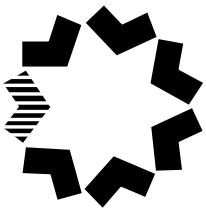

NATIONAL COMPETITION COUNCIL

ANNUAL REPORT 1997-98

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31 August 1998

The Honourable Peter Costello, MP
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer,

We submit to you the third Annual Report of the National Competition Council, for the year 1997-98. The report is prepared and submitted in accordance with section 29O of the *Trade Practices Act 1974*.

Yours sincerely,

Graeme Samuel
President

Stuart Hohnen
Councillor

Elizabeth Nosworthy
Councillor

Michael Easson
Councillor

Paul Moy
Councillor

CONTENTS

Part A Competition policy in overview

ABBREVIATIONS

ABARE	Australian Bureau of Agricultural and Resource Economics
ABB	Australian Barley Board
ABCS	Australian Black Coal Statistics
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACF	Australian Conservation Foundation
ACM	Australian Chamber of Manufactures
ACP	Australian Council of Professions
ACT	Australian Capital Territory
ACTO	Australian Cargo Terminal Operators Pty Ltd
ADT	Administrative Decisions Tribunal
AGA	Australian Gas Association
AGL	Australian Gas Light Ltd
ANL	Australian National Line
ANZMEC	Australia New Zealand Minerals and Energy Council
APAM	Australia Pacific Airports (Melbourne) Pty Ltd
APRA	Australian Prudential Regulation Authority
ARMCANZ	Agriculture and Resources Ministerial Council of Australia and New Zealand
ATC	Australian Transport Council
AUS	Australian Union of Students
AWB	Australian Wheat Board
COAG	Council of Australian Governments
Council	National Competition Council
CIE	Centre for International Economics
CPA	Competition Principles Agreement
CPU	Competition policy unit
CSO	community service obligation

CTOs	cargo terminal operators
DEETYA	Department of Employment, Education, Training and Youth Affairs
DLWC	Department of Land and Water Conservation (NSW)
DPIE	Department of Primary Industries and Energy
EEO	equal employment opportunity
FAC	Federal Airports Corporation
FOI	freedom of information
GBE	government business enterprise
GDP	gross domestic product
GJ	gigajoule
GPOC	Government Prices Oversight Commission (Tasmania)
GRIG	Gas Reform Implementation Group
GTE	government trading enterprise
HEC	Hydro-Electric Corporation
HRC	Healthy Rivers Commission (NSW)
HVA	Heavy Vehicles Agreement
ICA	Insurance Council of Australia
IGA	Intergovernmental Agreement
IPARC	Independent Pricing and Regulatory Commission (ACT)
IPART	Independent Pricing and Regulatory Tribunal (NSW)
LVA	Light Vehicles Agreement
MCRT	Ministerial Council for Road Transport
MDBC	Murray Darling Basin Commission
MHz	megahertz
MRA	*Mutual Recognition Act 1992* (Clth)
NCC	National Competition Council
NCP	National Competition Policy
NECA	National Electricity Code Administrator
NEM	National Electricity Market
NEMMCO	National Electricity Market Management Company

NR	National Rail (Corporation)
NRMA	National Roads and Motorists Association
NRTC	National Road Transport Commission
NSW	New South Wales
OECD	Organisation for Economic Cooperation and Development
OHS	occupational health and safety
ORG	Office of the Regulator-General (Victoria)
ORR	Office of Regulation Review (Clth)
QR	Queensland Rail
RAC	Rail Access Corporation (NSW)
R&D	research and development
RIS	regulation impact statement
SCARM	Standing Committee on Agriculture and Resources Management
SMA	statutory marketing arrangements
TAA	*Transport Administration Act 1998* (NSW)
TAB	Totalisator Agency Board
TCF	textiles, clothing and footwear
TPA	*Trade Practices Act 1974*
USO	universal service obligation
VCA	Victorian Channels Authority
VDTF	Victorian Department of Treasury and Finance
WAMP	Water Allocation Management Plan
WEA	Wheat Export Authority
WMA	*Wheat Marketing Act 1989* (Clth)

Abbreviations used in references are provided in the references section.

SETTING THE SCENE

In 1995, Australia's nine governments together agreed to implement a package of measures called National Competition Policy (NCP).

The NCP package builds on the 'pro-competition' principles embodied in the *Trade Practices Act 1974*. Both are based on the idea that competition, if properly harnessed, can provide substantial benefits for consumers and boost economic performance. Like the Trade Practices Act, NCP contains an explicit 'public interest' test to allow restrictions on competition to be retained where they serve the broad community interest. But whereas the Act remains limited in its scope, NCP seeks to reap the benefits available from competition, where it is appropriate, in all parts of the economy.

Now three years into the NCP program, evidence of major benefits has begun to emerge. Price reductions of up to 40 percent for rail freight and 60 percent for energy give a striking indication of some of the benefits available from competition. They can substantially lower business costs and make the difference between profitability and non-viability, particularly for businesses competing in export markets. Lower prices will also increase household spending power. However, there is a need to proceed with the NCP program if these benefits are to be fully realised.

At the same time though, political pressure to resist competition policy has increased over the last year. This is reflected in the difficulties encountered by some governments in fully meeting their NCP commitments and also in a recent increase in electoral support for groups that advocate, among other things, a retreat from competition policy.

These pressures reflect some genuine concerns among parts of the community. They stem, in part, from the inherent costs and social dislocation involved in economic change. But they also stem from the failure of governments to adequately address related issues such as equity and adjustment assistance, and limited community understanding and acceptance of the nature, need for and place of competition policy itself.

Australia's governments knew that implementation would not be simple when they embarked on the NCP program. While capable of lifting the economy's overall performance, the program challenges the monopolistic status of several groups. Further, the costs of change are often concentrated in a particular area and borne immediately, whereas the benefits are more diffuse and longer-term. And the arguments in favour of competition policy are not always reducible to a simple media grab.

But meanwhile, the economic pressures that drove the development of the NCP program have not gone away. The Asian crisis re-emphasises the importance of Australia improving the flexibility and performance of its economy.

Against this background, this report addresses not only governments' and the National Competition Council's progress in implementing competition policy; it also addresses the place of competition policy, and the other matters governments must attend to if the benefits from competition policy are to be fully reaped, equitably shared, and put to the best use.

In Chapter A1, the Council points out that, notwithstanding some recent slippages, there has been impressive progress in implementing competition policy to date. The chapter also outlines the task ahead and Part B elaborates on these matters. The key message is that, while substantial benefits are starting to flow from competition policy (see Box 1), considerable reform is still required if the prospective benefits are to be realised in full Australia-wide.

In Chapter A2, the Council discusses the relationship between competition policy and other elements of government policy.

It starts by pointing out that, contrary to the way competition policy has often been represented recently in public debate, NCP does not require privatisation, blanket deregulation, contracting out, reductions in community services, cuts in welfare, or reductions in the size of government. Nor does it ignore the environment, equity, unemployment, regional issues, or the social effects of change. And nor is it focussed simply on money, markets, materialism and economic growth. In other words, NCP is quite different from so-called economic rationalism.

Box 1 Some early outcomes from competition reform

- Electricity bills have fallen by around 23 to 30 percent on average, and up to a maximum of 60 percent, for those NSW and Victorian businesses covered by the national competitive market. As well, wholesale prices in Queensland have fallen by 23 percent since its internal competitive electricity market commenced.
- Gas prices for major industrial users fell by 50 percent after deregulation of the Pilbara market in 1995, while gas distribution tariffs are set to fall by 60 percent by the year 2000 in NSW.
- Rail freight rates for grain in Western Australia have fallen by 21 percent in real terms since deregulation in 1992-93, while rail freight rates for the Perth-Melbourne route fell 40 percent, and service quality and transit times improved, following the introduction of competition in 1995.
- Conveyancing fees in NSW fell by 17 percent between 1994 and 1996, after the abolition of the legal profession's monopoly and the removal of price scheduling and advertising restrictions, leading to an annual saving to consumers of at least $86 million.
- Prices for the outputs of government trading enterprises fell on average by 15 percent, and payments to governments doubled, in the four years to 1995-96, due partly to competition reforms.
- In Queensland, ten of the seventeen largest local councils have implemented two-part tariffs for water, resulting in an average saving in water usage of 20 percent in the first year.
- Following a review of business licensing in NSW that found significant duplication and overlap, some 72 licenses have been repealed and more are being scrutinised. Among other changes, 44 categories have been collapsed into just three.

Further details and examples are contained in Chapters A1 and A2 and Part B.

The Council also builds on a point from its last Annual Report that, in parallel with competition reform, governments need to address other elements of their policy mix — including social policy, the environment, tax reform, education and the labour market. This is important if the prospective benefits of competition policy are to be fully reaped, equitably shared and put to the best use. Hence, NCP should be seen as one plank in a platform of policies necessary to secure Australians' wellbeing and to help deal with our changing economic circumstances.

A key need is for governments to address mechanisms for dealing with the social effects of change, not just those associated with policy changes, but also those stemming from changes in the economy generally. There is a range of measures governments can use, from seeking to delay change to equipping people to cope with change, and compensating people adversely affected by change. That said, governments need to ensure that their policies do not negate incentives for necessary changes. They also need to recognise that many NCP reforms will enhance equity by removing long-standing privileges enjoyed by certain interest groups, at the expense of other members of the community. They therefore need to carefully scrutinise claims for special adjustment assistance — over and above that available to members of the community generally — and to ensure that any special assistance is rigorously justified, transitional in nature, and facilitates appropriate change.

The main themes from Chapter A2 are summarised in Box 2.

Finally, the Council reports on its own performance and operations over the last year in Chapter A3, with Part C providing administrative details.

Box 2 How NCP ties in with the broader policy spectrum

- While privatisation is one of several options from which a government can choose to apply 'competitive neutrality' principles to one of its businesses, the NCP agreements do not require the privatisation of any government business.
- Where a government chooses to privatise a public monopoly, NCP requires that the government undertake a review first with the aim of ensuring that appropriate pro-competitive safeguards are in place.
- NCP involves both increases and decreases in regulation; it does not require the removal of all anti-competitive regulation. This is because all markets need basic regulatory ground rules to operate efficiently and some markets require additional regulation to overcome deficiencies or inequities in the market.
- Although some industry development measures could contravene NCP principles, competition policy generally complements industry policy.
- NCP does not aim to increase economic growth itself but provides scope for higher and more sustainable growth. Governments seeking maximum sustainable growth rates also need to address other aspects of their policy mix.
- NCP does not require reductions in subsidised community services, and a number of NCP measures will enhance social welfare and fairness.
- Where NCP measures adversely affect a particular sub-section of the community, governments need to provide appropriate adjustment assistance. Special adjustment assistance – over and above that available to members of the community generally – needs to be rigorously justified and transitional in nature, and needs to facilitate appropriate change.
- As a complement to competition policy, governments may need to give more weight to social welfare and fairness issues when addressing matters such as tax, social security and labour market policies that are efficient means of achieving these goals.

Box 2 cont..

- Various NCP processes integrate economic and environmental considerations. For example, the NCP water reforms have ecological sustainability as a central objective and include measures to conserve water, improve river quality and address land salinity problems.
- NCP is not a form of 'economic rationalism', as commonly defined.

Further details are contained in Section A1.4 and Chapter A2.

PART A COMPETITION POLICY IN OVERVIEW

A1 IMPLEMENTING COMPETITION POLICY: PROGRESS TO DATE

The National Competition Policy (NCP) package contains a range of measures designed to reap the benefits that competition, properly harnessed, can bring. It involves some one-off changes to the Trade Practices Act that reduce the scope for market rigging, plus a range of reforms to:

- essential service industries (like transport and energy);
- government businesses (from local council garbage collection services to major electricity suppliers); and
- anti-competitive legislation (such as laws giving the legal profession a monopoly on conveyancing in Queensland).

NCP was adopted by the Commonwealth and all State and Territory governments in 1995 and they continue to be responsible for its implementation.

Because of the size of the package, implementation has been split into three stages or 'tranches'. The Council assesses each government's progress in meeting its reform commitments at the end of each tranche: that is, in July 1997, 1999 and 2001. There is also scope for follow-up assessments to deal with unresolved matters. These assessments are important because, to share the benefits of competition policy, the Commonwealth has agreed to make payments to the States and Territories, provided they make satisfactory progress in implementing the agreed policies. All up, these payments are worth around $16 billion over the period to 2005-06.

The Council has just finalised its first tranche assessments, and the progress to date has been positive. All governments have taken significant steps to meet their NCP commitments. Most of the early activity focused on getting the policy processes right. Many reforms have now also been implemented, with some promising early results. That said, both the Commonwealth and NSW governments fell short of fully meeting all their NCP obligations. However, apart from recommending a potential deduction from NSW's NCP payments in relation to one matter, the Council was able to recommend that all States and Territories receive their complete first tranche NCP payments.

But difficulties lie ahead. Political resistance to change has increased, and some governments have shown a reluctance to press on with certain reforms. To meet their second tranche commitments, governments will need to address these matters and to increase the rate of implementation. As part of this, governments will also need to examine their other policies to ensure that the potential benefits of NCP are fully realised.

In this chapter, the Council reviews progress with NCP to date and outlines its views on the task ahead.

A1.1 Improving the performance of essential service industries

Services such as energy supply, transportation, communications and water supply play a vital role in the Australian economy. They are major business inputs, essential services for consumers, and the industries that supply these services are major resource users in their own right.

NCP takes a two-pronged approach to improving these essential service industries:

- specific national agreements for reforms in the energy, water and transport sectors; and
- general 'access' regimes for all infrastructure services.

Energy

The NCP energy reforms are the furthest advanced. They seek to improve the efficiency of the electricity and gas industries, open these markets up to new businesses, and cut costs to energy users.

So far, in relation to electricity reform:

- most governments have corporatised or, in some cases, privatised their electricity utilities, to help prepare them for competition;
- several governments have also separated the generation, power lines and retail parts of their electricity systems, establishing new stand-alone bodies in each part;
- the first stage of the national electricity market commenced in May 1997, with direct trade between NSW, Victoria and the ACT, and indirectly with South Australia;
- Queensland has introduced a parallel competitive market in preparation for joining the national market, and Tasmania has also announced its intention to interconnect with the national system; and
- there has been considerable work to develop the national electricity code, with the Australian Competition and Consumer Commission (ACCC) granting conditional approval for the main part of the code in December 1997.

Similar measures have been implemented in relation to gas. The key reform completed during 1997-98 has been the finalisation of the national gas access code, with most governments passing legislation to implement the code by June 30.

Competition reform in these sectors is already paying dividends. Savings in electricity bills for customers eligible to choose their own supplier have averaged around 23 to 30 percent, and certain gas prices have fallen or will fall by 26 and 50 percent. Reductions of up to 60 percent have been experienced or foreshadowed in some instances (Box A1.1).

Governments are continuing reform efforts in these areas to ensure that the prospective benefits are reaped Australia-wide. For example:

- electricity price reductions should spread as competitive market arrangements expand to cover smaller consumers and as more states join the national market. After several delays, the full national market is now scheduled to commence in mid November 1998;

Box A1.1 Some recent changes in energy prices

- A survey by the Australian Chamber of Manufactures of businesses able to select their own electricity supplier under the national market found an average reduction in electricity bills of 30.6 percent in NSW and 23.2 percent in Victoria, with a maximum reduction of 60 percent. Almost 90 percent of the businesses surveyed considered that they were better off under competition (ACM 1998).
- A similar study of major businesses (Delloite 1998) found that 88 percent had achieved savings of more than 20 percent, with a quarter of firms saving more than 40 percent.
- A survey by NUS International (1998) indicated that electricity prices in Melbourne and Sydney for 'contestable' customers are half the national average and considerably cheaper than in 16 other industrial countries.
- Since the commencement of the competitive wholesale market in Queensland in March 1998, wholesale electricity prices have fallen by around 23 percent (QERU 1998).[a]
- In Western Australia, gas prices fell 50 percent for major industrial users after deregulation of the Pilbara market in 1995 (Barnett 1996); while transport tariffs on the pivotal Dampier-Bunbury pipeline will fall by around 26 percent between 1997 and 2000 under a transitional price path (Moran 1997, Farrant 1998).[b]
- Gas distribution prices in NSW are to fall by up to 60 percent in real terms by 2000 under an AGL access undertaking accepted by the NSW regulator in 1997 (IPART 1997).

a) Demand weighted spot prices were around $52 per MWh in March 1998, falling to approximately $40 per MWh by late August. Additional data supplied by QERU.

b) The transitional price path was adopted as an interim measure prior to applying the national code to the pipeline from 1 January 2000. The tariffs quoted are based on a load factor of 1.0 (98 percent probability of supply).

- some governments are considering restructuring and/or privatising their electricity utilities. While NCP does not require privatisation, it is important that utilities have the right structure to obtain the full benefits of electricity reform; and
- with significant reform now accomplished or in train in relation to the gas transportation chain, attention is being given to the 'upstream' sector where there is scope for greater competition between and within gas basins. An inter-governmental working group is currently examining this matter and developing reform options.

Other matters also need to be addressed. In relation to electricity, for example, there is a need to complete implementation of all the national market arrangements. In relation to gas, governments have proposed exemptions from the national code for some pipelines that may result in competitive prices being achieved more slowly in some parts of the nation than others, with consequences for regional economic development. The Council considers that any exemptions should be minimal and transitional in nature.

In view of the importance of the energy sector and the benefits proffered by reform, the Council will give considerable weight to progress in this sector when making its second tranche assessment. Energy reform is discussed in detail in Chapters B7 and B8.

Water

Water reform is another key part of NCP. Over $90 billion is presently invested in Australia's water infrastructure, but the water industry has significantly under-recovered costs. At the same time, regional variations in water quality and availability, and the environmental problems with Australia's river systems that have emerged in recent years, have focused attention on issues of sustainability and water use.

The NCP water reforms seek to address both the economic viability and ecological sustainability of water supply. They include reforms to water pricing, allocations and trading of water entitlements, the structure of water supply utilities, and appraisal processes for investment in new or extended rural water schemes.

Implementation is being phased in over five to seven years, to give people forward notice and time to adjust, and also because of the sheer size and complexity of the package.

So far, the scope and pace of reform appear to differ across Australia. Each government is taking a different approach to water reform and rates of progress vary. NSW and Victoria are the furthest advanced. Other governments have implemented fewer reforms or are still in the process of developing their approach. That said, all governments face a difficult task to meet the current timetable for reform.

Work to date continues to involve task forces of experts and government officials seeking to resolve complex policy issues and technical matters, as a precursor to implementation of parts of the reform package.

There have also been some tangible reforms, particularly in relation to urban water pricing and the structure of water supply utilities. Box A1.2 outlines some recent changes.

