates

¹⁶ Page 9

levels of water use efficiency, in which case would be in the higher end of the value range.¹⁷

The valuer says nothing about what the Commonwealth, or any other buyer, “should expect to pay”. He makes it clear that the majority of OLF licences in the region would be at the lower end of his estimated range.¹⁸ In order to justify any premium, the Department and the ANAO needed to satisfy themselves that the Clyde and Kia Ora properties were considered to be “individual properties of a high standard”. Neither has done so. When asked about this in Senate Estimates, the representative of the ANAO puts great weight on a sale of water from one particular property, “Boongargil”:

Senator PATRICK: I put it to you that no reasonable person could somehow extrapolate what is clear in the valuer's report as to the range of the valuation. I think you might have been suckered in by the department in terms of how they might have interpreted it.

Mr White: I think the statements in the report are very clear when it talks about how the Boongargil sale at \$2,300 would be the absolute minimum that could be expected if it was sold again. That's outside of the range that's provided in the conclusion, because it reads into it the 10 to 30 per cent premium that's expected.

Senator PATRICK: The range actually goes up to \$2,300.

Mr White: The report actually also says that that would be the absolute minimum that you could expect and that future sales would even be higher than the Boongargil sale.

In this answer, the ANAO fails to mention that the Boongargil property is more than 150 kilometres away and in a different valley from the Kia Ora and Clyde properties that sold the strategic purchase water to the Commonwealth.

Furthermore, the valuation makes it clear that the valuer considered Boongargil a “good quality irrigation holding”, particularly in relation to its use of overland flow water. In other valuations, some by the same valuer, the Kia Ora and Clyde properties are considered the worst performing comparable properties with measures of efficiency just 39 - 47% of the highest performers. Far from being high performers, EAA was operating at a considerable loss prior to the sale, with net liabilities in 2017 of

¹⁷ Colliers International Valuation & Advisory Services (2016) Valuation of Overland Flow licences: Condamine Balonne Water Resource Plan, Available under FOI LEX 3189

¹⁸ Colliers International Valuation & Advisory Services (2016) *Valuation of Overland Flow licences: Condamine Balonne Water Resource Plan*, Available under FOI LEX 3189

\$28,570,000, up from \$15,383,000 in 2016. These details are covered in our report *A little more valuation, a little less redaction please*.¹⁹

In writing that report, we obtained seven external valuations for two properties located in between the two EAA properties. Two of those valuations were prepared by the same individual valuer used by the Department. All of the external valuations used a similar valuation method. They each used comparable properties in the Balonne valley, including the two EAA properties. None of those seven valuations compared properties outside the Balonne valley.

However, the valuation prepared for the Department used a different method and used ten 'comparative' properties, only two of which were in the Balonne valley. The market value of the properties in different valleys were higher than the market value of properties in the Balonne valley.

This example shows that the ANAO has not met its Audit Standards, as it has failed to:

- Obtain an understanding of the work of the external expert valuer;
- Evaluate the appropriateness of that valuer's work as audit evidence for the relevant assertion;
- Evaluate whether information produced by the Department being audited is sufficiently reliable by obtaining audit evidence about the accuracy and completeness of the information;
- Evaluate whether the information is sufficiently precise.

Neither the Department nor the ANAO, in its audit, or in Senate Estimates, has offered any rationale or evidence for how the conclusion was reached that the EAA properties were of 'high standard' to justify the 20% premium on the top end of the reported range and almost double the point estimate in the valuation report. At time of writing the ANAO had not answered Senator Patrick's question on notice on this issue.

Recommendations: The Committee should ask the ANAO for a detailed explanation on:

- **How its finding that prices paid were below valuation maximums are consistent with the unredacted valuation by Colliers International titled *Valuation of Overland Flow licences: Condamine Balonne Water Resource Plan*.**

¹⁹ Slattery and Campbell (2020) *A little more valuation, a little less redaction please*, <https://australiainstitute.org.au/report/a-little-more-valuation-a-little-less-redaction-please/>

- **How the audit evidence used in relation to the Condamine-Balonne purchase, and the ANAO's efforts to understand that evidence, meet its Audit Standards.**

Importantly, the CEWH has subsequently paid two million dollars for EAA to forgo accessing OLF Licences from one of the properties where the strategic purchase was made.²⁰ This was to access the first flush of water in the system for the environment. This payment was for a single event. The need for the CEWH to make additional, potentially ongoing, multi-million dollar payment to the same company it purchased \$80 million of OLF, calls into question whether the original purchase was value for money and whether the evidence relied on by the ANAO is reliable.

LOWER DARLING/BAAKA

The purchase of 22 gigalitres for \$80 million, plus the next year's water allocation from Tandou station on the Lower Darling/Baaka was controversial due to the price paid and the fact that, at the time, a similar deal was not available to other local water holders who had been in negotiations with the Government for several years. By contrast, this purchase saw major agribusiness Webster Limited apparently approached by government to sell theirs.²¹

The Auditor-General's claim that prices paid for water were within commercial range is based on published valuations ranging between \$25 million and \$52 million, with the final price paid being \$38 million (Table 4.1). In a note to this table it says that the purchase "also included an additional \$40 million compensation payment". With the 'compensation payment' included, the price paid is clearly higher than any possible valuation of the water assets and notably Webster reported a \$36.4 million profit on the transaction.

The Auditor-General is quiet on aspects of the valuation that should have called the Department's evidence into question and cast doubts over the reliability of that evidence, namely:

- The business was valued at 'Highest and Best Use' and assumed 100% of water in 100% of years,

²⁰ Davies (2020) *Government to spend millions buying water from company it already paid \$80m*, <https://www.theguardian.com/australia-news/2020/feb/26/government-to-spend-millions-buying-water-from-company-it-already-paid-80m>

²¹ Personal correspondence with Webster Limited dated 16 October 2018, available on request.

- The valuation included an additional compensation of 117% of the market value of the entire business (including water), in addition to payment for water and the land stayed with the vendor;
- The water valuation was based on Murrumbidgee prices: \$3,253/ML for High Security and \$1,526/ML for General Security, not Lower Darling/Baaka prices;
- The vendor was given an extra year's water free, with no reduction in the value of the water, or compensation.

It is clear from correspondence from Webster executive, Chris Corrigan, that the price paid was based on a price set by Webster, rather than the Commonwealth's valuation of the water. Mr Corrigan wrote to The Australia Institute and objected to us highlighting the compensation component in our report *I'll have what they're having*:

This is just semantics. We had a property and some water entitlements. We made an assessment of its value as a productive asset and we negotiated a commercial price. Whether you term it compensation, sale price or something else the simple facts are that we had no intention of selling the [water] assets at a lower price than they were worth to us.²²

Leaving the unprecedented "compensation" aside, the water valuations themselves are problematic. One values Tandou's Lower Darling/Baaka water at Murrumbidgee prices, rather than Lower-Darling or Murray prices. Water licences in the Murrumbidgee are the most expensive in the Southern Basin after the upper NSW Murray. Another assumes a change in trade rules with no clear reason for this assumption. Regardless, the prices paid were the highest ever paid for both high and general security licences in the Lower-Darling.

The ANAO omits discussion of Tandou being gifted a water allocation for the following water year. This enabling it to harvest a \$35 million cotton crop. This was not included in any valuation study of the value of the water or property. Please find full details and references relating to these points in our report *I'll have what they're having: A step-by-step guide to valuing compensation in the Lower-Darling*.²³

The NSW Independent Commission Against Corruption (ICAC) recently handed down a report that included scrutiny of the Tandou purchase. That report included information that should have been known to the Auditor-General and directly relevant to this audit:

²² Personal correspondence with Webster Limited dated 16 October 2018, available on request.

²³ Slattery & Johnson (2018) *I'll have what they're having*, <https://australiainstitute.org.au/report/ill-have-what-theyre-having/>

- In July 2016, the Department noted that Tandou was transitioning to a dryland operation because it was no longer viable as an irrigated cotton enterprise, because diminished inflows limited operations to two years out of six,
- The purchase may not meet the Commonwealth procurement rules,
- The water was valued above Murrumbidgee market value, despite the Commonwealth not supporting this valuation,
- That using the Murrumbidgee market doubled the valuation if the Lower Darling/Baaka market was used,
- Relevant valuations were undertaken by Tandou Ltd, and the price paid was not based on independent valuations,
- NSW officials organised the 'independent' valuation that was ultimately relied on by the Department,
- No evidence relating to the reasoning to compensate Tandou Ltd for the decommissioning of that business.²⁴

Recommendations: The Committee should ask the ANAO to explain whether the valuations used in the Lower Darling/Baaka purchase comply with its Audit Standards, particularly in light of the NSW ICAC report.