The Council recognises that water reform is a difficult area, and that the NCP agreements provide scope for governments to take different approaches. Because of these differences, it will be necessary for individual governments to discuss their approach with the Council early, to ensure that it will meet the NCP reform requirements. The Council re-emphasises the importance it attaches to water reform. It will give this area significant weight in its assessment of governments' progress during the second tranche. Water reform issues are discussed more fully in Chapter B9.

Box A1.2 Some recent water reforms

- In NSW, a two-year price path for bulk water charges has recently been announced. Prices for bulk water will rise by between 13 and 26 percent over the period 1998-2000 (IPART 1998). The changes will reduce the under-recovery of costs and bring NSW prices closer to those applying in neighbouring states.
- Also in NSW, a limit of around 10 percent of annual diversions has been reserved for the environmental integrity of key rivers for 1998-99 (NSW Department of Land and Water Conservation 1998).
- Reforms introduced by Victoria in January 1998 entail an average 18 percent reduction in water prices for consumers across the State (Victorian Office of the Premier 1997).
- In Queensland, ten of the seventeen largest local councils have implemented two-part tariffs for water resulting in 20 percent average reductions in water usage in the first year (Marsden Jacob 1997).

Land transport

The NCP program also covers road transport. There is already significant competition in the road transport industry itself, so the reforms are focusing on matters such as national licensing requirements for heavy vehicle operators, road pricing and vehicle standards. The National Road Transport Commission estimates that full implementation will benefit the Australian economy by around $450 million per year (NRTC 1996).

However, progress to date has been limited, with only one of six modules agreed to in 1991 having been implemented. There has been considerable work in relation to some of the other modules, but national implementation has been hampered by difficulties perceived with the 'template legislation'

approach that was originally proposed, as well as by the lack of a concrete timetable for reform. In the lead up to its second tranche assessment, the Council is seeking agreement on a reform timetable and will be looking for further progress towards implementation.

While rail reform is not formally covered by the NCP agreements, there has been significant pressure for change resulting from the operation of the NCP 'access' regime (discussed in the next sub-section). This has proven to be slower and more cumbersome than if a national approach had been taken, and does not address various 'non-access' issues, such as the problem of different safety systems and operating procedures in different States.

Recognising this, during 1997-98 Australia's Transport Ministers have agreed to a range of measures to address these problems and to provide a 'one stop shop' for national rail operators. Rail is an important transport mode, particularly for bulk commodities and rural communities, and recent competition has resulted in some freight rate reductions of up to 40 percent (see Box A1.3). This indicates the benefits available from robust rail reform, and highlights the need to quickly push ahead. The Council endorses this new national approach.

Land transport reforms are discussed in detail in Chapters B10 and B11.

Box A1.3 Some recent reductions for rail freight rates

- Rail freight rates for grain in Western Australia have fallen by 21 percent in real terms since deregulation in 1992-93 (WA Government 1998, 161).
- Freight rates for the Perth-Melbourne route fell by around 40 percent, and service quality and transit times improved, following the introduction of competition in 1995 (NCC 1997a, 180).
- Coal freight charges in the Hunter Valley fell by 25 percent between 1995-96 and 1997-98, and are scheduled to fall further to reflect a 10 percent reduction in rail access charges in 1998-99 (see Box B12.5).

Access to other infrastructure services

The NCP package includes an 'access' regime to allow businesses to use essential services provided by other businesses' infrastructure facilities. For example, a transport company may be able to gain access to a rail network and operate its own trains, in competition with the existing train operator. The regime also seeks to ensure that access is provided on 'reasonable' terms and conditions, like a fair price.

The Commonwealth, States and Territories have already established several access regimes, dedicated to specific infrastructure services such as telecommunications networks, gas pipelines and shipping channels, and they are developing others. For nationally significant infrastructure services not covered by other effective access regimes, the NCP package provides a generic national regime. The Council has a role in approving State and Territory access regimes and handling applications from businesses that want to obtain access rights under the national regime (see Chapters A3 and B12).

To date, most use of the national arrangements has been in relation to rail transport. As mentioned earlier, the lack (until recently) of a national approach to rail reform has forced many freight businesses, seeking to compete with existing government train operators, to use the access provisions.

The Council has recommended that several services be 'declared' for access, although most of these matters have been appealed to the Australian Competition Tribunal. The Tribunal is yet to hand down a substantive decision.

While delays of this nature are part and parcel of testing a new law, in several cases the threat of imminent declaration appears to have forced the pace of change. For example, after appeals have been lodged, some businesses that applied for access have been able to strike private deals with infrastructure owners where they were previously unable to (see Section B12.3).

At the same time as these developments in access, there has been evidence that the prospect of access to previously locked-up markets is supporting investment in infrastructure, and that access arrangements are not causing

undue uncertainty for infrastructure owners (see Section B12.3). These were matters of concern when the access arrangements were being developed.

Overall, while there have been some early delays, the access reforms proffer the benefits of greater competition and better utilisation of Australia's infrastructure. Chapter B12 provides the details.

A1.2 Reforming government businesses

As part of NCP, governments are reforming their significant businesses in three ways:

- by restructuring them;
- by making them compete on an equal footing with private businesses; and
- by monitoring their prices where the businesses retain monopoly power.

Structural reform

Governments have undertaken wide-ranging structural change of their big, monopolistic enterprises. For example:

- NSW has broken up its State Rail Authority into seven smaller entities, each specialising in a particular facet of rail operations; and
- Victoria has restructured its port operations, putting responsibility for shipping channels in one body, and other wharf functions, which are amenable to competition for private businesses, elsewhere.

In some cases, governments have gone further than is required under the NCP agreements and privatised some of their businesses.

In making these changes, governments have generally applied the principles for structural reform in the NCP agreements. They have separated regulatory functions from business roles, and reviewed the commercial objectives and structure of their monopoly businesses before privatising them or exposing them to competition. In some cases, however, the Commonwealth has not undertaken explicit reviews to meet these requirements. Chapter B5 contains the details.

Competitive neutrality

The 'competitive neutrality' measures are also progressing. In essence, competitive neutrality seeks to ensure that competition between public and private businesses happens on a fair basis, by making sure they face the same taxes, incentives and regulations. 'Corporatisation', 'commercialisation' and 'full cost pricing' are some ways competitive neutrality can be introduced into government businesses.

To date, governments have corporatised or commercialised many of their businesses, and are progressively introducing pricing reforms to many others. Further, all governments have also established units to deal with any complaints about unfair advantages enjoyed by particular government businesses, as is required under the NCP agreements.

While genuine progress has thus been made, governments will need to give several matters special attention in the period ahead. These include:

- ensuring that the competitive neutrality principles are applied to all significant government business activities;
- progressing reform at the local government level, where implementation to date has been hampered by several matters;
- the application of prices that reflect a full attribution of costs; and
- the independence, scope and powers of units established to deal with complaints from private businesses that feel government competitors retain an unfair advantage.

These matters, and progress with competitive neutrality generally, are discussed in detail in Chapter B4.

Price monitoring

Where government businesses retain monopoly power, the NCP calls on governments to consider having their prices scrutinised by an independent body. Most governments have indicated compliance with this requirement, and a number of government business are subject to prices scrutiny (see Chapter B6).

These types of changes to government businesses — many of which predated the NCP agreements — appear to be delivering positive results (see Box A1.4), although factors such as technological change may also help explain the recorded improvements.

Box A1.4 Recent performance of government businesses

The Standing Committee on National Performance Monitoring of Government Trading Enterprises (1997) found improvements in the performance of government businesses over the four years to 1995-96. While the outcomes have varied between the enterprises studied, overall there were:

- improvements in labour productivity;
- a doubling of total payments to governments;
- average price reductions of around 15 percent; and
- limited improvements in service quality.

A1.3 Reviewing anti-competitive legislation

As part of the NCP, governments have agreed to review and, where appropriate, reform all their laws that restrict businesses from competing for the consumer dollar. The program covers almost 2000 pieces of legislation. It also entails mechanisms to vet new or amended regulations to ensure that they do not unduly restrict competition.

The guiding principle for reviews is that legislation should not restrict competition unless it confers an overall community benefit and its objectives cannot be obtained in other ways.

The NCP agreements list a range of public interest matters that must be taken into account in assessing the benefits and costs of a restriction, including the environment, employment, regional effects, consumer interests and the competitiveness of business.

While the early work revolved around developing review schedules and processes, the pace of undertaking reviews has picked up in the last year. The Council estimates that, by July 1998, governments had completed more than 300 reviews with a similar number underway. This compares with a total of around 100 State and Territory reviews completed as at March 1997. The outcomes of some early reviews are set out in Box A1.5. However, governments are yet to implement decisions in response to the recommendations of many of the recent reviews, and in cases where governments have implemented changes, there generally has been insufficient time to gauge their precise effects.

There was some slippage with implementation during the last year at the Commonwealth level. It did not implement the recommendations of an independent review of the textiles, clothing and footwear industry, without providing a public interest justification consistent with the NCP agreements. The Commonwealth has also announced its decision to not implement the full recommendations of the Council's recent review of postal services, although the details of the Commonwealth's approach are yet to be finalised. As well, in a number of cases, the Commonwealth has enacted new legislation that restricts competition, without providing evidence that the legislation has been rigorously tested against the NCP principles. That said, the Commonwealth has undertaken to address most of these matters.

Box A1.5 Some outcomes of early legislation reviews

- The Commonwealth rationalised prudential regulation, strengthened financial disclosure requirements and created a new 'payments system board' within the Reserve Bank, following the 1997 Wallis review of the financial system.
- Following a review of 250 business licences in NSW that revealed significant overlap and unnecessary regulation, 72 licenses have been abolished (as at 1 January 1998), with a further 13 nominated for possible repeal. Among other changes, 44 categories have been collapsed into just three.
- In Victoria, a 1997 review of physiotherapy regulations recommended the removal of restrictions on practice, the retention of registration requirements and the introduction of compulsory professional indemnity insurance.
- Following a 1997 review, the Queensland Government repealed legislation that gave the Queensland Coal Board 'reserve powers' to compulsorily acquire coal, set prices and regulate aspects of mines. It also removed live requirements that certain coal users buy from specified mines.
- In Western Australia, the legislation giving statutory marketing powers to Western Australia's Dried Fruits Board was not found to be in the public interest and is to be repealed.
- In South Australia, a review found that while aspects of the Water Resources Act are restrictive, they generate net benefits by mitigating the risk of environmental degradation and disputes over water usage. It therefore recommended that they be retained.
- In the ACT, restrictive and discriminatory trading hours legislation was repealed in 1996 after a preliminary examination suggested that the costs to the community clearly exceeded the benefits.

Source: Jurisdictions (1998 legislation review schedule updates and information supplied to the Council).

Likewise, the NSW Government did not implement the recommendations of an independent rice industry review to end the domestic marketing monopoly. Nor did it provide a bona fide public interest justification for non-implementation. In its July 1998 supplementary first tranche assessment, the Council recommended a deduction of $10 million from NSW's NCP payments if appropriate reform is not undertaken before February 1999, as recommended by an independent review in 1995. The Council, NSW government officials and industry representatives are currently working to resolve this matter (see Section B3.5).

At a more general level, based on the Council's experience with the legislation review program to date, governments will particularly need to address three broad areas if they are to fully meet their second tranche commitments:

- the scope of their legislation review programs;
- review processes, including the need for appropriately scoped terms of reference, independent review panels, rigorous analysis and opportunities for public input; and
- the implementation of review recommendations, except where a bona fide public benefit justification can be demonstrated.

Chapter B3 discusses the details of these and other legislation review issues.

A1.4 Addressing the broader policy mix

Beyond the need to progress the NCP reforms, the Council considers that governments may need to address other aspects of their overall policy mix if the potential benefits of competition policy are to be fully realised.

Competition policy can play a major role in enhancing the performance of the economy. Its strength lies in improving productivity and economic efficiency. This can directly improve people's material living standards and, in conjunction with other measures, enable the attainment of the community's social and environmental goals.

However, implementing competition policy alone does not guarantee these outcomes. Competition necessarily entails losers as well as winners, particularly in the short term. And whether or not the potential benefits of competition reform are realised in full, shared equitably, and put to the best use will depend on other government policies and economic conditions.

As the Council noted in its last Annual Report, if these other areas are not adequately addressed, people may simply equate competition policy and micro-economic reform with job losses, breakdown in communities, reduced government accountability and impaired environmental quality.

The Council went on to discuss four sets of implications:

- the need for specific, ongoing action to address issues such as social justice, the environment, tax reform, education and labour market reform;
- the need for governments to revisit the issue of adjustment assistance for both individuals and communities that are affected by economic reform;
- the need for governments to ensure that they do not use competition policy processes to introduce inappropriate reforms; and
- the need for governments (and the Council) to clearly and accurately explain to the community the interface between the competition reforms, other aspects of government policy, and overall community objectives.

The importance of addressing these matters has increased in prominence over the last twelve months. The Council adds to its comments from last year's report in the following chapter.

A2 UNDERSTANDING COMPETITION POLICY AND ITS PLACE IN THE POLICY SPECTRUM

Recent public debate has revealed widespread confusion about competition policy and how it ties in with other government policies. For example, it has been suggested that the NCP agreements require certain policy actions such as repealing all anti-competitive legislation or privatising government businesses. Conversely, NCP is sometimes thought to preclude certain policy actions by governments, such as subsidising community services. More generally, there exists a concern that NCP is a form of 'economic rationalism' which focuses on money, markets and materialism with no regard for equity, the environment or the social fabric.

These concerns stem in part from limited awareness of the public interest safeguards built into the NCP processes. For example, when reviewing anti-competitive legislation, governments must explicitly consider the effects of reform options on an array of public interest matters. These include the environment, employment, social welfare and consumer interests, as well as business competitiveness and economic efficiency. These matters are also relevant when assessing the merits of applying competitive neutrality to particular government businesses or reforming the structure of public monopolies (see Box A2.1).

The concerns about competition policy also stem from limited awareness of what the NCP program actually requires of governments. For example, NCP does not require privatisation, contracting out, or cuts in subsidised community services.

But while NCP does not require many of the policy actions attributed to it, governments do need to address other elements of their policy mix if the benefits of competition policy are to be fully realised, equitably shared and put to the best use.

As noted earlier (Section A1.4), the Council discussed some of these matters in its last Annual Report. In this chapter, the Council elaborates on those comments, as well as discussing the more general issue of the relationship between NCP and other elements of government policy.

Box A2.1 The NCP public interest test

Clause 1(3) of the Competition Principles Agreement (CPA) requires governments to consider the following matters when assessing the merits of possible reforms in relation to competitive neutrality, anti-competitive legislation and the structure of public monopolies:

- government legislation and policies relating to ecologically sustainable development;
- social welfare and equity considerations, including community service obligations;
- government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;
- economic and regional development, including employment and investment growth;
- the interests of consumers generally or of a class of consumers;
- the competitiveness of Australian businesses; and
- the efficient allocation of resources.

The list is open-ended, meaning that governments must also take into account any other matter relevant to determining the merits of the reform being examined.

By way of example, the NCP competitive neutrality principles require that significant government business activities price their services at full cost where appropriate. Some private businesses have lodged complaints regarding products made by prison-based businesses being sold at below cost.

In such cases, governments need to weigh the benefits of facilitating competition between private and public providers against social objectives such as fewer repeat offences, lower containment costs and higher prisoner quality of life. NCP provides for exemptions from competitive neutrality principles where the community benefit arising from these factors outweighs the benefit from greater competition.

A2.1 Competition policy and economic measures[1]

Privatisation

The term 'privatisation' refers to the process of selling a government-owned entity to the private sector.[2]

Privatisation is one of several options from which governments can choose to meet the NCP requirement of applying 'competitive neutrality' principles to significant government business activities. Other options include corporatisation, commercialisation and full cost pricing (see Chapter B4).

Importantly, NCP does not require privatisation. The NCP agreements leave it to governments to determine whether privatising a particular government business is warranted in the circumstances. And where a government chooses to privatise a public monopoly, NCP requires the government to undertake a review first with the aim of ensuring, among other things, that the right competitive environment is in place.

Hence, any decision by governments to privatise a public asset reflects a policy decision of the government in question — not a requirement of NCP.

That said, the Council recognises that elements of the NCP package may add to pressures for the privatisation of some government businesses. For example, the introduction of competition into a particular market may make

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1 For convenience, this chapter divides issues into three main categories: 'economic', 'social' and 'environmental'. The Council recognises that this classification is somewhat arbitrary. For example, all of the matters discussed in Sections A2.2 and A2.3 could be deemed economic, and many of the matters discussed in Section A2.1 have a social and/or environmental dimension.

2 The term is sometimes given a wider meaning, to include matters such as 'deregulation' and 'contracting out'. However, there is not necessarily any relationship between these matters. For example, it is possible, and sometimes sensible, to increase the level of regulation applying to a firm that is to be privatised, particularly if it is a public monopoly. Likewise, contracting out can be undertaken by private or publicly-owned businesses, and the firm that wins the contract may be a private or public business.

it more volatile. This is happening under the NCP electricity market reforms, for example. In such circumstances, governments may consider it sensible to privatise their businesses rather than exposing tax-payers' dollars to the greater risk by maintaining those businesses in public ownership.

However, it is still up to individual governments to decide whether privatisation is warranted, and there will be cases in which this is unlikely. Privatising any particular publicly-owned business will not necessarily confer an overall community benefit. Consequently, the merits of privatising businesses need to be assessed on a case-by-case basis.

Deregulation

While the Council is unaware of any formal definition of 'deregulation', its most literal and common meaning is a process by which the government regulation applying to an entity, industry or market is reduced or eliminated.

The NCP measure that is likely to have most impact on the level of regulation in Australia is the legislation review program. Under the program, all legislation that restricts competition is to be reviewed and where appropriate reformed by the year 2000. The guiding principle is that legislation should not restrict competition unless it confers an overall community benefit and its objectives cannot be obtained in other ways. Some 2000 pieces of legislation are scheduled to be reviewed.

Several legislative restrictions on competition have been abolished or pared back under the program. Examples include trading hours restrictions in Victoria and the ACT, certain business licensing requirements in NSW, and vehicle licensing requirements contained in the Tasmanian Traffic Act. In some cases, these laws have been deemed to be unnecessary or inappropriate. In others, the legislation review process has determined that the broad objective of the law is appropriate, but that reforming the law would allow the objective to be achieved in a less costly and/or less restrictive way.

At the same time, several legislative restrictions have also been retained. Examples include aspects of the South Australian Water Resources Act and Liquor Licensing Act, the 'single export desk' arrangements in the NSW rice industry, and registration arrangements for physiotherapists in Victoria.

Hence, the NCP legislation review program is not about competition for competition's sake, nor does it necessitate deregulation. Rather, anti-competitive legislation is subject to a public interest test to determine whether it should be retained, refined or repealed.