In December 2019, the Department purchased an additional 1,159 megalitres of High Security water from five families in the Lower-Darling/Baaka for \$8,500 per megalitre, and an additional \$26.2 million for:

- a business restructuring package, including loss of business value and income;
- removal of permanent horticultural plantings; and
- restrictions placed on the future use of the properties.²⁵

This purchase was not examined by the ANAO, despite it being a strategic purchase that was finalised during the period that the ANAO report was being prepared. The Department's website describes the transaction:

This purchase provided good value for money. All elements of the transaction including the negotiated price of \$8,500/ML for the water entitlements, were

²⁴ Independent Commission Against Corruption (2020) *Investigation into complaints of corruption in the management of water in NSW and systematic non-compliance with the Water Management Act 2000*, <https://www.icac.nsw.gov.au/media-centre/media-releases/2020-media-releases/icac-recommends-changes-to-government-water-management-in-nsw-after-years-of-focus-on-irrigation-industry-interests>

²⁵ Department of Agriculture, Water and the Environment (2020) *Surface water purchasing – limited tender*, <https://www.agriculture.gov.au/water/markets/commonwealth-water-mdb/limited-tender#nsw-lower-darling-december-2019>

consistent with independent valuations. The transaction was overseen by an external probity advisor.²⁶

It is not clear how Lower Darling/Baaka High Security water entitlements could have increased in value from the already inflated price of \$3,253 in 2017 to \$8,500 in 2019. A proposal from that group of water holders to the Commonwealth Government in 2015 noted that water security in the Lower Darling was declining:

Since the 1980's, the security of water supply in the Lower Darling River downstream of Menindee has been reduced as a consequence of upstream irrigation development and, more significantly, from changes to the operations of the Menindee Lakes.²⁷

Recommendation: The Committee should ask the ANAO whether valuations of Lower Darling/Baaka entitlements support the prices paid in December 2019 and whether this audit can be extended to investigate these purchases.

WARREGO

Similar valuation issues are likely to exist for the Warrego purchase. The Auditor-General's Table 4.1 shows that the valuation amount, maximum considered, and seller's offer are all exactly the same amount.

It seems that the Auditor General relied solely on the 'independent' valuation commissioned by the Department, despite questions about the reliability of that evidence.

Documents obtained by Senator Patrick under a Freedom of Information request and made available under Order for Production of Documents 579, 37 months after they were requested, show the Warrego valuation used the same valuer and method to that used for the Condamine-Balonne valley.

The valuation relied on comparable properties outside the Warrego valley to justify the price paid by the Department. The ANAO should have harboured doubts about the

²⁶ Department of Agriculture, Water and the Environment (2020) *Surface water purchasing – limited tender*, <https://www.agriculture.gov.au/water/markets/commonwealth-water-mdb/limited-tender#nsw-lower-darling-december-2019>

²⁷ Lower Darling Horticultural Group (2015) *Proposal for the removal of irrigation of permanent plantings on the Lower Darling river between Weir 32 at Menindee and the upstream confluence of the Wentworth Weir on the River Murray*, Obtained via GIPA

Condamine-Balonne valuation, and because the same valuer and method was used, about the veracity of this valuation.

The price paid of \$1,600 per megalitre was double the only other Commonwealth purchase of water in the Warrego in 2008. The ANAO completed an audit of that purchase and concluded that the price paid of \$719 per megalitre was reasonable. That same report noted that at the time, that the Department considered a price of \$783 per megalitre as 'excessive'.

The doubling of the price from the time of the previous Warrego purchase is not consistent with water market price changes generally.

For more information, see our report *Moving Targets: Barnaby Joyce, Warrego valley buybacks and amendments to the Murray Darling Basin Plan*.²⁸

Recommendation: The Committee should ask the ANAO for a detailed justification of why valuations of water outside the Warrego were used for this purchase and why the value of Warrego water has more than doubled to \$1,600/ML since it declared \$783/ML 'excessive'.

MURRUMBIDGEE

The Department paid \$370 per megalitre for 12,117 megalitres in the 2017 Murrumbidgee strategic purchase of Lowbidgee Supplementary water.

The value for money assessment was a simple desk-top analysis undertaken by the Department. It analysed the sales of Murrumbidgee Supplementary water share prices, not Lowbidgee Supplementary prices.

While the name is similar, Murrumbidgee Supplementary shares are a different water share category to Lowbidgee Supplementary shares and should not be used as a price comparison. That is, the Department's desktop analysis is in error.

The ANAO concluded that the price paid for the Murrumbidgee was less than the market valuation. To reach that conclusion, the ANAO either relied entirely on the Department's valuation, or less likely, undertook the same analysis and made the same error.

Additional evidence was available to the ANAO, including;

²⁸ <https://australiainstitute.org.au/report/moving-targets-barnaby-joyce-warrego-valley-buybacks-and-amendments-to-the-murray-darling-basin-plan/>

- Our submission, *Strategic failure: Submission on procurement of strategic water entitlements*, which identified the error;
- NSW Water Register; and
- The ANAO audit, *Funding and Management of the Nimmie-Caira system enhanced environmental water delivery project*.

Prior to this strategic purchase, there were no trades of the Lowbidgee water shares, except the previous purchase by the Commonwealth in 2014, the Nimmie-Caira purchase, at \$175 per megalitre. The Auditor-General's 2015 audit concluded that the government had paid a premium then. Rather than providing 'exceptional value', the Department paid more than double (211%) of the price that was previously determined to be at a premium.

The Auditor-General was asked about this in Senate Estimates:

Senator PATRICK: When you looked at the purchase, DAWR had used a desktop valuation that related to Murrumbidgee supplementary licences; that's how it came to the conclusion that it was paying the right price. However, under the water-sharing plans you're not allowed to transfer water from the Murrumbidgee to the Lowbidgee area. I'm just wondering why you accepted the valuation methodology of the department, taking valuations from one valley (sic) and using them in another?²⁹

At time of writing no answer had been provided to this question taken on notice.

For more detail, please see our submission to the Auditor-General, *Strategic failure: Submission on procurement of strategic water entitlements*.³⁰

Despite these issues, in January 2020, the Department purchased an additional 13,506 megalitres of LowBidgee Supplementary entitlements at \$560 per megalitre, more than 50% higher than the already inflated previous purchase of the same entitlement class.

This purchase was not examined by the ANAO, despite it being a strategic purchase that was finalised during the period that the ANAO report was being prepared. The Department's website describes the transaction:

This purchase provided good value for money at the nominated price. The accepted price of \$560 per ML was within independent market valuation range.

²⁹ Hansard (2020) Finance And Public Administration Legislation Committee Estimates Monday, 19 October 2020, p166, https://www.aph.gov.au/Parliamentary_Business/Senate_estimates/fpa/2020-21_Budget_estimates

³⁰ <https://australiainstitute.org.au/report/strategic-failure/>

The proposal recovered water in a region where further water recovery was required to bridge the gap to the Basin Plan's sustainable diversion limit.³¹

The same error continues to be made around LowBidgee Supplementary and Murrumbidgee supplementary water, with ongoing costs for taxpayers and the environment, discussed below.

Recommendation: The Committee should ask the ANAO to explain why Murrumbidgee supplementary valuations were used to evaluate purchase of Lowbidgee water, and whether this approach meets ANAO audit standards.

³¹ Department of Agriculture, Water and the Environment (2020) *Surface water purchasing – limited tender*, <https://www.agriculture.gov.au/water/markets/commonwealth-water-mdb/limited-tender#nsw-lower-darling-december-2019>

Bridging the gap

The ANAO report states:

The department's strategic purchases of water through limited tender contributed to the government policy to bridge the gap and obtain water for the environment.³²

'Bridging the gap' refers to the difference between the historic levels of water diversion, the 'Baseline Diversion Limit' (BDL) and the level of water diversion that Basin scientists consider sustainable, the 'Sustainable Diversion Limit' (SDL). The policy intent of 'Bridging the Gap' is to reduce water used for irrigation and increase water available for the environment. To give proper effect to 'Bridging the Gap', the following criteria must be met:

- the Commonwealth Environmental Water Holder must own the water licence (ownership);
- the reliability (or yield) of the water licence must not be diminished after acquisition (reliability);
- the water licence must be able to be utilised in a way to meet the SDL or Environmentally Sustainable Level of Take (meet the ESLT);
- the water licence usage must have been in the BDL (in the BDL), and
- the purchase should not enable increased production.