Other elements of the NCP program entail an increase or enhancement in regulation. For example:

- Part IV of the Trade Practices Act has been amended to extend the scope of its anti-competitive conduct provisions (although this change itself reduces the need for some other existing regulation);
- a new regulatory regime has been included in Part IIIA of the Act to give businesses 'access' to certain infrastructure services;
- under the NCP agreements, before privatising a public monopoly or exposing it to competition, governments are required to undertake a review to ensure, amongst other things, that the regulation applying to the market is appropriate;
- the NCP water reforms require, among other things, that investment in new or extended rural water schemes be undertaken only after appraisal indicates that it is economically viable and ecologically sustainable; and
- the NCP electricity and gas reforms have involved significant regulation to allow competitive markets to proceed.

Some of the increase and enhancement in regulation, or retention of existing regulation, under NCP stems from the fact that all markets require basic regulatory ground rules to operate efficiently and some markets require

additional regulation. Additional regulation may be necessary to overcome forms of 'market failure'[3] or 'inequity'.

Overall, the NCP program entails a reduction in regulation in some cases, the modification of regulation in other cases, and an increase in regulation in other cases. And where the NCP agreements do result in a reduction in regulation, this reflects the outcome of an assessment of the regulation against a public interest test.

Industry policy

Industry policy is commonly used to refer to government interventions in markets to boost the performance of industry. Within this definition, it is possible to identify two broad schools of industry policy:

- one concerns itself with correcting problems in the economic framework within which business operates; and
- the other concerns itself with targeting specific sectors, industries or businesses, and directly assisting them by using either protectionist policies or, more progressively, policies aimed at cultivating leading edge industries.

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3 The term 'market failure' refers to features of a market that mean that its unfettered operation will lead to economically inefficient outcomes. Common examples include:

- 'cognitive limitations' and 'imperfect information', such as the problems consumers face in attempting to discern the quality of certain professional services;
- 'externalities' or 'spillovers', such as greenhouse gases emitted into the atmosphere as a by-product of a firm's production processes;
- markets with 'natural monopoly' characteristics, such as rail networks, in which it would be wasteful to have two tracks competing side-by-side; and
- 'public goods', such as parks and defence, where it is difficult or not sensible to directly charge individuals for the service provided.

Factors such as persuasive advertising, addiction and peer group pressure, that distort people's preferences, are also sometimes classified as leading to market failure (see IC 1994, 197-198).

Where substantive market failure exists, economic theory indicates that government intervention can improve on market outcomes, provided that the costs associated with the government intervention do not exceed the costs associated with the original market failure. Regulation is one way that this may be achieved.

An example of the first school of industry policy is government support for research and development (R&D). Conventional economic thinking recognises that markets, left to their own devices, will not provide enough incentives for businesses to invest in R&D. This is because an individual business will not capture all the benefits of its research — often, other companies will be able to benefit too. Because of this market failure, there is a strong economic case for governments to intervene in markets to encourage more R&D than there would otherwise be. Assistance for businesses undertaking R&D is therefore one element of a framework approach to industry policy.[4]

This first school of industry policy and the NCP program are natural complements. Both aim to address the economic framework within which businesses operate, although there are some differences in the way they do this. For example, the legislation review program seeks to improve the economic framework largely (but not solely[5]) by removing inappropriate government intervention in markets, whereas the first school of industry policy seeks to do this by adding necessary government intervention to augment market incentives. As noted earlier though, other elements of competition policy also add necessary government intervention to improve the economic framework within which business operates.

The second school of industry policy directs government assistance to selected firms or industries. Examples include establishment subsidies for foreign firms, and industry plans and associated measures, such as tariffs, designed to achieve output or employment targets in the selected industry.

This type of intervention might be warranted where, for example, a critical mass of industry is required to provide the synergies necessary for particular

4 This is not to imply that any government policy to encourage additional R&D will be warranted. There will come a point when measures to increase R&D involve more costs than benefits, and some measures will be a more efficient means of encouraging R&D than others. However, from an economic viewpoint, there are solid grounds for some level of government intervention in markets to encourage R&D.

5 As noted earlier, where legislation that restricts competition is found to confer a net community benefit that cannot be obtained in other ways, it is to be retained under the legislation review principles. Reviews may also recommend refinements to existing anti-competitive legislation, and it is plausible that an NCP review may find insufficient intervention to address a particular market failure and recommend an increase.

types of industrial development, or where there are technological 'spillovers' associated with a specific firm or industry.

In such cases, selective industry support would be consistent with the NCP principles provided that the mechanism used to deliver the industry support:

- does not restrict competition; or
- restricts competition but delivers an overall community benefit that cannot be attained using mechanisms that do not restrict competition.

That said, many proposals for selective assistance that rely on restrictions on competition may fail the latter test. This is because assistance to one industry can come at the expense of more productive industries, to the detriment of the economy as a whole.[6] The effects of globalisation also limit the effectiveness of traditional measures for providing selective assistance.[7] And even if selective assistance were judged to provide a community benefit such as increased employment, it is likely that more targeted measures, such as specific labour market programs, that do not restrict competition could also achieve this benefit.

Nevertheless, where selective assistance is provided to a firm or industry, its effects will be amplified by the pursuit of NCP reforms within the economy generally. This is because, as well as benefiting from its special assistance, the selected firm or industry will also be able to capture the benefits of lower input costs and/or higher consumer spending power resulting from the NCP program generally.

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6 For example, a tariff on imported products would push up the price of those products and therefore the price domestic producers can charge. This could result in an increase in employment and output in the protected industry. However, higher prices would increase the costs of other industries that use the protected products as inputs in their own production processes. Higher prices would also leave consumers less to spend on other industries' goods and services.

7 The international mobility of capital in today's global economy means that assistance provided to attract or retain capital may have a limited or temporary effect. Once market demand for the output produced by the capital decreases, or the assistance provided is reduced or removed, or overseas sites become more attractive, 'footloose' capital is likely to move off-shore. These problems also apply to non-selective attempts to attract international capital, and add to the case for directing public resources away from industry incentives and towards workforce skills, education and infrastructure, that are likely to remain in Australia long-term. (See Latham 1998, 43-49).

Hence, while certain industry policy initiatives may be inconsistent with the NCP principles, the NCP reforms generally act as a complement to industry policy measures.

Economic growth

'Economic growth' refers to increases in national income or output, and is commonly equated with changes in gross domestic product (GDP).[8]

NCP does not aim to increase economic growth *per se*. Rather, the main thrust is to use society's resources — that is, people's skills and labour, land and capital — in more efficient and sustainable ways, thereby increasing the value that society obtains from those resources. 'Value' in this sense refers not only to money values; it also refers to other things people value, including leisure and environmental amenity.

The focus on efficient and sustainable resource use is reflected in various parts of the NCP. For example:

- the objective of the competitive neutrality component is "the elimination of resource allocation distortions" (CPA clause 3(1));
- the NCP water agreements focus on the "efficient and sustainable reform of the Australian water industry" (COAG 1994); and
- one of the aims of the electricity reforms is "the most efficient, economic and ecologically sound development of the electricity industry…" (SPC 1991).

The NCP legislation review principles have a slightly different focus. The key principles are that anti-competitive restrictions are to be retained only if

8 Changes in GDP are a narrow measure of economic growth and community welfare. Argy (1998, 13-20) provides a recent critique of the use of GDP as a measure of community welfare. Some time ago, the Treasury pointed out that "some of the alleged conflicts between economic growth and other goals only arise if the substance of growth is identified with its conventional statistical shadow" (Commonwealth Treasury 1973). Broader definitions of income, and thus of economic growth, see it as including matters such as unpaid work, environmental amenity and leisure — not just how much money people earn or spend.

the benefits (broadly defined) from doing so should exceed the costs (broadly defined), and if the legislation's objectives cannot be obtained without restricting competition. The "efficient allocation of resources" is one matter that reviews must take into account as part of the community benefit-cost test, and the principles will tend to promote economically efficient outcomes. However, there is also scope for reviews to trade off efficient resource use for other considerations, such as equity, when assessing the case for reform.

While the reforms focus mainly on efficient and sustainable resource use, their implementation is generally likely to bring or allow higher economic growth. For example, by cutting energy costs, the electricity reforms are likely to result in an expansion in the employment and output levels of industries that use energy in their production processes. Provided this expansion exceeds any contraction in the electricity industry itself, economic growth should increase. At a more general level, competition can drive greater innovation, itself an important factor in growth. And as discussed in the Council's 1996-97 Annual Report, NCP should also increase the rate of growth the economy can sustain in the long-term.

However, it is possible that some of the reforms will reduce economic growth, at least as measured by changes in GDP. For example, under NCP, some water prices are being increased partly to help protect the environment. Higher water prices may reduce the incomes of certain water users which, in turn, could reduce GDP. This reflects the fact that NCP focuses on efficient and sustainable resource use, rather than economic growth (narrowly defined).

More generally, while most of the NCP measures offer the potential for higher growth, the actual level of growth attained depends on factors other than just NCP. Growth depends not just on the productive potential of particular resources. It also depends on the extent to which, and speed with which, resources displaced through economic change are redeployed in other productive pursuits. This in turn depends partly on governments' macro-economic policy settings and other policies such as labour market arrangements, welfare policies and adjustment assistance. More broadly, 'new growth theories' suggest that long-run economic growth is driven by technological progress. These theories emphasise the importance of generating knowledge through education, training and R&D, and investment in equipment and infrastructure (Romer 1986; Lucas 1988). Similarly, work

on long-run competitiveness stresses the importance of 'human capital' and skills training (Porter 1990).

Consequently, NCP needs to be seen as just one element of a suite of policies governments need to pursue if seeking to increase economic growth.

A2.2 Competition policy and social measures

Equity

While the Council is unaware of any universal definition of 'equity', it is often used to refer to the fairness of the distribution of society's resources and opportunities among its people.[9] Improving equity is an important goal of many societies and the NCP agreements explicitly refer to equity as one matter that must be considered when assessing the merits of competition reforms.

In practice, most NCP reforms will affect equity either directly or indirectly, and they are likely to have a range of effects.

9 Determining what constitutes 'equity', or whether one situation is more equitable than another, requires a value judgment about the basis for deciding what is fair. Sen (1973) points to 'need' and 'desert' (or 'merit') as the major categories of such judgments. In practice, the level of equity depends on matters such as the extent to which: all of society's citizens have access to life's basic entitlements, to a level appropriate to the sophistication of the society; there is a fair distribution of monetary income and wealth between people; all people who want gainful employment can obtain it; there is scope for people to influence their socio-economic circumstances; people in similar circumstances are treated equally; people can pursue their goals without undue impediments such as discrimination; and current generations do not impose undue burdens on future generations. See for example Glennerster (1995), Richardson (1995), and Argy (1998).

At a broad level, implementation of the NCP reforms should improve 'horizontal' equity[10] by ensuring that the disciplines of competition are shared more evenly across society. At present, some groups do business from behind anti-competitive arrangements, which can allow them to maintain their incomes, or work and lifestyle conditions, at levels higher than they otherwise could. The legal profession's monopoly on conveyancing in Queensland may be an example of this (see Box A2.2), as may be the controls applying to certain medical specialists (see Box A2.3). Meanwhile, people in otherwise similar circumstances do not enjoy these privileges. One principle of NCP is that restrictions on competition should be maintained only where they confer an overall community benefit, rather than simply providing privileges for the sheltered group at the expense of others.

As well as improvements in horizontal equity, some NCP measures will also bring about general improvements in 'vertical' equity — that is, the gap between the rich and the poor. For example, as noted earlier, the energy reforms are bringing substantial reductions in electricity and gas prices. These will cut consumers' power bills. As low-income households spend a larger proportion of their incomes on energy than households on high incomes, these reforms should bring a coincidental improvement in equity.[11]

However, improving equity is not the central focus of the NCP package. Rather, the NCP agreements simply require that all competition reviews consider "social welfare and equity considerations" when assessing the case for reform. While this will tip the scales in favour of decisions that enhance equity, in practice reforms are likely to have a range of effects on equity — some good, some bad.

10 'Welfare economics' distinguishes between 'vertical' and 'horizontal' equity. Vertical equity refers to the fairness of the treatment of people in different circumstances, such as different income brackets. Horizontal equity refers to the fairness of the treatment of people in similar circumstances. For example, under the value judgment that disparities in wealth are inequitable, a policy that taxed all the rich but subsidised only some of the poor would improve vertical equity (between the rich and the poor) but would worsen horizontal equity (among the poor). (Ng (1983, 159) and Quiggin (1996, 43-44) discuss some limitations).

Importantly, however, equity need not imply equality. Nor does it always imply the equal treatment of people on the same monetary income. For example, members of a particular social group that suffers entrenched discrimination may have difficulty obtaining employment or promotions relative to other people with the same skills and workplace

Box A2.2 Conveyancing restrictions

Under Queensland's *Legal Practioners Act 1995*, conveyancing is restricted essentially to members of the legal profession.

Similar restrictions used to apply in most other states and territories, but have been removed over recent years. In NSW in the early 1990s, the market was opened up to non-lawyers with appropriate qualifications, and fees scales and advertising restrictions were removed. Conveyancing fees subsequently fell by 17 percent resulting in a saving to NSW consumers of at least $86 million (Baker 1996).[a]

In other words, these restrictions had effectively boosted the incomes of members of the legal profession, but at the expense of consumers and others wishing to compete for their custom.

The Queensland restrictions are to be reviewed under the NCP legislation review program. This review will need to determine, among other things, whether there is a public interest justification for restricting competition in conveyancing services and, if there is, whether community objectives can be achieved in less restrictive ways, such as the approach taken in NSW.

a This figure is based on the size of the NSW conveyancing market in 1992-93, converted to 1996 dollars. However, the study notes that the market has increased in both volume and size since then, suggesting that the savings estimate is conservative (Baker 1996, 37).

performance. For members of the discriminated group to achieve the same income as other people, the implication is that they generally will have had to work harder. On 'desert' grounds, therefore, governmental equity measures that provide additional benefits to members of the discriminated groups, relative to other people on the same monetary income, may be warranted.

11 While household power bills are likely to fall as a result of the NCP energy reforms, it should be recognised that cross-subsidies are also being phased out, meaning that business customers will receive more direct benefits than households. Larger businesses are also likely to obtain greater cost reductions than smaller businesses. That said, lower prices for business inputs can be expected to lead to a reduction in their prices and/or an expansion in their sales, and thus in their demand for labour. This in turn will benefit households, particularly the less well-off.

Box A2.3 Controls on entry into specialist medical professions

Medical 'colleges' typically set numerical restrictions on who can train to become a medical specialist.

In a report to the Australian Health Ministers that drew on Department of Health data, Paterson (1994) argued that supply restrictions have inflated average incomes in several medical specialties. For example:

- the ratio of cardio-thoracic surgeons to the population size had been held well below the target set by governments. Cardio-thoracic surgeons earned almost $400 000 per annum, with the top 25 percent of surgeons grossing almost $700 000 per annum;
- the top quartile of orthopaedic surgeons earned approximately $400 000 per annum, with high co-payments indicating market power; and
- shortages of opthalmologists helped top quartile earnings to nearly $600 000 per annum.

Paterson also found prima facea evidence that supply restrictions had caused an extension in public hospital waiting lists.

Following Paterson's report, the Australian Health Ministers established the Australian Medical Workforce Advisory Committee within the health portfolio, to address issues of appropriate supply on a case-by-case basis.

As part of NCP, those State-based legislative restrictions that exist on entry and practice in the medical profession are scheduled for review. As well, Part IV of the *Trade Practices Act 1974* – which deals with anti-competitive business behaviour – has been extended to cover the activities of, among other things, medical partnerships.

For example, it is likely that some reviews of anti-competitive legislation will find that reforming the legislation would improve equity. Under the NCP's community benefit-cost framework, this would count as an additional benefit of reform and would thus add to the case for it.

On the other hand, some reviews may find that a reform would worsen equity. This could occur if, for example, a reform would cause job losses in an already depressed area that would not be sufficiently offset by more jobs elsewhere.[12] This would count as a cost under the NCP's community benefit-cost framework, and would tip the scales in the other direction — that is, against reform. If, however, the review still judged that the community benefits of reform exceeded the costs, including the costs of the reduction in equity, reform would still be appropriate.

Where a reform, while providing an overall community benefit, will adversely affect a particular group, industry, or community, governments should provide appropriate adjustment assistance to equip people to cope with change. (The issue of adjustment assistance is discussed further in the next sub-section.)

That said, the Council considers that governments may also need to address the issue of equity more comprehensively and directly and, indeed, see it as a concomitant requirement to the implementation of competition policy and like reforms.

One reason is that, as the Council noted in its last Annual Report, failure to adequately address social justice (and other) policy areas could result in people simply equating competition policy and micro-economic reform with, among other things, job losses and breakdowns in communities. The Council

12 The Council discussed the implications of NCP reform for employment in its 1996-97 Annual Report. In brief, NCP reforms will add to both the generation and elimination of jobs that occur as part of normal economic activity. While there are reasons to believe that the net effects on employment of the NCP program will be positive, the Council emphasised that higher employment is not the primary aim, nor an automatic outcome, of competition reform. It noted, rather, that to seriously tackle problems of unemployment, governments also need to address other elements of their policy mix, including labour market programs and education (NCC 1997a, 32-34).

noted that this in turn could reduce the impetus for broadly-based competition reform. Recent events add weight to this view.

But beyond these recent developments, the changing nature of our economy and society suggests to the Council that the role for government to address equity is increasing.

First, there is evidence of a greater dispersion of incomes and opportunities among people as we move to a so-called 'post-industrial' or 'information age' society. Work relying mainly on intellectual skills is generally attracting higher rewards compared with other forms of work. Meanwhile, people relying on other forms of work are generally losing ground (Reich 1991, 208-224).[13] This greater dispersion arguably increases the case for greater efforts to redistribute from the rich to the poor, to promote social cohesion as well as for equity itself.

Second, there is evidence that, as society's materialistic wealth increases in aggregate, the benefits derived from additional increases are lessening. At higher levels of wealth, people's wellbeing appears to depend less on how much wealth they have in an absolute sense, and more on how much they have relative to those around them. While individuals can improve their own wellbeing by increasing their wealth, this comes at a cost to other people's wellbeing (Hirsch 1976; Oswald 1997). While this evidence has implications for government policy beyond the matter of equity[14], it also indicates a need for governments to give more attention to equity compared to the issue of increasing aggregate wealth.

There are limits on the extent to which these problems can be addressed. For example, governments' ability to raise taxes on the wealthy to address equity is constrained to some degree by the effects of globalisation. In particular, beyond some point, increasing taxes on the wealthy or on corporations may result in the movement of some people and projects off-shore. Further,

13 Reich discusses these trends with reference mainly to the United States. In the Australian context, Harding (1997) reports that that the dispersion in monetary incomes in Australia arising from market outcomes — that is, before considering the effects of governmental redistributive policies — has been increasing since at least the early 1980s.

14 For example, Frank (1997) indicates that relative consumption effects can justify government intervention to reallocate resources from consumer goods towards other uses such as health and leisure.

because Australian's materialistic expectations partly depend on the material living standards of foreigners, measures which curtail increases in our material living standards will still come at a cost to our collective sense of wellbeing.