Whilst all the purchases we examined met the criteria of ownership, they did not meet at least one of the other criteria, and therefore failed to 'Bridge the Gap'.

The Auditor-General did not provide any evidence or rationale as to how the purchases resulted in 'Bridging the Gap'. Notably, the Auditor-General's report does not include the terms "Baseline Diversion Limit" or "reliability".

CONDAMINE-BALONNE

The Condamine-Balonne purchase was made up of two Overland Flow Licences (OLF) one each on the properties 'Kia Ora' and 'Clyde'. At least part of the OLF licence associated with Clyde was not in the BDL and therefore should not count towards 'Bridging the Gap'.

The BDL was finalised when the Basin Plan was made in November 2012, but the volume associated with the Clyde OLF was negotiated between the Federal and Queensland Government and the vendor during 2016 and 2017 and the licence was only created in September 2017, after the sale to the Commonwealth was finalised.

The BDL is determined by a hydrological model, called the Integrated Water Quantity and Quality simulation Model (IQQM). The vendor's Chief Executive Officer explains in an email to DAWR that the Clyde overland flow volume was not in the IQQM model:

[Consultant] Owen Droop has suggested that to integrate this data [the S11 OLF take] into the IQQM model it may be necessary to also model in the relationship between flow at the DH gauge (which is in the model) and the height at the gauge.³³

If the Clyde OLF licence was created in September 2017 and it was not in IQQM when the Basin Plan was finalised, it could not have been in the BDL. That means it could not have been included in the BDL and cannot count towards 'Bridging the Gap.'

This is explained further in our report #*Watermates*.

Recommendation: The Committee should ask the ANAO to explain how it determined that Condamine-Balonne overland flow licences were included in the Baseline Diversion Limit and if they can fully contribute to water recovery or 'bridging the gap'.

In addition, OLF only have legal status on the property where they are located. The OLF licences only have a value to the Commonwealth Environmental Water Holder (CEWH) if they can be allowed to flow off the property into the downstream floodplain or rivers and be protected from downstream extraction. Some of the ways the CEWH could achieve this is by:

- goodwill or remunerated negotiations with adjacent landholders,
- goodwill or negotiation with the Queensland Government when announcing downstream pumping access,
- goodwill or negotiation with the NSW Government to allow any OLF water entering the State to be protected from extraction.

These actions are challenging and governments have been attempting solutions for more than a decade, with limited success to date. Notwithstanding, none of the actions proposed to date ensure that OLF water owned by CEWH has legal status

³³ Bickford-Smith (2017) Email to Mary Colreavy: RE: S11 intake calculations for the purposes of establishing OLF NV, Obtained by The Guardian under Freedom of Information 2017/18-86

outside its originating property. Thus, it is highly questionable whether the claim that OLF 'Bridging the Gap' is reasonable.

Recommendation: The Committee should ask the ANAO how it determined the Condamine-Balonne purchase water legal status and ability to contribute to 'bridging the gap', and whether the sources used for this determination meet its standards for audit evidence.

LOWER DARLING/BAAKA PURCHASE

The strategic water purchase in the Lower Darling/Baaka was justified by DAWR on the grounds that it would no longer have to be supplied;

The Tandou's water entitlements represent a major demand to be managed from water held at Menindee Lakes. Removing the need to manage these water entitlements from Menindee Lakes will enhance the potential outcomes from the proposed Menindee project and contribute to improved outcomes under the Basin Plan. The Murray-Darling Basin Authority has advised that a 650 gigalitre supply offset under the SDL adjustment mechanism will require an enhanced Menindee Project that includes a reduction in downstream water demands in the Lower Darling.³⁴

That is, the purchase was justified on the basis that it would be a water savings because it would no longer need to be supplied, which is another way of saying it will have a lower reliability. The Long Term Average Annual Yield (LTAAY) after the purchase and related Menindee Lakes project should be reduced, so less of the CEWH water should count towards 'Bridging the Gap'.