However, these concerns would need to be weighed against the benefits that a greater focus on issues such as equity would bring.

In addressing equity, it is important that the measures used achieve their objectives as efficiently as possible. Poorly targeted or ineffective measures can not only reduce the equity pay-off from government intervention but also undermine community support for redistributive measures generally.

As noted earlier, the NCP processes themselves require that consideration be given to equity issues. Further, retaining anti-competitive restrictions is unlikely to be an efficient way of achieving broader equity objectives. Indeed, several NCP reforms, particularly those that enhance the performance of government businesses that deliver community services, should enhance the ability of governments to pursue equity objectives.

Hence, rather than retreating from competition policy, the implication is that governments need to give more weight to equity issues when addressing reform to those government policies, such as tax, social security, community services and labour market programs, that are a relatively efficient means of delivering equity. That said, it remains the prerogative of governments to make decisions on these priorities.

Adjustment assistance

As noted earlier, some NCP reforms may adversely affect particular individuals, groups, industries or areas.

As the Council discussed in its 1996-97 Annual Report, adjustment assistance may be appropriate in some instances to facilitate changes to the structure of the economy and to compensate people or communities adversely affected by specific reforms. Phasing reform is one form of assistance that is widely applied, although there is a need to ensure that

phasing does not unduly delay the attainment of the benefits of reform. Alternatively, it may be appropriate to directly compensate people where reforms deprive them of pre-existing property rights and where rapid implementation is desirable. Specific retraining assistance programs may be appropriate where reforms are likely to involve lower employment in an industry.

Governments can also provide pro-active adjustment assistance. For example, prior to putting some of their functions to a competitive tendering process, some public bodies in Queensland and Victoria have provided training for their staff who undertook the relevant functions. This provided the staff with a better opportunity to win the work in open competition with the private sector or other government suppliers. There is a cost to this approach: namely, that governments may incur the cost of up-grading their workforce's skills only to find that they are still able to obtain a more cost-effective service from outside suppliers. Nevertheless, in some cases this cost may be justified by its perceived fairness and by the benefits of the reforms it helps facilitate.

In considering the case for adjustment assistance, several other matters are pertinent.

First, while some people may lose their jobs or find that their businesses become less viable as a result of a particular reform, it needs to be remembered that people are displaced from the workforce and a proportion of businesses lose viability regularly as part of normal economic activity. This is not to downplay the hardships for the individuals involved. Rather, it is to put them in some context.

Second, there already exist various measures, such as social security payments and subsidised training schemes, for people displaced as part of normal economic activity. These measures are also available for people displaced by economic reform. Governments may need to address the appropriateness of current levels or forms of these assistance measures. However, in the context of adjustment assistance for people affected by a particular reform, the question governments need to address is whether additional assistance should be offered to those affected.

Third, in some cases, the 'adverse effects' some people incur from reform are, in effect, simply a removal of the privileges they have previously enjoyed at the expense of other members of the community. This diminishes any ethical argument for providing special adjustment assistance in those cases.

Fourth, it is important to ensure that whatever assistance is provided does not negate incentives for necessary changes. Adjustment needs to be facilitated and adjustment assistance needs to focus on ways of helping people to cope with change.

Overall, these considerations mean that any special adjustment assistance for people affected by particular reforms, over and above that available for people generally, needs to be rigorously justified, transitional in nature, and targeted at equipping people to adjust to change.

Community services

Governments often also seek to address equity through community service obligations (CSOs). A CSO is a non-commercial activity that, while aimed at achieving a particular social outcome, would not be provided through the normal course of business. Traditionally, many government-owned businesses have been required to provide CSOs to meet government equity objectives.

For example, the Commonwealth Government requires Australia Post to provide a letter delivery service throughout Australia at a uniform rate of postage. While the current rate of 45 cents is more than sufficient to cover the costs of many mail users, it is insufficient to cover the costs of some regional and remote users. Hence, this CSO involves a cross-subsidy from some users of the service to others.

CSOs can be provided in various ways. One is the way just described, where a government business is instructed to provide certain services and does so using cross-subsidies. To ensure it is able to do this, governments have often used anti-competitive legislation to give the business a monopoly, and thereby prevent competitors undercutting it in the commercially viable areas of the market. Another way is for the government to allow competition, but

to provide a subsidy from its budget to the government business so that it can afford to provide the loss-making service. This transfers the source of funding from other consumers to taxpayers generally. Alternatively, the subsidy could be financed from a levy on other businesses competing in the market. Finally, the government can allow full competition and put the loss-making service out to tender.

CSO issues can arise in relation to the NCP water reforms. The water reform package requires pricing based on consumption, full cost recovery and desirably the removal of cross-subsidies. The water agreements specify that, where water delivery businesses are required to provide water services to customers at less than full cost, this subsidy is to be fully disclosed and ideally paid to the service deliverer as a CSO.

Similarly, while the NCP energy reforms generally involve the phasing out of cross-subsidies, they still provide scope for governments to provide CSOs to assist disadvantaged groups or areas.

CSO issues also arise under several aspects of the NCP competition principles package:

- when examining anti-competitive legislation, reviews are required to consider, among other things, "social welfare and equity considerations, including community service obligations";
- governments must also review any community service obligations provided by a government-run business when examining the merits of applying competitive neutrality reforms to that business; and
- before privatising a public monopoly or exposing it to competition, governments are required to review, among other things, "the merits of any CSOs undertaken by the public monopoly and the best means of funding and delivering any mandated CSOs." (CPA clause 4(3)(f))

In each case, it is open for reviews to recommend retention, increases or decreases to any CSOs provided by the government businesses under scrutiny and, where the CSO is to be retained, appropriate methods for its delivery.

Legislation review, competitive neutrality and structural reform issues all arose in the Council's review of Australia Post. The Council's report included twelve recommendations to maintain or strengthen existing CSOs and to provide guarantees that services will be maintained. The Council also recommended that the method of delivery revert from cross-subsidy to transparent funding. The funding method preferred was budgetary allocation or, alternatively, an industry levy, locked in for five years in legislation (see Chapter B13).

A2.3 Competition policy and the environment

Over recent years, there has been a trend towards the integration of economic and environmental considerations into government decision-making. This stems from the increasing recognition that sound environmental management and economic performance are interdependent, a notion popularised by the World Commission on Environment and Development (Brundtland 1987).

The integration of economic and environmental considerations is reflected in various aspects of the NCP package.

Water

Ecological sustainability is a central objective of the NCP water reform package. As discussed in Section A1.1 and Chapter B9, the package includes measures to conserve water, to improve river quality, and to address land salinity problems. Further, one part of the package specifies that investment in new water schemes or extensions to existing rural schemes is to be undertaken only after appraisal indicates that it is economically viable and ecologically sustainable. Importantly, the package also gives explicit recognition to the environment as a legitimate user of water.

Energy

As noted earlier, one of the aims of the electricity reforms is stated as being "the most efficient, economic and ecologically sound development of the electricity industry…". However, there is little specific attention given to environmental matters within the detail of the agreements themselves. Rather, the reforms focus on improving the efficiency of the energy industries, subject to whatever environmental policies are in place.

It is possible that implementing the energy reforms could cause, as a by-product, increased environmental impacts in Australia. This is because the significant price reductions for energy flowing from the reforms (discussed in Section A1.1) could increase the total amount of energy demanded in Australia, thereby increasing the environmental impact of producing and supplying it. That said, from a global perspective, changes in environmental impact would be lessened to the extent that the expansion in energy-intensive industries in Australia comes at the expense of industries overseas. Nevertheless, it is possible that, of itself, lower prices could increase energy production/usage overall.

Offsetting this, the energy reforms may provide certain environmental benefits. For example:

- the creation of wholesale trading arrangements through a national electricity market allows suppliers to sell 'green energy' into the market and makes it easier for consumers to buy energy from renewable sources. A green energy market was launched in NSW in 1997;
- the gas reform package is expected to contribute to an expansion in natural gas consumption from its current 18 percent share of total energy consumption to about 28 percent by the year 2010, at the expense of black and brown coal and petroleum products (ABARE 1997). Natural gas emits less carbon dioxide per unit of energy than any other fossil fuel; and
- the introduction of national 'access' codes in gas and electricity will allow for more efficient use of gas pipelines and electrical power lines, and discourage wasteful duplication of these facilities.

Nevertheless, should it be determined that price reductions are leading to excessive expansion in energy use, governments would need to consider appropriate policy responses. For example, tradeable emissions rights are one approach that provides incentives for people to reduce their energy consumption. This in turn may facilitate the use of tighter emissions targets over time. The aim would be to marry the benefits of least-cost energy provision under NCP, with the benefits of least-cost pollution abatement using an appropriate policy tool. This aligns with ecologically sustainable development principles.

Other NCP reforms

Environmental objectives are not the central focus of other elements of the NCP package, but the NCP agreements require that review panels consider "government legislation and policies relating to ecologically sustainable development" when assessing the merits of particular competition reforms. Importantly, under the NCP agreements, environmental considerations are of no intrinsically greater or lesser importance than other considerations, such as social and financial considerations.

This means that NCP review panels need to weigh environmental effects together with other effects. For example, under the legislation review principles, anti-competitive legislation is to be retained if the benefits (including the environmental benefits) exceed the costs (including the environmental costs) of doing so, and if the legislation's objectives cannot be attained in other ways.

An example is the 1995 review of the South Australian Water Resources Act. As noted in Section A1.3, the review found that while aspects of the Act are restrictive, they generate net benefits by mitigating the risk of environmental degradation. It therefore recommended that they be retained.

A2.4 Competition policy and economic rationalism

While 'economic rationalism' is rarely defined precisely or consistently, it is most commonly used in public debate to describe policies and practices such as privatisation, blanket deregulation, free markets, 'laissez faire' economics, welfare cutbacks, contracting out, small government, reduced social services and a focus on markets, money and materialism.

Competition policy does not require any of these things. For example, it is entirely consistent with competition policy for governments to increase spending on welfare, to increase the level of government funded or subsidised social services, to retain businesses in public ownership and so on.

Further, as noted earlier, the NCP agreements explicitly recognise a need for government intervention in markets. They also give social and environmental values no intrinsically more or less weight than financial considerations in determining where the public interest lies.

A3 SUPPORTING COMPETITION POLICY: THE COUNCIL'S CONTRIBUTION

When Australia's nine governments jointly agreed to implement the NCP package, they also established the Council to assist them with the process.

The Council comprises five part-time councillors drawn from different business sectors and regions of Australia, supported by a secretariat of around 20 staff based in Melbourne.

Although funded by the Commonwealth, the Council is a national body, having been established and empowered by agreement of all Australian governments and with responsibilities to them as a group. As a statutory body, the Council is also independent of the executive arm of any government.

The Council has four main roles:

- to assess jurisdictions' progress in implementing the NCP reforms;
- to evaluate applications relating to the National Access Regime;
- to undertake other work as requested by Australian governments; and
- to increase understanding and to provide advice on the NCP process generally.

In this chapter, the Council discusses its recent work and foreshadows the task ahead. It also discusses the findings of two Senate Committee reports that have commented on the Council's role and performance. More details on the Council's operations and management are contained in Part C.

A3.1 Assessing jurisdictions' performance

The Council is required to assess each State and Territory government's progress in meeting its NCP commitments at the end of each of the three reform tranches: that is, on 1 July 1997, 1999 and 2001. These assessments are important because, to share the benefits of competition reform, the Commonwealth has agreed to make payments to the States and Territories, provided they make satisfactory progress in implementing the agreed reforms. All up, these payments are worth around $16 billion over the period to 2005-06.

First tranche matters

The Council completed its first assessment in July 1997. The Council's approach, processes and recommendations were discussed in last year's Annual Report.

In brief, the Council found that all governments had taken significant steps to meet their NCP commitments, and recommended that all States and Territories receive all NCP payments for the first year of the first tranche. However, the Council also identified some matters in which sufficient progress had not been demonstrated. The matters related to:

- insufficient progress by all jurisdictions in implementing the National Gas Access Code;
- the application of competitive neutrality to local government business activities;
- the omission of certain gambling legislation from some jurisdictions' legislation review schedules;
- Western Australia's exclusion of resource development agreement Acts from consideration for possible restrictions on competition under the NCP program;
- Western Australia's slow progress in removing legislative restrictions to competition in the gas industry; and
- non-implementation of the NSW rice industry review recommendation to abolish the domestic marketing monopoly.

Rather than recommending deductions on these matters, the Council resolved to revisit them in June 1998 and to link jurisdictions' progress on them to the NCP payments for the second year of the first tranche. The Commonwealth Treasurer accepted these recommendations.

The Council completed its assessment of these residual matters on 30 June this year, and forwarded its recommendations to the Treasurer. In the case of the NSW rice review, the Council found that satisfactory progress had not been made, and recommended that $10 million be deducted from that jurisdiction's NCP payments, unless domestic deregulation occurs by 31 January 1999, in line with the recommendations of the independent review. In relation to gambling legislation, given the nature of the issues involved and the proposed Productivity Commission inquiry into gambling, the Council considered that these matters are better resolved outside the first tranche assessment process. In relation to the other residual matters, the Council found that progress had been satisfactory and recommended full payment of competition moneys.

On 21 August, the Treasurer announced that he accepted these recommendations except that, in respect of the NSW rice industry reform, the Treasurer reserved any decision until early 1999. This will allow the Treasurer to take into account any developments arising from current investigations of mechanisms for implementing the recommendations of the 1995 review, involving NSW Government officials, rice industry representatives and the Council (see Section B3.5).

During the year, the Council also examined the Commonwealth's progress in relation to its first tranche commitments. This is not formally required under the NCP agreements, because there are no monetary transfers riding on the Commonwealth's progress. However, to enhance the transparency of the NCP process, the Commonwealth has agreed to have the Council assess its performance too.

The Council found that, while the Commonwealth had made solid progress in many areas, there were several specific matters on which it had not met its NCP reform commitments. The Commonwealth did not comply with the NCP principles in relation to some anti-competitive legislation. Nor did it conduct appropriate reviews before undertaking the structural reform of certain public monopolies. It also failed to establish a competitive neutrality

complaints mechanism by 1 July 1997. The Commonwealth has since rectified, or indicated it will address, most of the problems identified by the Council.

The Council will publish its full assessment of first tranche progress, including progress by the Commonwealth, later this year.

Second tranche matters

The Council is now preparing for its second tranche assessment, due in mid 1999. It intends to use the same 'no surprises' approach as it used for the first tranche assessment, albeit refined to reflect the lessons drawn from it.

It has commenced by seeking to clarify with jurisdictions what actions they will need to take to make 'satisfactory progress' in implementing their reform commitments. To this end, it is:

- consulting with officials in all jurisdictions;
- disseminating material elaborating on aspects of the NCP agreements; and
- seeking agreement from jurisdictions about what they need to do.

The Council has set out its current views on these matters in various parts of Part B of this report, as well as in formal advice to jurisdictions.

The next step is to gauge jurisdictions' overall progress against their commitments. In doing this, the Council will draw on the annual NCP progress reports which jurisdictions provide in the lead up to the July 1999 assessment. The Council also welcomes information about achievements and possible slippages in the reform program from other parties, and will draw on its own knowledge and investigations of specific reforms. As and if particular slippages or shortcomings in the reform program became apparent, the Council will raise these with the relevant jurisdictions.

The Council intends to circulate a preliminary assessment to jurisdictions in early 1999. Among other things, the assessment will set out any matters on which the Council has formed concerns that jurisdictions may not have met their reform commitments.

The Council will then seek clarification or further evidence on any omissions or matters of contention from jurisdictions. As the assessment deadline nears, the Council intends to meet with senior officials and ministers, where necessary, to discuss any unresolved issues, together with any subsequent matters about which the Council becomes concerned.

Immediately prior to the assessment deadline, the Council will circulate its draft final assessment to governments to provide an opportunity for comment. Finally, after taking into account governments' responses, the Council will finalise its recommendations and dispatch them to the Commonwealth Treasurer by 1 July 1999.

A3.2 Processing applications for access

Under the National Access Regime, the Council is required to assess applications and make recommendations to the relevant government on two matters:

- whether infrastructure services should be 'declared' for access; and
- whether particular State or Territory access regimes should be 'certified' as being effective under the National provisions.

In August 1996, the Council published a draft guide on how it would approach its task. Among other things, it undertook to use open processes, such as preparing background papers to help interested parties to make submissions. It also undertook to meet with the applicant and the affected parties, to avoid undue legalism, and to seek to complete its assessment within sixteen weeks. The Council also provides comprehensive supporting analysis for its recommendations, which are released to the public when the relevant Minister makes his or her decision.

Prior to 1 July 1997, the Council had received seven sets of declaration applications. It had completed its assessment process and made its recommendations to the relevant government in relation to five of these. One other application had been withdrawn before the Council completed its

process, and one more was carried over into 1997-98. During 1997-98, the Council completed its assessment of this application and of one more set of applications that was lodged during the year. There were no declaration applications outstanding as at 30 June 1998.

The public processes adopted by the Council appear to have worked well. On the whole, interested parties, including applicants and infrastructure owners, have made positive contributions and worked cooperatively. The Council's policy of dealing with applications openly and transparently has given all interested parties the opportunity to participate and to gauge the extent to which their views have been taken into account. In some instances, the Council has had to exceed deadlines to ensure that parties have a reasonable opportunity to respond to information provided by others. On the whole, however, the Council has been able to achieve its 16 week objective for considering declaration applications.

For all but one Council recommendation in favour of declaration, the relevant Minister has decided not to declare the service. Each of these related to infrastructure services owned by a state government, meaning that the State Premier was the relevant Minister. This highlights a possible flaw in the regime: that the relevant Minister will often be required to make a decision about access to an infrastructure service that the Minister's government owns.

In all of these cases, and in the case where the relevant Minister (the Commonwealth Treasurer) did declare the services, the Minister's decision has been appealed to the Australian Competition Tribunal. This provides an opportunity for the Tribunal to 'test' the Council's and Ministers' approaches to these issues. However, the Tribunal is yet to hand down a decision on a substantive matter. In some cases, the parties to these proceedings have taken the opportunity to negotiate outcomes, rather than proceed with the appeal. In cases where appeals are still proceeding, parties have sought time to attempt to reach negotiated settlements but so far have been unable to agree. Consequently, the Tribunal has not yet had the opportunity to substantially consider the issues raised by appeals against Ministers' decisions.

In relation to State and Territory access regimes, prior to 1 July 1997, the Council had received three applications for certification, of which it had finalised its consideration of two. In both cases, it recommended to the

Commonwealth Treasurer that the State regime be certified as 'effective'. The Treasurer accepted these recommendations. Consideration of the other application, which relates to the NSW rail access regime, has entailed considerable dialogue between the Council and the NSW Government and several revisions to aspects of the application. The Council released a draft recommendation on this matter in April 1997, but it is yet to finalise the process.