There is also a view that the purchase is aimed at removing a large source of demand with powerful owners. Without this demand there is less need to keep water flowing in the Darling below Bourke, raising environmental management, equity and Aboriginal rights issues. In other words, the purchase affects reliability of supply for other users and is therefore against the rules of the Basin Plan. For discussion of this issue, please see our report *Trickle Out Effect: Drying up money and water in the Lower Darling*.³⁵

Recommendation: The Committee should ask the ANAO to explain how it determined that the reliability Lower Darling/Baaka water purchase was not

³⁴ OPD 420

³⁵ Slattery & Johnson (2020) *Trickle Out Effect*, <https://australiainstitute.org.au/report/trickle-out-effect/>

affected, whether it can contribute to ‘bridging the gap’ and whether the sources used in this determination meet ANAO audit standards.

WARREGO PURCHASE

The SDL in the Warrego has already met, meaning there is no longer any gap to bridge. The point of the purchase was to substitute with shared reduction from the Border Rivers. A swap like this may be beneficial if the ‘swap’ actually contributes downstream. However, very little Warrego water reaches the Barwon Darling, so the shared reduction would not be achieved and should not count towards bridging the gap in that valley. For more information see our *Moving Targets* report.

Recommendation: The Committee should ask the ANAO to confirm that there is no ‘gap to bridge’ in the Warrego, and if so, how it determined that a potential transfer to another valley would contribute to government policy.

MURRUMBIDGEE PURCHASE

As discussed above, the Murrumbidgee Water Access Licences (WALs) purchased were ‘Lowbidgee Supplementary’ licences.

The ANAO undertook a previous audit of Lowbidgee Supplementary licences in 2015. That audit found that;

While the LTAAY from the 381 GL to be obtained under the project equated to 173 GL, only 133 GL was assessed by Environment as counting towards ‘bridging the gap’ targets as it considered that 40 GL was already committed to pre-existing environmental watering purposes. This assessment has been contested by the NSW Government and is subject to further consideration in 2016.³⁶

³⁶ANAO (2015) *Funding and management of the Nimmie-Caira System Enhanced Environmental water delivery project*, <https://www.anao.gov.au/work/performance-audit/funding-and-managementnimmie-caira-system-enhanced-environmental-water>

The additional purchase of 12,117 gigalitres of Lowbidgee Supplementary licences in 2017 further exacerbates this problem of not being in the BDL and therefore not contributing towards 'Bridging the Gap'.

On the contrary, the vendor had told the Department that they were looking to use funds raised by selling unused Lowbidgee water to increase irrigation elsewhere, as discussed in a released Departmental email:

They will continue to dryland farm on that property, however with the monies they are looking to increase production and water efficiency on their (redacted) property. They have livestock there along with annual and permanent pastures and are wanting to put in another pivot to increase the intensity of their production down there.³⁷

It is clear that this water purchase was not going to contribute to environmental goals, further demonstrated by the CEWH's preference not to buy it, clear in the Auditor-General's Table 4.1.

The Commonwealth Environmental Water Holder did not want this water, as noted in the Auditor General's Table 4.1. In Paragraphs 3.39 to 3.41 of the Auditor General's report, particularly 3.41, the Lowbidgee supplementary and Murrumbidgee supplementary terms are used interchangeably. As mentioned above, yet more of the same class of water was bought in January 2020, with no comment from the ANAO.

Recommendation: The Committee should ask the ANAO to confirm that there is no 'gap to bridge' in the Lowbidgee area, and if so, how it determined that further purchases there contribute to government policy on water recovery.

For further information, please see our submission to the Auditor-General, *Strategic failure: Submission on procurement of strategic water entitlements*.³⁸

³⁷ Williams (2016) Email to DAWR officer: Lowbidgee, <https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id:%22publications/tables/papers/59682649-2fa2-43b1-955f-ae16caecef45%22>

³⁸ Slattery & Campbell (2019) *Strategic Failure*, <https://australiainstitute.org.au/report/strategic-failure/>

Conflict of interest

The Auditor-General found that there were inadequate process relating to conflict of interests. However, no conclusion was reached whether there were any actual conflict of interests.