As well as its formal access assessment and recommendation role, the Council undertook a draft assessment of the National Gas Access Code against the National access principles during the year. This was the first stage in a process that will result in each State and Territory applying individually to the Council for certification of the National Code as it applies in that jurisdiction. The Council's draft assessment focussed on generic issues relevant to the broad framework and operation of the National Code. The aim was to resolve any outstanding issues prior to the Code being finalised and implemented by each jurisdiction. Following the draft assessment, several amendments were made to the National Code to address issues identified by the Council.

The Council has now had considerable experience in dealing with access applications, and will use it to develop the final version of its guide to the National Access Regime, replacing the current draft guide. Work is underway on this project, and the Council aims to release the new guide in early 1999.

A3.3 The broader work program

The Council also undertakes projects determined by agreement of a majority of Australia's governments. The work program can include the conduct of reviews and provision of advice to governments covering matters arising out of the NCP agreements, including: the review of restrictive legislation; the structural reform of public monopolies; prices oversight; and competitive neutrality. The work program can also include any other projects as agreed to by a majority of governments.

Australia Post review

In May 1997, with the States' and Territories' agreement, the Commonwealth Treasurer referred the *Australian Postal Corporation Act 1989* for review by the Council.

In conducting the review, the Council publicised the review widely and undertook significant public consultation. It released an issues paper in June 1997 to indicate to interested parties the types of issues under the review and to assist them in making a submission. It held a series of meetings and workshops with relevant bodies, and visited several regional and remote communities to get a better understanding of the issues involved. It also released an options paper in October 1997 to provide people an opportunity to make additional comments on the matters under review and possible approaches to reform. After the release of the options paper, the Council conducted a further series of workshops and held more meetings with interested parties. The Council also commissioned three consultancies to examine and report on various issues associated with the review.

The Council released its report in February 1998 and, after public debate, the Commonwealth Government announced its response to the review in July. In brief, the Government adopted a different approach to reform than that recommended by the Council.

The Council's review processes and recommendations, and the Government's response, are discussed in more detail in Chapter B13.

Trade Practices Act exemption provisions review

With the agreement of the States and Territories, on 4 June 1998 the Commonwealth Treasurer referred two subsections of the *Trade Practices Act 1974* for review by the Council. The subsections (51(2) and 51(3)) provide for the exemption of certain businesses and/or commercial arrangements from some of the anti-competitive provisions of the Act (see Box A3.1). The terms of reference are summarised in Box A3.2.

The Council released an issues paper in June, and invited written submissions from interested parties. Given the nature of the matters under review, the Council intends to rely heavily on written submissions. The Council will also release an interim report in October this year to provide further opportunity for people to comment before the Council formulates its recommendations. The Council is required to forward its recommendations to the Treasurer by 5 March 1999.

Box A3.1 Section 51 exemptions from the Trade Practices Act

Section 51(2) provides a number of standing exemptions to the prohibition of restrictive trade practices in Part IV of the Trade Practices Act (TPA), except for secondary boycotts and resale price maintenance. The exemptions, in general terms, relate to:

- employment conditions;
- restrictive covenants in employment contracts;
- sale of business contracts and partnership agreements;
- approved standards; and
- export contracts.

Section 51(3) of the TPA also provides an exemption to the prohibition of restrictive trade practices prohibited in Part IV. However, it does not extend to misuse of market power and resale price maintenance. The exemption covers certain conditions of licenses or assignments of statutory intellectual property rights relating to:

- patents;
- registered designs;
- copyright;
- trade marks; and
- circuit layouts.

Box A3.2 Terms of reference for the Section 51 review

The terms of reference reflect the provisions of clause 5 of the Competition Principles Agreement and asks the Council to have regard to a number of matters, including:

- the objectives of sections 51(2) and 51(3) of the TPA;
- any restrictions on competition contained in sections 51(2) and 51(3);
- the likely effect of these restrictions on competition and on the Australian economy generally;
- the costs and benefits of the restrictions; and
- whether there are alternative ways of achieving the objectives of sections 51(2) and 51(3).

The terms of reference identify several other factors to be taken into account by the Council, including:

- Federal and State industrial relations legislation and international agreements relating to labour that recognise collective bargaining;
- the common law doctrine of restraint in relation to restrictive covenants pertaining to employment, partnerships, and the protection of goodwill in the sale of a business;
- standards made by the Standards Association of Australia;
- the Government's obligations under intellectual property treaties and conventions arising from Australia being a signatory to various International Property Agreements and Conventions;
- Australian intellectual property legislation including the *Copyright Act 1968*, the *Designs Act 1906*, the *Patents Act 1990*, the *Trade Marks Act 1995*, the *Circuit Layouts Act 1989* and the *Plant Breeder's Rights Act 1994*; and
- other nations' experience with provisions similar to sections 51(2) and 51(3).

Specific TPA exemption and prices surveillance matters

Under the NCP, the Council can be requested to:

- provide advice to the Commonwealth Parliament when it is considering overriding State or Territory exceptions from aspects of the Trade Practices Act; and
- recommend on whether State and Territory government businesses should be subject to prices surveillance.

These functions are explained in Chapters B2 and B6 respectively, although the Council was not required to assist on either of these matters during 1997-98.

A3.4 Improving understanding of competition policy

Improved community understanding and acceptance of the NCP package are necessary if the package is to be successfully implemented. The Council highlighted this point in its last Annual Report when it noted the role for governments (and the Council) to clearly and accurately explain to the community the interface between the competition reforms, other aspects of government policy, and overall community objectives. Similarly, two Parliamentary inquiries into the Council and the NCP program have emphasised the importance of community consultation and communication. Recent political debate has further emphasised these points.

In disseminating information about NCP, the Council seeks to project its message to a range of audiences. It recognises that the subject matter of competition policy is neither straightforward nor always immediately intuitive. It also recognises that different groups will have inherently different levels of interest in, and understanding of, competition policy issues. It therefore provides both short and accessible information for some audiences, as well as more technical information for others.

The Council entered 1997-98 with much of its 'communications infrastructure' already in place. During the previous eighteen months, the Council had published various information papers explaining aspects of the NCP (see Box A3.3), launched its newsletter, *NCC Update*, established its web site and undertaken an extensive series of speeches and meetings to discuss aspects of the NCP program. These are discussed in last year's Annual Report.

Box A3.3 Information papers available from the Council

- The National Access Regime: a draft guide to Part IIIA of the Trade Practices Act (August 1996);
- Considering the public interest under the National Competition Policy (November 1996);
- Competitive neutrality reform: issues in implementing Clause 3 of the Competition Principles Agreement (January 1997);
- Compendium of National Competition Policy agreements (January 1997)
- Legislation review compendium (April 1997);
- Assessment of State and Territory progress with implementing the National Competition Policy and related reforms (July 1997)

During 1997-98, the Council built on these developments in various ways.

- During its review of Australia Post, the Council undertook extensive consultation with interested parties (see Chapter B13). Among other things, it released a special edition of *NCC Update* that contained various articles on aspects of the review in an accessible manner.
- In July 1997, a secretariat staff member, in conjunction with the Gas Reform Implementation Group, made a series of presentations around the country on aspects of gas reform and how the Council would approach assessing applications to certify new gas access regimes.

- Councillors and secretariat staff presented papers at more than forty conferences, and made many less formal presentations on NCP to interested parties (see Appendix C3).
- Councillors and secretariat staff met with a wide range of people with an interest in NCP matters, including politicians, various government officials, business people and interest groups.

However, the level and nature of public debate about NCP has changed significantly in recent months. Awareness of the existence of competition policy has increased, although understanding of what it entails appears to have become more confused. This stems partly from the complex nature of the NCP package, and partly from the misrepresentation of NCP processes and outcomes by certain groups. Further, in the current political climate, there are limited incentives for community leaders to publicly support specific competition reforms, even if they believe that the reforms offer a substantial community benefit.

The Council is therefore redeveloping its communications strategy in various ways.

First, it is focussing on correcting misunderstandings about NCP and highlighting the public interest safeguards built into the NCP agreements.

Second, it is currently relying less on the media to communicate its message and instead travelling and speaking with communities directly affected by reform. For example, in July the Council President and senior officials met with representatives of rice growers in Leeton to discuss the recommendations of the NSW rice industry review, and competition policy generally. Likewise, in August senior officials met with several local councils and water authorities in Queensland to discuss relevant aspects of competition policy face-to-face. The Council has found that these types of discussions have:

- reduced many of the misconceptions about NCP that some people have gained from indirect reporting and discussion in the media;
- given the Council a clearer understanding of how reform is proceeding 'on the ground'; and

- been encouraging, in that many people charged with local level implementation, including in local councils and government instrumentalities, have expressed support for the NCP processes and the benefits they are seeing.

Third, the Council is also investigating with governments the possibility of undertaking a more substantial information campaign on NCP than its present resources allow.

That said, the Council recognises the limitations of one body seeking to alter the course of public debate. In the year ahead it will thus seek to build a greater constituency of groups that support particular reforms and the overall NCP process, and encourage those groups to make their views public.

A3.5 Parliamentary inquiries

Two Commonwealth Parliamentary Committees have completed reports that look at the Council or aspects of its work.

In June 1998, the House of Representative Standing Committee on Financial Institutions and Public Administration reported on its Review of the National Competition Council Annual Report 1996-97. The Committee concluded that:

> The NCC has made an encouraging start so far with its limited resources. The task however is becoming more challenging as possible difficult decisions on competition payments may have to be made; as the real work of the reforms begin, some in more politically sensitive areas; and as community questioning about the benefits and implications of reforms become more prominent particularly in the absence of jurisdictional rigour in selling the reforms. It is critical that the NCC's (and other competition agencies') public education role be improved. The Committee will continue to monitor the NCC's progress in this increasingly more difficult task.

The Committee made one recommendation:

> That the Commonwealth, State and Territory Governments and agencies involved in the implementation of national competition policy devote resources to ensure community understanding and debate about the contents of the policy and its outcomes.

Also in June 1998, the Joint Committee of Public Accounts and Audit produced a report on General and Specific Purpose Payments to the States which contained some discussion of the Council's operations. Among other things, the Committee stated that:

- it supports the Council's recent efforts to improve consultative arrangements with interested organisations in the community;
- it appears that the Council had adopted a reasonable, commonsense approach in exercising flexibility and discretion in its assessment of states' compliance, which was consistent with the cooperative framework for implementing NCP;
- it considers that the Council assessment process is structured, transparent and provides natural justice to affected parties;
- it sees merit in an external, independent review of the key competition policy institutions – the ACCC, the Council and the Australian Competition Tribunal; and
- it supports the proposal for an independent review of the Council, but recommends that it should be brought forward to the first half of 2000.

As well as these reports, in July 1998, the Senate established an inquiry to examine the socio-economic consequences of NCP, with the report scheduled for early next year.

These inquiries and reports are discussed further in Section C3.3.

PART B COMPETITION POLICY: DEVELOPMENTS IN DETAIL

B1 ABOUT THE NCP PROGRAM

B1.1 Origins

The performance of the Australian economy at the micro-economic level has received increasing attention since around the mid-1980s, with governments at all levels undertaking numerous reforms:

- some of these introduced greater competition into sectors of the economy, as in the case of domestic airline deregulation;
- others involved more centrally coordinated changes to the structure and operations of particular sectors, as in the case of reforms to higher education; and
- many, such as tariff reductions and the abolition of quantitative import restrictions, sought to reduce inefficiencies in the traded goods sector.

By the late 1980s and early 1990s, it had become clear that a more balanced and coordinated approach to reform across the three spheres of government was required. Some progress was made at the 1991 Special Premiers' Conference. Subsequent meetings of Australian heads of governments advanced the agenda and, in 1993, governments created the vision for a national approach to competition reform when they commissioned the Independent Committee of Inquiry into National Competition Policy (Hilmer 1993).

Following receipt and analysis of the committee's report and recommendations, the Council of Australian Governments (COAG) agreed to implement the National Competition Policy (NCP) package in April 1995.

The package contains a range of measures designed to realise the benefits which competition, properly harnessed, can bring. It builds on the pro-competition principles embodied in the *Trade Practices Act 1974* (TPA). The TPA contains various rules to limit the abuse of market power by businesses, its broad aim being to promote fair trading and efficient industry practices

and to protect consumers. The NCP package expands the scope of the Act to cover all businesses – some were previously exempt – and adds new pro-competitive regulations to open up markets characterised by natural monopolies. It also applies pro-competitive rules to the operations of government businesses. With this increase in pro-competitive regulation, the package also requires governments to review and, where appropriate, reform anti-competitive regulation applying to specific industries. In effect, the package involves a shift away from anti-competitive arrangements in specific industries to general pro-competitive rules, to enhance economic performance and consumer interests.

While seeking the benefits available from competition, the package also contains processes that recognise that other approaches are sometimes needed to meet Australia's social, environmental and other economic goals.

B1.2 The reforms

Under the NCP, governments agreed to:

- extend the reach of the anti-competitive conduct laws in the TPA;
- establish 'access' arrangements for the services of nationally significant infrastructure;
- review and, where appropriate, reform all laws which restrict competition, and ensure that any new restrictions provide a net community benefit;
- introduce competitive neutrality so that government businesses do not enjoy unfair advantages when competing with private businesses;
- processes for restructuring public sector monopoly businesses to increase competition;
- consider extending prices oversight to certain State and Territory government businesses; and
- implement and continue to observe previously agreed reforms in the areas of electricity, gas, water and road transport.

Governments also agreed to apply these reforms to local governments in their jurisdiction.

B1.3 The mechanics of the NCP program

Competition Policy Reform Act

The Commonwealth Government enacted the *Competition Policy Reform Act 1995*. It:

- amended the competitive conduct rules (Part IV) of the TPA and extended their coverage to State and local government businesses and unincorporated bodies;
- created a new Part IIIA of the TPA to provide a National Access Regime;
- amended the *Prices Surveillance Act* to extend prices oversight arrangements to State and Territory business enterprises; and
- created two new institutions to oversee the implementation of the NCP package – the Australian Competition and Consumer Commission (ACCC)[1] and the National Competition Council.

The intergovernmental agreements

Governments' NCP commitments are contained in three intergovernmental agreements:

- the Conduct Code Agreement;
- the Competition Principles Agreement (CPA); and
- the Agreement to Implement the NCP and Related Reforms (the Implementation Agreement).

The Conduct Code Agreement sets out the basis for extending the coverage of the TPA.[2]

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1 The ACCC was created through the merger of the former Trade Practices Commission and the Prices Surveillance Authority. Its principal responsibility is enforcement of the TPA. The Trade Practices Tribunal was also renamed the Australian Competition Tribunal.

2 The Conduct Code Agreement also covers consultative processes for amending the competition laws of the Commonwealth, States and Territories, and for appointments to the ACCC.

The CPA sets out the principles to be followed by governments in relation to all the agreed reforms[3], other than those contained in the Conduct Code and the specific reforms in gas, electricity, water and road transport.[4]

The Implementation Agreement sets out the conditions for provision of financial payments by the Commonwealth to the States and Territories, and the role and functions of the Council in assessing States' and Territories' progress on the reforms and advising the Commonwealth Treasurer on eligibility for the NCP payments. The NCP reform program has been split into three 'tranches', and the Council assesses each government's progress in meeting their commitments at the end of each tranche: that is, on 1 July 1997, 1999 and 2001. The Commonwealth has agreed to make payments to the States and Territories, provided they make satisfactory progress in implementing the agreed reforms. All up, these payments are worth around $16 billion over the period to 2005-06.

All three agreements are set out in the Council's compendium (NCC 1998).

Timing of the reforms

Under the Implementation Agreement, different reforms are required at different times in relation to the various reform areas. For example:

- for the reforms to extend the reach of Part IV of the TPA, the States and Territories needed to make a once-only legislative change by July 1996, with no further action required;
- for the National Access Regime, the Commonwealth was required to make a once-only legislative change, with further action limited to appropriate amendments to fine-tune the regime;
- in relation to legislation review and competitive neutrality, ongoing reform action is required, although each jurisdiction was responsible for compiling its own reform program;

3 The CPA also sets out consultative arrangements for determining appointments to, and deciding the work program of, the National Competition Council.

4 The reform principles and commitments in relation to these areas are set out in other COAG agreements, and the requirement to implement them in the context on the NCP package is set out in the Implementation Agreement.

- for matters such as prices surveillance and structural reform of public monopolies, jurisdictions simply need to observe the processes and requirements set out in the CPA if and when these matters arise; and
- for the specific infrastructure reforms, the nature and timing of the necessary reforms are set out in intergovernmental agreements. In electricity, gas and road transport, specific progress is required for each of the three tranches. For water, progress is formally only required for the second and third tranches.

The Council's functions

The general assessment function

The Council examines State and Territory progress in relation to each of the reform areas listed in Section B1.2, and makes recommendations to the Commonwealth Treasurer about the provision of NCP payments to the States and Territories.

The Council completed its first assessment in July 1997 and made its recommendations to the Commonwealth Treasurer, and completed its follow up assessment in July this year. The Council also assessed the Commonwealth Government's progress in implementing the agreed reforms during 1997-98.

In undertaking its assessments, the Council relied on information provided in governments' annual progress reports, as submitted to the Council in March 1997 (except in the Commonwealth's case, where the report was submitted in February 1998), in conjunction with other information obtained by the Council. A description of the procedures followed by the Council is contained in Section A3.1.

In Chapters B2 to B10 and B12 of this report, the Council discusses the agreed reforms and its assessment of progress to date in relation to each reform area. In most cases, each chapter sets out:

- the background to and rationale for the particular reform(s);
- governments' commitments in relation to the reform(s), and the progress expected in relation to each tranche of the NCP program;
- progress made to date; and
- implementation issues which have arisen and/or the task ahead for governments.

The chapters do not provide comprehensive information on all actions undertaken by Australia's governments in relation to each of the reform areas. Rather, they provide an overview of the reforms to date, including indicative examples of specific reforms.

Functions related to specific reforms

The Council assesses applications and makes recommendations to the relevant government in relation to the National Access Regime. In undertaking this role, the Council must consider arguments and weigh evidence to determine whether to recommend in favour of, or against, a particular application. The Council uses public processes and publishes its recommendations and analysis. The Council's processes are discussed in Section A3.3. In Sections B12.4 and B12.5, the Council discusses each application received during 1997-98 and, where the relevant government has announced its decision, provides a detailed summary of the Council's deliberations and recommendations. It also updates developments on prior applications.

The Council also has an advisory role in relation to Section 51 of the TPA, and a recommendatory role in relation to prices surveillance of government businesses. These are discussed in Sections B2.2 and B6.2 respectively.

The Council can also be requested to undertake other work on behalf of Australian governments in relation to the review of anti-competitive

legislation. Earlier this year, the Council completed its inquiry into the *Australian Postal Corporation Act 1989*, as part of the Commonwealth's NCP legislation review program. The review is discussed in Chapter B13. The Council is currently undertaking a review of Section 51(2) and (3) of the TPA (see Section A3.3).