The risk of actual conflict of interest are high, based on:

- Purchases found not to be developed within a value for money framework;
- The high value of the purchases;
- Absence of open tender process;
- Absence of a finalised framework for strategic purchases.

In our reports, *#Watermates* and *Rough Estimates*, we identify a potential actual conflict of interest in relation to Tony Reid, a close, long-time business associate of Energy Minister Angus Taylor, who had associations with the EAA properties.

We note that the Auditor-General's report discussed conflict of interest only in relation to the valuations of water purchases. There are other potential conflicts of interest, including:

- Undertaking the modelling of overland flow licences in the Condamine-Balonne;
- The due diligence of modelling of overland flows licences in the Condamine-Balonne;
- The preparation of any reports relating to the decommissioning of structures relating to purchases in the Condamine-Balonne or in the Lower-Darling/Baaka.

Recommendation: The Committee should ask the ANAO whether it looked for actual conflicts of interest relating to the purchases from valuers, modellers and people involved in other aspects of the transactions.

Decommissioning works

Part of the purchase negotiations required the decommissioning of works at Kia Ora (Condamine-Balonne). It seems the Auditor-General obtained insufficient evidence to determine whether those works were actually decommissioned at the relevant times.

CONDAMINE-BALONNE

Much of the controversy around the EAA strategic purchase was whether a dam at Kia Ora was decommissioned, as requested by the Minister, prior to the purchase.

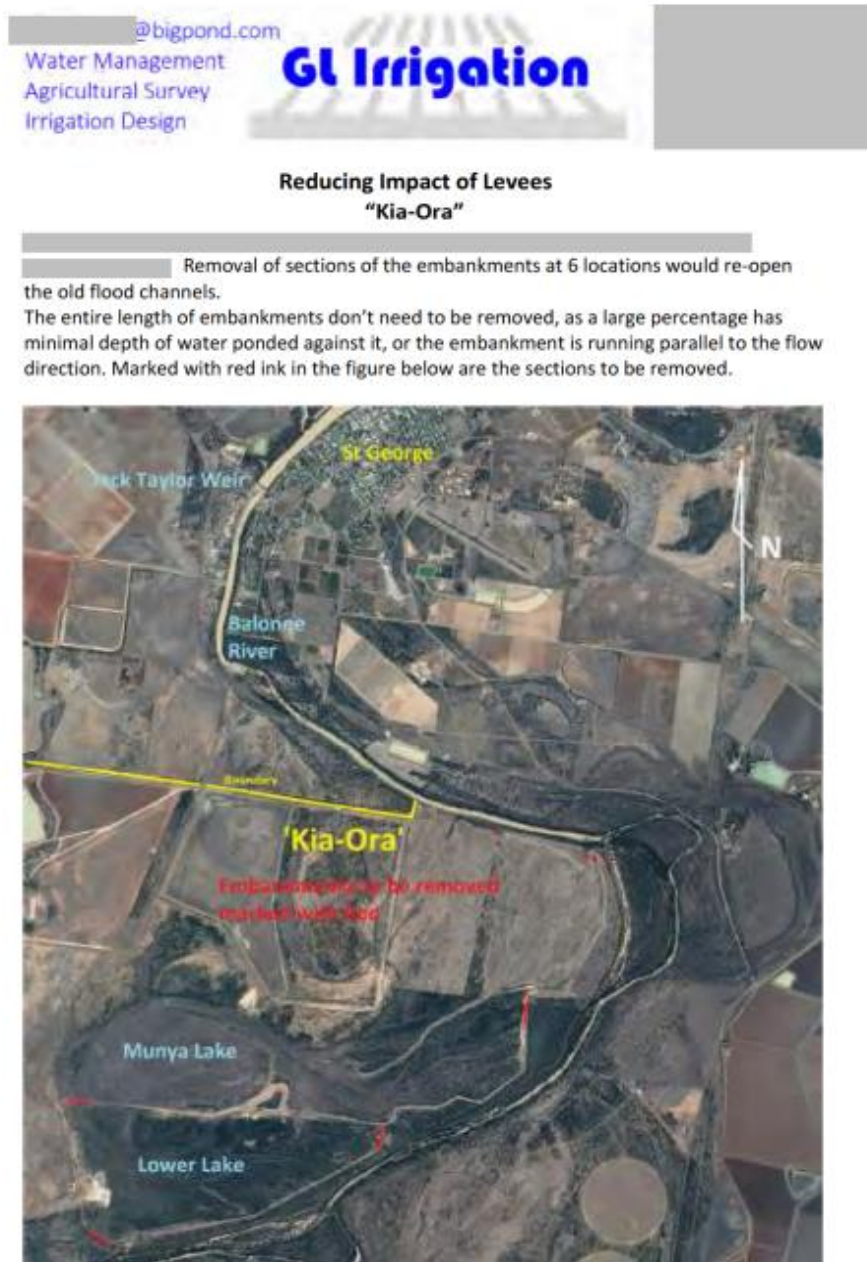
The Auditor-General reported:

There is no evidence that the department obtained verification of the report from the Queensland Department of Natural Resources and Mines.

The report cited in the ministerial brief consisted of a single page, including one satellite image of the location with red ink annotations and the following text: In the 2010, 2011 and 2012 floods, the levees on the eastern side of “Kia-Ora” raised floodwater levels. Removal of sections of the embankments at 6 locations would re-open the old flood channels. The entire length of embankments don’t need to be removed, as a large percentage has minimal depth of water ponded against it, or the embankment is running parallel to the flow direction. Marked with red ink in the figure below are the sections to be removed.

That single page reproduced in its entirety at Figure 1 below.

Figure 1: Documentation to support the decommissioning of banks at Kia Ora



We agree with the Auditor-General's inference that the single page of satellite imagery shown in Figure 1 is inadequate evidence to demonstrate that the banks were decommissioned at the time of purchase, or in a timely manner thereafter.

The ANAO notes that "the CEWH confirmed in March 2020 that the decommissioning had occurred and subsequently allowed water to return to the floodplain" (p42), referring to an appearance at Senate Estimates by Commonwealth Environmental

Water Holder Jody Swirepik. Note that the CEWH provided that answer ten months after television footage showed that the dams were not decommissioned.³⁹ This allowed ample time for decommissioning between the allegations being made and before the Senate estimates answer was given.

To summarise this issue:

- The ANAO found that the Department did not verify the decommissioning;
- Television footage showing the dam was not decommissioned at May 2019;
- The ANAO identified that a single page satellite image was the entirety of the Department's evidence around the decommissioning;
- An answer to Senate Estimates in 2020 was ANAO's evidence for the decommissioning.

Recommendation: The Committee should ask the ANAO to explain whether it found any evidence of the Condamine-Balonne purchase conditions being met prior to March 2020 and whether the evidence relied on in the audit meets Audit Standards.

³⁹ MacDonald (2019) *The Project: WaterGate*,
<https://www.facebook.com/TheProjectTV/videos/2410887885799878/>

Conclusion

In 2018 the Australian Government purchased an area of land for a future Sydney airport, an area now known as the Leppington Triangle, for \$30 million. The Department of Infrastructure revalued the land at just \$3 million in mid-2019. This ‘significant and unusual’ revaluation triggered a detailed examination by the Auditor-General and intense public scrutiny.⁴⁰

If similar standards were followed with the valuation of water held by the Commonwealth Environmental Water Holder, the likely devaluation of rights acquired through “strategic purchases” would dwarf the Leppington Triangle purchase, demonstrated by just two of the vendors announcing \$90 million in profit from their transactions.

Yet the Auditor-General’s report into strategic purchases highlighted only poor processes and recommended improvements in assurance mechanisms, procurement guidance and evaluation frameworks. It is unclear why this investigation did not go further into where taxpayer money went and whether the problems highlighted resulted from incompetence or maladministration. Given the \$698,700 cost of the strategic water purchase audit, it seems unlikely that the ANAO team lacked the resources needed to understand the complex world of water administration. It is interesting that unlike the Leppington Triangle audit, no interviews were conducted with external valuers or any other parties outside of the departmental staff involved in the purchases.

We commend the Committee’s efforts to understand these issues and would be happy to provide further evidence in writing, via video link, or in person.

⁴⁰ Australian National Audit Office (2020) *Purchase of the ‘Leppington Triangle’ Land for the Future Development of Western Sydney Airport*, https://www.anao.gov.au/sites/default/files/Auditor-General_Report_2020-21_9.pdf