B2 EXTENSION OF THE COMPETITIVE CONDUCT RULES

B2.1 Implementing the competition code

Under the Conduct Code Agreement, governments agreed to extend the operation of Part IV of the *Trade Practices Act 1974* (TPA) to all business activities.

Broadly speaking, Part IV prohibits a range of anti-competitive trade practices including:

- anti-competitive agreements;
- misuse of market power;
- exclusive dealing;
- resale price maintenance; and
- mergers which have the effect, or likely effect, of substantially lessening competition.

Constitutional limitations had previously prevented application of these provisions to unincorporated businesses, such as legal partnerships, operating solely in one State. Further, many State and Territory government businesses had 'Shield of the Crown' immunity from the TPA.

To rectify this, State and Territory governments have enacted a modified version of Part IV, called the competition code, in each of their jurisdictions.

B2.2 Council recommendations for competition law exceptions

Section 51(1) of the TPA allows the Commonwealth, States or Territories by legislation or regulation to specifically authorise conduct that would otherwise breach Part IV of the Act. The Commonwealth Treasurer may, however, override a State or Territory exception under section 51(1) by regulation.

Section 51(1) has been part of the TPA since its enactment in 1974 and has, for example, been used to exempt exclusive licence arrangements entered into by a government. The Australian Competition and Consumer Commission (ACCC) publishes a cumulative list of all laws that rely on section 51(1) in its annual report.

Operation of the section 51(1) exception

Section 51(1) of the TPA was substantially revised in 1995 by the *Competition Policy Reform Act 1995* as part of the extension of the Competition Code (a modified version of Part IV). The operation of the revised section 51(1) is subject to the following limitations set out in section 51(1C).

- The Commonwealth, State or Territory legislation or regulation that relies on section 51(1) must expressly refer to the TPA.
- State or Territory legislation or regulations cannot approve a merger or acquisition that would breach sections 50 and 50A of the TPA. The Commonwealth may approve a merger or acquisition that would breach sections 50 and 50A, but only by legislation and not regulation.
- Regulations made by the Commonwealth, States or Territories that rely on section 51(1) are only effective for two years after they are made. Any similar regulation made after that time is ineffective. For an exception to continue, it must be enacted in legislation.

- State or Territory legislation or regulations relying on section 51(1) are only effective if the State or Territory is a fully participating jurisdiction and a party to the Competition Principles Agreement (CPA). A fully participating jurisdiction is one that:
  - is a party to the Conduct Code Agreement and applies the Competition Code in its jurisdiction; and
  - is not subject to a notice published by the Commonwealth Treasurer under section 150K of the TPA. A section 150K notice may be published where a jurisdiction has made substantial modifications to the Competition Code.

Where a State or Territory ceases to be a party to the CPA or is subject to a notice under section 150K, any exceptions made by that State or Territory under section 51(1) become ineffective after 12 months.

Transitional arrangements exist for exceptions that were made, based upon the version of section 51(1) that existed prior to the *Competition Policy Reform Act 1995*. Those exceptions lapsed on 20 July 1998 unless they had been modified to comply with the current version of section 51(1).

Conduct Code Agreement reporting obligations

Under the Conduct Code Agreement, the Commonwealth, States and Territories have reporting obligations to the ACCC on section 51(1). These obligations are:

- to notify the ACCC of legislation that relies on section 51(1) within 30 days of the legislation being enacted or made; and
- to have notified the ACCC by 20 July 1998 of legislation relying on the previous version of section 51(1) that will continue pursuant to the current section 51(1).

The Council will consider jurisdictions' compliance with the Conduct Code reporting obligations in its second tranche assessment of jurisdictions' NCP progress.

The Commonwealth's role in disallowing legislation relying on section 51(1)

The Commonwealth has discretion to disallow State or Territory exceptions relying on section 51(1) by regulation. However, after four months from the date of notification of a State or Territory exception to the ACCC, the Treasurer can only exercise the discretion to disallow after receiving a report from the National Competition Council on:

- whether the benefits to the community from the State or Territory legislation, including the benefits from transitional arrangements, outweigh the costs;
- whether the objectives achieved by restricting competition by means of the legislation can only be achieved by restricting competition; and
- whether the Commonwealth should make regulations for overriding the legislation.[14]

A regulation disallowing a State or Territory exception must be tabled in both Houses of Federal Parliament and is subject to the normal procedures for the passage of subordinated legislation.

The Council is yet to receive a request from the Commonwealth to report on a section 51(1) exception.

The Council's approach to reporting on section 51(1) referrals

The section 51(1) mechanism provides a means by which State and Territory Governments are able to protect restrictive conduct by their businesses on the ground that it is in the public interest.

14 Clause 2(2) of the Conduct Code Agreement.

However, increased use of section 51(1) might be seen as inconsistent with the policy objectives for NCP. For example:

- increased reliance might impact adversely on the broad application of Part IV; and
- new legislation reliant on section 51(1) is, in essence, new legislation restricting competition, and places obligations on governments under the CPA.

The Council's view is that, in order to ensure exceptions under section 51(1) are consistent with the policy objectives underlying NCP, States and Territories should:

- be guided by the policy objectives of NCP; and
- ensure that section 51(1) exceptions meet the competition tests; that is, there is evidence that restrictions on competition provide a net benefit to the community and the objective of the legislation can only be achieved by restricting competition.

Consistent with this, the Council, where it is asked by the Commonwealth to report in relation to action to override a State or Territory exception, will assess the benefits and costs to the community in terms of the public interest factors set out in clause 1(3) of the CPA.

B3 LEGISLATION REVIEW

B3.1 Background

Regulation impinges on everyone in some way. It affects the hours people can shop and the goods and services they can buy, the hours worked, the type of businesses people run and how they can run them, and more generally how the community can achieve desired economic and social outcomes. Further, because many of our goods and services are sold in global markets, the domestic regulatory environment is also important to our international competitiveness.

This pervasiveness of regulation is well recognised. For example, the Commonwealth Interdepartmental Committee on quasi-regulation has described regulation as a spectrum ranging from self regulation, where there is no government involvement, through various regulatory arrangements with increasing degrees of government influence and involvement, to explicit government regulation.

Like many other developed countries, Australia faces a range of problems with its regulatory systems:

- overly stringent and prescriptive regulations reduce competition and can impose substantial costs on business, consumers and society;
- regulations which focus on existing problems and are not adaptable to new situations lose relevance once the problem they were designed to address is resolved or superseded;
- regulatory differences within and between levels of government add unnecessarily to the costs of Australian business, which is operating increasingly on at least a national level;
- the domestic regulatory environment is important for the international competitiveness of Australian firms; and

- there is often a tendency for rapid growth in regulation, especially in areas of quasi-regulation where governments influence business compliance although not through explicit laws.

Recognising these risks, and that effective regulation is fundamental to good government, governments in Australia have been seeking to address inappropriate regulation since the mid-1980s. But attempts to do this have not always been successful. There have been gaps in programs, the mechanisms available for reviewing regulations have been limited, compliance with regulation review principles has been overridden by other considerations, and the review programs generally have not directly addressed problems of the anti-competitive effects of regulation.

Under the April 1995 NCP agreements, each government undertook to review and, where appropriate, reform all existing regulations which restrict competition by the year 2000. Governments agreed that legislation should meet two threshold competition tests. They are that legislation (both existing and proposed) should not restrict competition unless:

- the benefits of the restriction to the community as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.

B3.2 Governments' commitments

Under clause 5 of the NCP Competition Principles Agreement (CPA), governments undertook to:

- develop a comprehensive legislation review timetable, including local government regulation, by June 1996;
- review, and where appropriate, reform legislation that restricts competition over the period to 2000;
- ensure that proposals for new legislation which restrict competition are accompanied by evidence that the legislation is consistent with the competition tests; and

- produce annual reports of their progress with their legislation review programs.

A key element of the NCP approach is the presumption in favour of competition. Thus, under NCP, governments retain restrictions on competition only if they can show there is a net community benefit from the restriction and if their policy objective can only be achieved by restricting competition.

Notwithstanding this, NCP explicitly recognises that there will be circumstances where restrictions on competition are justified. Thus, the key to evaluating policy instruments which restrict competition is the maximisation of net community benefit, consistent with the central tenet of NCP that competition be promoted as a mechanism for improving Australia's well being rather than an end in itself.

With a number of minority or near-minority governments and/or governments which do not control the upper house, there will inevitably be issues of contention between the government of the day and the Parliament. The Council views a commitment to the NCP agreements and agenda by jurisdictions as binding not only on the government of the day, but also on the jurisdiction's Parliament, particularly as governments change over time. In this respect, the Council considers that it is incumbent upon a government to devote effort to ensure that reforms are accepted by the Parliament.

B3.3 Progress to date

Setting the legislation review agenda

As required under the CPA, all jurisdictions developed a timetable for reviewing anti-competitive legislation within their jurisdictions by June 1996. Where governments identified legislation likely to impact on other jurisdictions, they nominated the legislation for national review.

Typically, the legislation review timetables include information on:

- the name of the legislation;
- the government agency responsible for administering it;
- a description of the legislation and/or the nature of the restriction on competition it involves; and
- the proposed scope and date of the review.

Assessing the stock of legislation and associated regulations to determine whether they contain restrictive provisions was a complex and lengthy task. Because it involved judgments by governments about the existence and extent of restrictions on competition and the costs and benefits arising from restrictions, inevitably there were cases where anti-competitive legislation was left off the timetable. To deal with this, all jurisdictions accept that, where a genuine case is made for reviewing legislation that was not identified in their original June 1996 legislation review programs, the legislation will be scheduled for review. Jurisdictions regularly update their review timetables.

All up, the schedules cover almost 2000 pieces of legislation. The individual schedules are published in a consolidated format by the National Competition Council (NCC 1997c). A sample of the legislation scheduled for review over the remainder of the NCP review period, demonstrating the broad scope of the overall program, is set out in Box B3.1.

Box B3.1 Selection of legislation scheduled for review over the remaining period of the NCP legislation review program

Jurisdiction	Legislation
Comm	Dairy industry legislation
Comm	Financial Corporations Act
Comm	Intellectual property protection legislation
NSW	Professional Standards Act 1994
NSW	Classification (Publications Films and Computer Games) Enforcement Act 1995
NSW	Rail Safety Act 1993
Vic	Architects Act 1991 and Regulations 1994
Vic	Conservation Forests and Lands Act 1987
Vic	Fisheries Acts and Regulations
Qld	Environmental Protection Act 1994 & Regulations
Qld	Consumer Credit Legislation Amendment Act
Qld	Invasion of Privacy Act 1971 & Regulations
WA	Dental Act 1939 & Regulations
WA	Grain Marketing Act 1975 & Regulations
WA	Taxi Act 1994 & Regulations
SA	Hairdressers Act 1988
SA	Meat Hygiene Act 1994
SA	Landlord and Tenant Act 1939
Tas	Door to Door Trading Act 1986
Tas	Land Use Planning and Approvals Act 1993
Tas	Shop Trading Hours Act 1984
ACT	Education/schooling legislation
ACT	Prostitution Act 1992
ACT	Motor Traffic Act 1936
NT	Retirement Villages Act
NT	Agent's Licensing Act
NT	Housing Act

Source: Jurisdictions' legislation review timetables.

Jurisdictions' progress against their review agendas

Early progress by States and Territories against their legislation review obligations was formally examined by the Council in June 1997 in its first tranche assessment of NCP reform progress. The Council's assessment revealed gaps in some jurisdictions' review programs, which have since been rectified, and a failure by NSW to implement arrangements for the domestic marketing of rice as recommended by an independent review group. Issues relating to domestic rice marketing are discussed in section B3.5. The Council published its first tranche assessment in June 1997 (NCC 1997b).

All jurisdictions have continued to advance their legislation review agendas over the past 12 months. Typical reform outcomes to date include repeal of redundant legislation, streamlining of licence categories, implementation of pro-competitive reforms and, in several cases, retention of anti-competitive arrangements where there is a supporting net public benefit case. However, the information available to the Council suggests there has been some slippage against review objectives set in the June 1996 timetables. For some jurisdictions, there is significant ground to cover if the review and reform program is to be completed by the target date of the year 2000.

Most jurisdictions have undertaken considerable preparatory work, including preparing guidelines for those conducting reviews and external consultants contributing to reviews, and conducting workshops on legislation review matters. Governments have also given some attention to exchanging information on issues and processes, with Victoria and Queensland co-sponsoring a conference for all governments' legislation review practitioners in February 1998.

As expected with any broad program of several years duration, progress is not consistent across jurisdictions. There are several reasons for this.

First, some jurisdictions, for example NSW, Victoria, the ACT and the Northern Territory, have set their programs such that the bulk of their reviews should be completed in the first three years of the NCP program. Others, for example South Australia, scheduled the majority of their reviews for later in the NCP period.

Second, individual jurisdictions' circumstances have required changes in scheduling. For example, the Commonwealth deferred reviews of superannuation and insurance supervision legislation pending a decision in response to the Wallis Inquiry into Australia's financial system. Queensland delayed commencing its review of the *Land Act* from 1996-97 as scheduled until 1998 to allow time for issues concerned with native title to become clearer. The Northern Territory deferred the expected date of completion of the review of its *Mining Act* by two years for the same reason. Jurisdictions have also reorganised timetables, adding new reviews and bringing some matters forward or combining them in broader industry based reviews.

Third, although many legislative review questions have national implications and governments' June 1996 timetables anticipated that a wide range of matters would be dealt with on a national basis, few national review processes have been established. This meant that jurisdictions have had to schedule matters originally listed for national review within their own timetables, and investigate means by which national consistency can be achieved. In some cases, this has caused jurisdictions to defer their own reviews or delay implementing review recommendations pending the outcomes of reviews of similar legislation by other jurisdictions.

The following section summarises the progress achieved by each jurisdiction over the first period of the NCP legislation review program. Because some jurisdictions are still to provide their annual reports for 1998, the Council is not able to indicate overall progress to a common point.

The Commonwealth

The Commonwealth has scheduled around 100 reviews of legislation and associated regulations in its NCP program. About 30 of these had been completed at 31 March 1998.

After satisfactory progress in the early part of the Commonwealth review program, the second year has seen some slippage. At 31 March 1998, only 15 of the 28 reviews scheduled to begin in 1997-98 had commenced and, of

these, only one had been completed. The Commonwealth deferred seven reviews scheduled to commence in 1997-98, was still to begin another five 1997-98 reviews, and deleted the *Wool International Act 1993* from its review schedule. Ten reviews which commenced in 1996-97 were still underway at 31 March 1998.

Notwithstanding the slippage, there have been some significant reform outcomes. Far reaching changes to Australia's financial regulatory structure came into effect on 1 July 1998 in response to recommendations of one of the first NCP reviews, the Financial System Inquiry (the Wallis Committee).[1] In addition, because the Commonwealth's review program focuses on legislation imposing costs or benefits on business as well as restrictions on competition, the outcomes of some reviews have had the effect of reducing costs to business. For example, following review of the *Census and Statistics Act 1905* in 1996-97, the Australian Bureau of Statistics was required to reduce the cost to small business of completing statistical returns by 20 percent and a code of conduct for private statistical collection agencies was introduced.

New South Wales

The NSW legislation review schedule lists some 185 pieces of legislation, with about 80 percent of these scheduled for the first two years of the program. At 1 January 1998, NSW had completed approximately 50 reviews and had a further 66 in progress. Around 30 reviews scheduled for the period to 30 June 1998 were still to be commenced at the end of 1997. NSW is confident that its review schedule should permit the completion of nominated reviews by the year 2000.

NSW is conducting a licence reduction program in conjunction with the NCP process. The Government has reviewed over 250 licences, of which 85 have been nominated for repeal. Some 51 of these have been repealed by

1 The Australian Prudential Regulation Authority (APRA) has been established to take responsibility for supervising banks, life and general insurance companies and superannuation funds. Supervision of building societies, credit unions and friendly societies is expected to transfer to APRA from State-based regulators later in 1998. The Australian Securities and Investments Commission has responsibility for market integrity and consumer protection across the financial system.

administrative action or specific legislation and the remaining 34 were included in the NSW *Regulatory Reduction Act 1996* for staged repeal by proclamation. At 1 January 1998, proclamations had been made repealing 21 licences, with proclamation of the remaining licences awaiting completion of review processes, including reviews under the NCP program.[2] Like other jurisdictions, NSW is also using the NCP process to clean up its statute books by repealing legislation which is redundant and replacing large numbers of industry specific regulations with generic laws.

Victoria

Victoria programmed around 430 Acts and regulations for review between 1996-97 and 1999-2000. About half of these were scheduled to be completed by July 1998.

Victoria conducted several significant reviews during the year, including reviews of barley marketing arrangements (jointly with South Australia), dentistry regulation and liquor retailing arrangements.

The review of the dental professional regulation examined matters such as restrictions on advertising, ownership of dental practices and on who can perform various dental procedures. Following similar reviews of other health professions, Victoria has removed bans on advertising and restrictions on ownership, and reduced or removed restrictions on who can perform certain procedures.

Following the joint review of barley marketing arrangements, Victoria and South Australia have announced removal of the Australian Barley Board's (ABB) domestic monopolies and is considering the future of the ABB's export monopoly. The Victorian Government is expecting to announce its decision on the liquor retailing review late in 1998.

Issues relating to liquor retailing, statutory marketing arrangements within agriculture and professions regulation are discussed in more detail in section B3.5.

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2 Following a NSW Government inquiry into the security industry, four security industry licences will not now be repealed.

Queensland

Queensland has programmed over 170 Acts and associated regulations for review between 1996-97 and 1999-2000. Early reform action by Queensland has included the repeal of a number of pieces of redundant legislation. Queensland anticipates that some other legislation, for example the *Egg Industry (Restructuring) Act 1993*, which provides for restructuring of marketing and regulatory arrangements, will be allowed to sunset within the NCP review period without review.

Queensland had completed about one-third of its NCP program at 1 July 1998. However, the Government is yet to announce a decision in several cases, and several proposals for pro-competitive reform are likely to be considered by the new Queensland Government. Recognising that there have been delays in commencing some reviews, Queensland has brought forward reviews and commenced development of the terms of reference for several reviews scheduled for 1998-99.

Western Australia

Western Australia's timetable lists about 270 pieces of legislation for review, scheduling almost half of these for completion by 30 June 1998. Early action by Western Australia includes the repeal of several pieces of redundant legislation and action to streamline the State's statute base. For example, the *Vocational Education and Training Act* and the *Censorship Act* have each replaced three pre-existing laws. The generic *Port Authorities Bill 1997*, when enacted, will replace a number of individual port Acts.

To date, Western Australia has completed 44 reviews to the stage of Cabinet endorsement. For about half of these, repeal or amendment to remove restrictions has been recommended and is being, or is soon to be, implemented. Another 39 reviews have reached at least the stage of having been submitted to the Western Australian Competition Policy Unit (CPU) for comment. The Western Australian legislation review process involves scrutiny by the CPU aimed at ensuring the quality and rigour of reviews and the appropriateness of the review process.

On the evidence available to the Council, there appears to have been some recent slippage in Western Australia's legislation review program. Against this, Western Australia's legislation review guidelines make it clear that all of the State's reviews of existing legislation are to be completed and review recommendations implemented by the end of the year 2000.

South Australia

South Australia lists around 180 pieces of legislation for review in its legislation review schedule. At May 1998, South Australia had completed 35 reviews, about 20 percent of the State's NCP program.

South Australia undertook several significant reviews over the past 12 months, including of the *Cooper Basin (Ratification) Act 1975*, the *Barley Marketing Act 1993* jointly with Victoria (see section B3.5), and the *Casino Act 1997*.

While South Australia has not completed many reviews to date, its progress is consistent with its legislation review schedule. South Australia has timetabled the bulk of its reviews for 1998 and beyond, leaving the State a larger task over the remainder of the NCP period.

Tasmania

Tasmania's legislation review program lists 236 Acts for review, although the State is now proposing, after preliminary examination, that some 22 of these not be reviewed.

Tasmania appears to be on track with its legislation review program. At April 1998, 42 Acts had been repealed, a further 26 laws were likely to be repealed without replacement, and 48 were expected to be repealed and replaced with legislation consistent with the competition tests. In seven cases, the Government is considering the recommendations of review panels or had decided to retain a restriction. Of the remaining reviews, 25 are underway and 66 are still to commence.

The Australian Capital Territory

The ACT's current NCP legislation review schedule lists over 190 Acts which restrict competition and/or impose significant or unnecessary costs or disadvantages on business. Concurrently with the NCP program, the ACT is systematically reviewing its legislation to remove any unnecessary burdens, costs or disadvantages that regulations place on businesses in the ACT.

Most of the ACT's reviews are scheduled to commence, at the latest, by the first half of 1999. This timing should allow the ACT Government sufficient opportunity to ensure that review recommendations are implemented by the year 2000. The Territory is yet to finalise review arrangements for some 18 pieces of legislation.

The Northern Territory

The Northern Territory scheduled its NCP legislation review program over three years from June 1996, with the majority of its reviews scheduled for completion by June 1998. At the end of December 1997, some 39 of the 43 reviews scheduled for commencement by June 1997 were either underway or completed.

There has been some slippage in the Northern Territory program. The Northern Territory indicated that it is aware of this and that it is taking steps to ensure all reviews are completed and, where possible, outcomes implemented, by 31 December 2000.

Two reviews have been rescheduled consistent with national processes. The start date for review of the Pharmacy Act was deferred from December 1996 to comply with a proposal by the Commonwealth for a national review of pharmacy regulation commencing in 1999. The review of the Water Act and Water Regulations has been rescheduled to link with COAG's water reform agenda. In addition, implementation of the recommendations arising from the review of the Architects Act has been delayed pending all governments resolving whether professions regulation is to be considered on a national basis.

Progress with national reviews

While most reviews are conducted by individual jurisdictions, the NCP also provides scope for joint-jurisdictional and national reviews. The attraction of a national approach to review is that it proffers synergies and benefits, particularly where it results in a uniform regulatory position across all jurisdictions. This removes unnecessary compliance costs and barriers to business, and the scope for regulatory arbitrage.

To date, national reviews are underway or being considered for:

- legislation regulating the registration and use of agricultural, veterinary and industrial chemicals;
- mutual recognition arrangements;
- the legislative and regulatory arrangements affecting travel agents made in relation to the National Cooperative Scheme for the Regulation of Travel Agents;
- State and Territory legislation regulating the operation of pharmacies, and any relevant Commonwealth legislation; and
- standards for drugs and poisons.

In other cases, governments are tackling particular categories of legislation on a nationally consistent basis. For example, all States are adopting a nationally consistent approach to reviews of their fisheries legislation. Western Australia is acting as the lead jurisdiction on this matter and commissioned the Centre for International Economics (CIE) to produce a model assessment framework (CIE 1998). Such an approach to 'national' issues facilitates consideration of the benefits of consistency in regulatory standards.

Apart from national reviews involving all nine governments, the CPA provides for inter-jurisdictional approaches encompassing two or more governments. South Australia and Victoria have jointly reviewed legislation establishing the Australian Barley Board (see section B3.5).

B3.4 Implementation issues

The experience of the first two years of the NCP legislation review and reform program suggests that there are three areas which warrant greater attention by governments.

First, in some instances, governments failed to schedule for review legislation that contains provisions restricting competition, or to demonstrate that proposals for new restrictive legislation met the competition tests. Second, there is evidence that some review processes have been inadequate. Third, there has been a failure by some governments to act in accordance with review recommendations where pro-competitive reform is shown to be in the community interest.

Scope of legislation review programs

Changes to jurisdictions' programs

Despite there being nearly 2000 pieces of legislation scheduled for review, it is inevitable that there will be cases where restrictions on competition which warrant review have been missed. Indeed, such gaps are likely to become more apparent as the community's awareness of the legislation review program increases.

All jurisdictions have been amenable to adding legislation to their review programs when omissions containing restrictions on competition are identified. For example, Western Australia has added over 20 Acts to its original review schedule, and South Australia and the Northern Territory have added four and three pieces of legislation respectively. The Commonwealth has added Part IIA of the *Health Insurance Act 1973*, which contains provisions regulating the number of pathology outlets that can provide services eligible for Medicare benefits. This was an area of deficiency in the Commonwealth's program reported in the Council's previous annual report.

Jurisdictions have also removed legislation from their review schedules. For example, following consultation with the Council, Queensland removed the *Liquid Fuels Supply Act 1984*, the *Explosives Act 1952* and the *Explosives Regulation 1955* from its review schedule. Tasmania has removed some 22 pieces of legislation after a preliminary examination revealed they contained no restrictions on competition. The Council does not oppose such removals where closer scrutiny reveals that any impact on market participants is non-discriminatory and where the jurisdiction discloses the change in its annual report.

To assist community awareness of the legislation review program and encourage public scrutiny of this aspect of the NCP, the Council publishes a compendium combining all governments' review programs. First published in April 1997, the compendium is being updated with the help of all jurisdictions for re-issue later in 1998. Jurisdictions' annual NCP progress reports also help raise public awareness of the legislation review program.

New legislation which restricts competition must be shown to provide a net community benefit

Under the NCP, governments must explicitly demonstrate that new and amending legislation which restricts competition complies with the competition tests: that restrictions on competition generate a net community benefit and restricting competition is the only means of achieving the objective of the legislation. The responsibility to do this applies in relation to all new legislation restricting competition enacted since the signing of the CPA in April 1995.

Each government has a mechanism for examining proposals to introduce new legislation and amending legislation. These mechanisms are generally units within the machinery of government, rather than independent bodies, and advise governments on regulatory issues and proposals for new legislation. For example, in NSW, all proposals for new legislation or amendments to existing statutes are reviewed by Cabinet Office officials. The Commonwealth requires a formal assessment of proposed changes to regulations that impact on business or restrict competition by the responsible agency oversighted by the Office of Regulation Review (ORR).

Typically, assessments of new restrictions on competition:

- involve examination of the incidence and, where possible the magnitude, of competitive restrictions, as well as alternatives to regulation;
- take the form of a regulation impact statement (RIS), a public interest test or a competition test;
- are coordinated by a central agency; and
- require inconsistencies between the legislation and NCP requirements to be referred to Cabinet or to the responsible Minister.

Processes such as assessment of regulatory impacts are intended to provide a consistent, systematic, and transparent means of assessing alternative approaches to problems which may require some government action. They involve identification of the problem giving rise to the need for action and the desired objectives of regulation, consideration of options for achieving these objectives, assessment of costs and benefits including compliance and impacts on small business, a recommended option and a strategy for achieving the recommended option.

All States and Territories added to their legislation review programs after scrutiny of legislation, enacted since April 1995, revealed that some restrictive legislation had not been scheduled for review. For example, on behalf of the ACT Government, the Productivity Commission is examining the justification for amendments to the ACT *Animal Welfare Act 1992* and *Food Act 1992*, which imposed new restrictions on the marketing and distribution of eggs within the ACT without a public benefit test. NSW added the *Superannuation Administration Act 1996*, which provides for trustees for State public sector superannuation schemes and the provision of investment and administration services for such schemes, to its review program.

The Commonwealth is examining legislation enacted since April 1995 for consistency with competition principles, in the face of evidence that Commonwealth Departments did not make full use of the Commonwealth RIS process in the early part of the NCP program (IC 1997c). Notwithstanding this, the Commonwealth is still to provide a substantive net

public benefit case in support of its 1996 legislation limiting Medicare provider numbers available annually to new doctors. This legislation restricts entry to medical practice and was identified by the Council in its previous annual report as requiring a net benefit justification if the Commonwealth is to be regarded as meeting its competition policy obligations.

Review and reform processes

Throughout the first two years of the program, the Council has consistently emphasised that objective review processes aimed at genuine reform outcomes are critical to achieving the community benefits envisaged by COAG. Important elements of the NCP legislation review process include:

- ensuring the terms of reference address the competition issues, including non–regulatory alternatives;
- having in place processes for public participation;
- ensuring independence of the review process and objective consideration of the evidence;
- implementing reform outcomes having regard for review recommendations; and
- completion of the program by the end of the year 2000.

All governments now have guidelines to assist their review bodies. These guidelines outline the review requirements arising from the CPA and cover procedures for examining net community benefit. Jurisdictions also conduct workshops and seminars to assist those undertaking the legislation reviews to understand the review frameworks and to discuss practical problems confronting reviewers. For example, the WA Government has held general introductory workshops on conducting reviews as well as workshops on specific regulation review matters.

Review terms of reference

The terms of reference for NCP reviews must allow for investigation of the restrictions on competition contained in legislation and assessment of the

costs and benefits of those restrictions. Most jurisdictions develop a formal terms of reference reflecting these objectives for each review using a template terms of reference based on the CPA.

There is evidence that some reviews, particularly those scheduled early in the review program, did not address fundamental NCP questions. For example, the Commonwealth review of the *Quarantine Act 1908* focused on increasing the internal efficiency and effectiveness of institutions administering plant and animal quarantine but did not appear to assess the justification for any associated restrictions on competition. Similarly, the terms of reference for the 1997 review of the *Commonwealth's National Health Act 1953* (Part 6 and Schedule 1) and the *Health Insurance Act 1973* (Part 3) undertaken by the Industry Commission, prevented the Commission from considering community rating, which is a significant regulatory influence on the nature of price and product competition by health funds (IC 1997a).

The Commonwealth is proposing to rectify the deficiencies in its review of the Quarantine Act by identifying those elements of the Act which restrict competition and which were unchanged following the review (if any), and subjecting these to a review consistent with clause 5 of the CPA.

Independence of review panels

Concerns relating to the independence of review panels continue to be brought to the Council's attention. These concerns generally relate to a perceived bias of industry members of review panels and, consequently, the potential pre-empting of review recommendations. Because there is almost inevitably conflict between some views, independence is particularly important in engendering confidence that all information and views presented to a panel are objectively considered.

There is obviously a need for industry representatives and members to participate in reviews of legislation affecting their industry. Among other things, they will have a detailed knowledge of the industry structure and the markets it operates in. They may be well placed to suggest useful options for reforming the relevant legislation, and are likely to be directly affected by any reform proposals.

The Council considers that the best means of incorporating input from industry representatives is through submissions and providing information to review panels. Ideally, however, so that reviews are objective and aim at genuine reform opportunities, the Council considers that there should not be industry representation on review panels themselves. Similarly, while the Council considers that government officials responsible for promulgating and/or administering particular regulations are well placed to have input into reviews of those regulations, it is cautious about situations in which such officials are appointed to review panels. This is because there is a risk that officials who administer regulations may get too close to the regulation and develop an interest in maintaining it.

Jurisdictions' approaches to ensuring the independence of their review processes differ. Only Victoria explicitly encourages the use of independent review panels in its review guidelines. Other governments suggest that, for important reviews, independence can be achieved through appointing an independent chairperson, and for less important reviews, by appointing an independent panel member to perform the role of 'honest broker'.

Public involvement in review processes

Review processes adopted by governments vary in nature reflecting to some degree the diversity of the legislation on governments' programs and their views about the likely extent of public involvement. Most governments adopt a range of review models:

- at one extreme, full scale public reviews are undertaken, often by an independent consultant, particularly where removal of legislative restrictions involves complex technical issues and/or matters of significant community interest; and
- at the other extreme, internal reviews are used, for example for matters where government policy is already clear or where legislation is redundant, and there is expected to be minimal requirement for public consultation.

Even in cases where public participation is likely to be minimal, governments' legislation review guidelines generally encourage public participation, including through advertising the commencement of each

review, disseminating information, consultation and meetings, and acceptance of submissions.

Despite this, one of the matters consistently raised with the Council by members of the community is the appropriate level of publicity about reviews and opportunity for public involvement. Typical concerns include failure to clearly advertise the commencement of reviews of restrictions which have a significant impact on the community and failure to allow access to discussion papers or to make review reports public.

The Council sees the differentiated approach as generally appropriate. Given the size of the overall review program and the varied nature of legislation programmed for review, there will be some matters which are satisfactorily addressed by internal review. At the same time, the Council emphasises the importance of robust processes and full opportunity for public participation for reviews of legislation which have far reaching effects on the community or particular groups within the community, or to which the community is particularly sensitive.

As the Council emphasised in its previous annual report, unless it can be convincingly demonstrated that open processes would impose net community costs by, for example, invoking 'sovereign risk' problems,[3] reviews should be conducted in an independent, open and transparent way, against clear terms of reference, and in a manner that allows interested parties to participate. Indeed, the explicit provision in the CPA for assessment of the costs and benefits of restrictions on competition suggests that the arbitrary exclusion of interested parties from review processes is contrary to the intent of NCP.

3 'Sovereign risk' type problems may arise, for example, in relation to the review of agreement or ratification Acts. These Acts are sometimes used by governments to facilitate large scale and/or complex development projects, particularly in the resources sector. Agreement Acts result from the ratification by Parliaments of agreements reached by negotiation between a government and project proponent. They are essentially contracts between a government and the project proponent, setting out the long term arrangements, rights and obligations of both parties, and providing increased certainty for investors. Some governments consider that "perceptions of capricious action by Government have an immediate and dramatic effect on levels of investment". They believe that such 'sovereign risk' problems are likely to pose significant risks for major economic activity, warranting either exempting agreement legislation from review or exposing it to a truncated review process only.

There several documents in the public arena which can help interested parties find out about review activities, including:

- governments' legislation review timetables;
- governments' annual NCP reports, which outline among other things progress against the objectives set out in their review timetables;
- the Council's Legislation Review Compendium; and
- the Council's assessment of governments' first tranche performance against NCP obligations.

The major source of information on specific reviews is the National Competition Policy Unit in each jurisdiction. Contact details are listed at the end of this report.

Legislation review guidelines

As mentioned above, all jurisdictions now have guidelines to assist review bodies, outlining review requirements arising from the CPA and covering procedures for examining net community benefit.

While every jurisdiction's guidelines address process matters such as those above, there is considerable variability in the breadth of coverage and the emphasis on various aspects. Some guidelines, such as those produced by Victoria, Western Australia and Tasmania, provide considerable detail about most elements of the review process while others are little more than expansions of the relevant clause in the CPA. Most of the guidelines recognise the need for public participation in reviews, but only the Victorian guidelines explicitly encourage the use of independent review panels. All note the need for demonstrating a net community benefit where restrictions on competition are to be maintained, but vary in their treatment of how to undertake a public benefit analysis and what is acceptable in particular cases.

Recognising the critical importance of review processes to the success of the program, and that most of the concerns raised with the Council to date have centred on process matters, the Council is giving consideration as to how it might help to facilitate robust review procedures. For example, in view of the variability in the guidelines, and the evidence that some review processes

have been less than satisfactory, the Council is giving consideration as to whether, in consultation with jurisdictions' competition policy units, it should develop a model review framework.

Implementing review recommendations

Achieving the benefits from the legislation review program is not just about conducting good reviews. Its also about timely implementation of the recommendations of those reviews.

The NCP objective is that all reviews of legislation, and implementation of appropriate reforms, are completed by the end of the year 2000. All jurisdictions have given at least an in principle commitment to achieving this, albeit most have foreshadowed the possibility that changes to certain arrangements may need to be phased in beyond 2000. The Council regards completion by the end of the year 2000 as a key commitment, and emphasises that delay in implementation beyond 2000 requires a robust net public benefit justification. In this regard, the information available to the Council (summarised in section B3.3) suggests that some jurisdictions are broadly on track while others have a considerable task over the next two years.

Assuming that reviews are thorough and objective, the Council looks for timely implementation of reforms which have regard to review findings. Where governments do not implement recommended reforms, they need to provide a bona fide public interest justification to support maintenance of the restriction on competition. Similarly, a public interest case is needed where new or amended legislation introduces a restriction on competition.

B3.5 Some key review areas in 1997-98

Governments' legislation review and reform effort has encompassed a wide range of areas over the first two years of the program. This section examines areas of the program which have proven more complex over the last 12 months.

Agricultural marketing arrangements

In its previous annual report, the Council foreshadowed emerging issues in relation to the review and reform of some statutory marketing arrangements (SMAs) for agricultural products. Subsequently, the Council's first NCP progress assessment in June 1997 identified the refusal by the NSW Government to liberalise its arrangements for the domestic marketing of rice, in line with the recommendations of the NSW Government's 1995 review, as an NCP compliance failure.

The review and appropriate reform of SMAs is a central competition matter. This is because arrangements underpinning SMAs are prima facie anti-competitive. Typically, they include centralised marketing boards with powers to compulsorily acquire or vest the entire crop, set quality grades and prices, and act as the single seller of the acquired product on either or both the domestic and export markets. In short, producers can sell their product only to the marketing body and customers can buy the product only from the marketing body.

Proponents of SMAs argue that the arrangements are necessary in order to:

- maximise grower income;
- stabilise prices, production and/or producer income;
- achieve price premiums based on market power, particularly in export markets;
- achieve economies of scale in marketing; and
- countervail the market power (real or perceived) of buyers and corrupt international markets.

Supporters of less regulated arrangements argue that there are significant benefits from freeing up compulsory marketing structures, including:

- freedom for farmers to choose how, when and to whom they sell their crops, and freedom to set the sale price;
- greater control by farmers over their production, marketing and risk management decisions;
- reduction in the share of a farmer's returns soaked up in administration costs;

- greater incentives and opportunities for individual farmers and rural communities to undertake more innovative marketing and to invest in higher-value post-farm production; and
- potential growth in industries which are major consumers of agricultural products such as food processing, and benefits to consumers.

Supporters can also point to a number of agricultural industries that have prospered without statutory marketing monopolies (see Box B3.2).

Assessment of the relative magnitude of costs and benefits such as those above is sometimes complicated, and needs to be considered on a commodity by commodity basis. For example, consideration of whether arrangements enable the exercise of market power sufficient to obtain price premiums on export markets will be influenced by the nature of the product and the relative importance of Australia as a producer. Furthermore, where price premiums are observed, these may be due to factors other than market power, such as effective marketing strategies or economies of scale in transport.

The task for governments under NCP is to assess whether the restrictions on competition which underpin SMAs are justified. For anti-competitive arrangements to be retained, it must be demonstrated that the benefits to the whole community (including primary producers) from each restriction outweigh the costs of that restriction and that the benefits to the community cannot be achieved without the restriction. Objective investigation of these matters is in any case important in ensuring that the environment facing producers and agricultural businesses is sufficiently innovative to allow each industry's potential to be fully realised.

NSW rice marketing arrangements

In 1995, the NSW Rice Review Group (the Review Group) recommended that the domestic rice marketing monopoly held by the NSW Rice Marketing Board (the Board) be deregulated, finding that this would deliver a net community benefit. The Review Group found a case for retaining the Board's export monopoly, noting that this achieves benefits for rice growers and Australia as a whole.

Box B3.2 Some agricultural industries without statutory marketing monopolies

Some of Australia's large agricultural industries have SMAs acting as monopoly sellers on domestic or export markets. However, many agricultural industries have developed and prospered in the absence of these types of marketing arrangements. Some examples are provided below.

Cotton

- Australian raw cotton is marketed under a competitive market system.[a]
- Exports, which today account for more than 90 percent of the total cotton crop, have risen from less than 6000 tonnes in 1976-77 to over 310 000 tonnes (or $760 million) in 1995-96.
- Average returns in the cotton industry have been substantially higher than in most other agricultural industries over the past decade.
- Cotton growers have survived and prospered through achieving economies of scale and applying sophisticated production technologies and marketing strategies.

Winegrapes and wine

- Australian winegrape and wine industries are largely free from statutory marketing arrangements.[b]
- Wine exports have increased from just 11 million litres in 1985-86 to 194 million litres (or a record $813 million) in 1997-98. Expectations are for continued strong export growth.
- Export success has been achieved through focused brand development, strong distribution relationships, the use of high technology and, more recently, a greater emphasis on higher margin red wines.

Box B3.2 …cont

Red meat

- In 1997, a producer-owned company, Meat and Livestock Australia, was established to undertake most of the research, development and promotion activities previously carried out by two statutory authorities, the Australian Meat and Livestock Corporation and the Meat Research Corporation.
- As before, there are no single desk marketing arrangements under the new arrangements.
- Annual beef production is valued at around $4 billion, with sheep and lamb production valued at around $150 million and $420 million respectively. Exports of meat and livestock totalled $3.4 billion in 1995-96.

Sources: ABARE (1996), NFF (1998), ACIL (1998).

a The Queensland Cotton Board operated as a statutory marketing authority in Queensland until 1989, at which time the industry was deregulated (with producer support) bringing it in line with NSW.

b The one exception is in the Murrumbidgee Irrigation Area in NSW, where the Wine Grapes Marketing Board has the capacity to act as a single seller of grapes from the region. Following a review of these arrangements, the Board's vesting power is to be extended until 31 July 2000 and then cease. The Australian Wine and Brandy Corporation administers export licensing arrangements and labeling standards, as well as undertaking some generic industry export promotion.

The Review Group proposed that deregulation be implemented by not renewing the power for the NSW rice crop to vest in the Board when its (then) current powers expired after 31 January 1999. However, contrary to this recommendation, the NSW Government decided to retain the existing vesting arrangements until 31 January 2004, with a review in 2002 to consider whether changed market conditions justify any alterations.

In its first tranche assessment of NCP progress in June 1997, the Council identified NSW decision not to reform its domestic rice marketing arrangements, consistent with the Review Group finding, as a compliance

failure. In essence, the Council was not satisfied that NSW had complied with the obligation under clause 5 of the CPA to retain an anti-competitive arrangement only where a net community benefit can be demonstrated. It is important to note that the Council's decision did not extend to the single desk export monopoly, which the Review Group had found to provide a benefit to Australia as a whole.

Following an undertaking from the NSW Government in June 1997 to enter into 'meaningful discussions' on the reform of domestic rice marketing arrangements, the Council agreed to reassess the matter prior to July 1998.

In the ensuing twelve months, NSW had opportunities to comply with its NCP obligations, either by liberalising its domestic rice marketing arrangements or offering a net community benefit case for retaining domestic restrictions. Despite extensive discussions with the Council, NSW offered no substantive additional information or justification for its decision. NSW claimed that it is not possible to deregulate the domestic rice market and retain effective monopoly export arrangements, although it provided little evidence to justify why domestic and export arrangements could not be decoupled as recommended by the Review Group.

In June 1998, the Council assessed NSW as not having met its commitments under clause 5 of the CPA with respect to domestic rice marketing. The Council recommended that the Commonwealth deduct $10 million from the 1998-99 component of NSW's first tranche NCP payments, but that the deduction not apply until after 31 January 1999 – the date for domestic market deregulation as recommended by the 1995 Review Group. The Council based its recommended penalty broadly on the costs that the Review Group estimated fall on the Australian community as a result of the current domestic arrangements.

The Council is continuing to work with the NSW Government and industry representatives to resolve this matter consistent with the interests of the Australian community. This includes ensuring not only that consumers benefit from lower prices through the elimination of income transfers to producers, but also that the rice industry is able to innovate and capitalise on opportunities – such as export and regional employment opportunities through investment in value adding activities (such as rice flour, crackers and noodles).

The Council will recommend that the $10 million deduction not be imposed if, prior to 31 January 1999, the NSW Government deregulates the domestic rice market as recommended by the 1995 Review Group. However, until the matter is resolved, the Council will continue to take it into account in assessing the extent to which NSW is complying with its NCP obligations in future assessments.

Noting the Council's recommendation, the Commonwealth Treasurer announced on 21 August 1998 that he will defer a decision on whether NSW should have a penalty applied to its 1998-99 NCP payments pending advice on the result of further work in this area.

The Australian Barley Board

The Australian Barley Board (ABB) is established under the *Barley Marketing Acts 1993* in South Australia and Victoria. The legislation provides the ABB with the power to compulsorily acquire and market the barley crop in these both States and oats in South Australia.

These powers impose significant restrictions on competition. The export of unprocessed barley (and oats in South Australia) is prohibited unless by or through the ABB. Growers cannot deliver barley to anyone other than the ABB, and purchasers cannot buy from growers unless purchasers have a permit for feed barley or a licence for malting barley. Licences and permits are issued by the ABB.

The Victorian and South Australian Governments commissioned a joint review of the legislation underpinning the ABB (CIE 1997). The review, by the CIE, examined whether:

- the ABB's compulsory acquisition and single desk export power enable it to extract price premiums in export markets;
- the ABB's single desk is a necessary or appropriate response to the power of central buying agencies in overseas markets, or of buyers in Australia;
- government intervention is needed to achieve economies of scale in marketing; and

- these restrictions provide a net benefit to the Australian community and, if so, whether the net benefit is achievable only by restricting competition.

The CIE concluded that the ABB's single desk export power did not enable it to extract price premiums in any overseas market for either feed or malting barley. In the two markets the CIE did find price premiums, it noted that these arose for other reasons. For feed barley, the CIE found a price premium in the Japanese market resulting from Japan's food security and trade policies. For the United Arab Emirates, the CIE found that better prices are due to the special characteristics of South Australian feed barley and savings on freight costs.

The CIE found no case for maintaining the single desk to countervail the buying power of overseas buyers of barley. It also concluded that there is no national interest case for restricting competition to achieve economies of scale in marketing or finance, noting that the ABB is not large compared with some alternative marketers.

Similarly for oats, the CIE found no evidence of net benefit, including any price premium in any market, arising from the anti-competitive provisions of South Australia's *Barley Marketing Act 1993*. The CIE noted that Eyre Peninsula Growers could easily form a co-operative to co-ordinate their marketing effort and sell to the trade as the ABB does at present if they see a benefit in this.

For the reasons above, the CIE recommended that:

- the domestic market for feed and malting barley in South Australia and Victoria be deregulated;
- the oats market in South Australia be deregulated; and
- the single desk export power of the ABB be abolished after a short transition period to allow development of alternative marketing structures.

The Council considers that the CIE review presents a robust case in support of its findings. Both jurisdictions have announced deregulation of the domestic feed barley market from 1 July 1998, deregulation of the domestic

malting barley market from 1 July 1999 and the privatisation of the ABB into a grower owned company before the end of 1998.

The Council looks forward to an early decision by the two governments on the ABB's export monopoly. Noting that the CIE review found no evidence that the ABB has been able to exert market power to extract price premiums in world markets because of its single desk power, the Council would expect the governments to abolish the single desk arrangement for exports as recommended by the CIE.

The Australian Wheat Board

In December 1997 and July 1998, the Commonwealth Government enacted legislation to privatise the Australian Wheat Board (AWB) into a grower owned company. The legislation extends the existing wheat export monopoly indefinitely and vests its management in a new statutory body, the Wheat Export Authority (WEA).

The *Wheat Marketing Act 1989* (the WMA) provides a subsidiary company of the privatised AWB with a five year automatic and exclusive right to export wheat. Requests to export wheat by other parties will be managed by the WEA in consultation with the AWB. In 2004, the WEA will conduct a review to assess the performance of the AWB subsidiary in its use of the export monopoly, including whether the company should continue to have the exclusive export right (Parliament of the Commonwealth of Australia, House of Representatives 1998b). The AWB subsidiary's exclusive export right is perpetual. It can only be discontinued if the Commonwealth Parliament amends the WMA.

The Commonwealth's extension of the AWB's export monopoly suggests a step away from full compliance with the competition policy obligations set out in clauses 4 and 5 of the CPA. The Commonwealth has, however, given an undertaking that its NCP review of the WMA, scheduled for 1999-2000, will examine all aspects of the legislation underpinning wheat marketing arrangements, including the WEA and the export monopoly, in accordance with the NCP principles.

For compliance with its NCP legislation review obligations, if the export monopoly is retained, the Commonwealth's 1999-2000 review will need to demonstrate that the monopoly provides a net benefit to Australia. Essentially, this means showing that the AWB is able to exert market power in the world wheat market such that it can achieve a price premium for Australian wheat. As the CIE review indicated in the case of barley, improved returns to growers from efficiencies such as economies of scale in transport and storage are not a result of market power and may be captured through voluntary arrangements authorised under the Trade Practices Act (TPA).

Clause 4 of the CPA obliges the Commonwealth to review the structure and commercial objectives of the AWB prior to privatisation. This includes, amongst other things, that arrangements for the regulation of the wheat industry, including arrangements for managing the export of wheat, are independent of any successor to the AWB. The Commonwealth has so far given no indication that it intends to examine clause 4 matters relating to the AWB.

The Commonwealth's current legislative activity with respect to the AWB, and the outcome of the 1999-2000 review, will be important indicators of the Commonwealth's compliance with its NCP obligations in this area.

The Australian dairy industry

Dairy farming is Australia's fourth largest rural industry, operating in all States and Territories except the Northern Territory. Victoria is the largest producer in Australia, accounting for more than 60 percent of annual milk production. NSW, with some 13 percent of production, is the second largest producer.

Raw milk is used as either 'market milk' (which is processed into fresh drinking milk) or 'manufacturing milk' (which is used in the production of manufactured dairy products such as milk powder, cheese and butter). Much of the economic regulation of the dairy industry is directed at the market milk sector. The manufacturing milk sector, which has a strong export focus, is relatively lightly regulated.

Dairy corporations in each jurisdiction have generally controlled the industry, with the key restrictive provisions typically involving price setting and supply management, regulation of food standards and provision of compulsorily funded industry services. In most States, arrangements beyond the farmgate are now deregulated. [4]

Each State is reviewing its dairy industry legislation under the NCP program. Some have already completed their reviews.

The NSW review was completed in November 1997 and publicly released in May 1998. Members of the Review Group were unable to agree on whether farmgate prices and supply management arrangements for market milk should be deregulated. The NSW Government announced it would not consider deregulation at the farmgate before 2003.

The Queensland review, which was completed in July 1998, recommended that regulated farmgate prices be retained until at least 31 December 2003, with any extension beyond 2003 being subject to further review before 1 January 2003. The Queensland review recommended that these arrangements should be reviewed earlier if industry changes and/or market forces compel a shortening of the transition process.

The ACT review, which reported in June 1998, recommended that post-farmgate arrangements be deregulated but that regulated farmgate prices for market milk be retained.

Victoria and Western Australia are expecting to commence their reviews in the second half of 1998. South Australia and Tasmania are awaiting the recommendations of the Victorian review before commencing their own examinations. Because of the dominance of the Victorian industry, the outcome of the Victorian review is likely to be an important consideration in determining arrangements for eastern and southern Australia. The Commonwealth is scheduled to review its dairy industry arrangements in 1998-99.

4 In the early 1990s, all States agreed to deregulate post-farmgate dairy prices and supply arrangements. Deregulation of post-farmgate arrangements has now occurred in all States except Queensland, where it is scheduled to occur on 1 January 1999.

Given the size and importance of the Australian dairy industry, the Council considers the review and, where appropriate, reform of restrictions on competition in the industry to be an important component of the NCP agenda. The Council will take account of the decisions taken by each government in future assessments of NCP progress. In particular, the Council will want to be convinced that, consistent with the CPA, any decision to retain farmgate pricing and supply management arrangements is in the interests of the Australian community.

Regulation of the professions

In the past, many professions had been shielded from normal competitive pressures through specific legislative and/or self-regulatory arrangements. They have also been exempt from the prohibition on anti-competitive behaviour contained in Part IV of the TPA. Typical elements of the regulatory landscape include professional associations, guilds and/or registration boards with the power to admit members to the profession, to regulate their standards and conduct, often through a code of ethics and, in some instances, to set schedules of fees. There have also been controls on ownership structures, and the reservation of certain work to members of the profession alone. In some cases, there have also been internal functional distinctions made as, for example, in the split between barristers and solicitors (see Box B3.3 for examples).

From a competition policy viewpoint, certain aspects of professional regulation may well be justified. In the market for medical services, for example, the availability of subsidised health care, and the fact that doctors both advise patients of the need for treatment and supply the service, mean that some form of regulation may be necessary to ensure that doctors do not over-service their patients. The information problems consumers face in selecting a practitioner of suitable capability may also justify regulation of entry into a profession through appropriate accreditation standards and reservation of professional title.

But some traditional forms of professions' regulation appear to do little other than to restrict competition to the benefit of professional practitioners. For example, prescribed fee scales for professional services appear to be designed

Box B3.3: Some forms of professions regulation which can affect competition

The legislation applying to professions can effect the market structure and conduct of these practitioners. Market structure can be affected through:

- restrictions on the use of professional titles;
- restrictions on entry into the market by professionals, para-professionals and other potential suppliers — such as licensing, certification requirements, educational and competency standards;
- functional splitting — arrangements where certain professions or persons within professions are not permitted to compete with each other; and
- restrictions on the ownership and organisation of professional practices.

Market conduct can be affected through:

- fee scales and fee limits;
- restrictions on certain types of advertising; and
- professional and ethical standards and disciplinary procedures.

primarily to limit competition. Similarly, where accreditation standards are set at unnecessarily high levels, they have the potential to exclude suitable service providers from the market.

There has been some reform of professional regulatory restrictions in recent years. For example:

- restrictions on the advertising of legal services have been lifted in most jurisdictions, and conveyancing is now (except in Queensland) open to non-lawyers;

- following reviews of various health professions, Victoria has removed bans on advertising and restrictions on ownership, and has reduced or removed restrictions on who can perform certain procedures;
- 'mutual recognition' of entry standards has removed some State-based barriers to competition within professions;
- the implementation of the NCP Conduct Code Agreement has extended the reach of Part IV of the Trade Practices Act to professional partnerships and individual practitioners; and
- some professional associations have revamped or are revamping their accreditation schemes.

However, for several professions, there remains a significant body of anti-competitive legislation. Provisions setting controls on advertising and ownership structures, price scheduling, and licensing schemes which restrict the number of practitioners rather than set reasonable minimum entry standards, are all areas of professional regulation which the Council considers should be subject to review and, where appropriate, reform under NCP.

The Council has discussed the NCP program with representatives of professional groups, including the Australian Council of Professions (ACP) Competition Policy Committee. A key objective for ACP is that arrangements, including review processes, recognise and facilitate national professions markets. ACP emphasises the desirability of reviews being undertaken on a national basis to facilitate consistent outcomes across all jurisdictions. ACP has also signalled that reservation of professional title is a central consideration for its members.

All jurisdictions have scheduled legislation regulating many professional and occupational groups for review over the period of the NCP legislation review program, often proposing a national approach. Some jurisdictions have deferred their own reviews, and the Northern Territory has deferred consideration of the findings of the review of its Architects Act, pending a decision by jurisdictions on a national approach. However, although discussions are occurring on the possibility of national reviews, at this stage there is agreement to a national approach only in respect of the legislative

restrictions affecting travel agents in relation to the National Co-operative Scheme and the review of legislation implementing the 1993 Mutual Recognition Agreement (MRA).[5]

The Council sees considerable benefit from reviewing the regulations affecting various professions on a national basis. The Council sees the area of professions regulation as an important NCP review matter and will continue to pursue sensible review processes and reform outcomes consistent with maximum community benefit.

Retailing restrictions

Several governments have recently reviewed or are currently examining restrictions on shop trading hours and licensing arrangements for liquor retailing.

Shop trading hours

Shop trading hours is an area that most jurisdictions have examined or propose to examine under the NCP legislation review program.[6]

Victoria deregulated its shopping hours in 1996. The ACT repealed its *Trading Hours Act 1996* in 1997 after it became clear that the restrictions did not provide a net public benefit. The Act restricted the trading hours of retailers in the larger shopping centres. In both jurisdictions, shops now have the choice of trading up to 24 hours a day.[7] In these jurisdictions, many large supermarkets now choose to trade 24 hours a day, and in some cases seven days a week, reflecting their response to consumer demand.

5 Under the MRA, each Australian government has agreed to recognise each other's regulations covering the registration of occupations and the sale of goods.

6 There is no legislation regulating shop trading hours in the Northern Territory.

7 In Victoria, a municipality can choose not to allow 24 hour trading if a referendum of eligible voters supports it.

NSW regulates trading hours through the *Factories, Shops and Industries Act 1962*. Some provisions of this Act, such as those regulating occupational health and safety practices and the licensing of hairdressers, are being reviewed by the NSW Government, although examination of trading hours arrangements has not yet commenced. However, trading hours regulation in NSW is already less restrictive than in many other jurisdictions.

Other States are reviewing or propose to review restrictive shop trading regimes. For example, in Queensland, trading hours vary throughout the State, and discriminate between stores according to size, ownership structures and location. In Western Australia, factors such as the number of employees a retailer has and the goods it sells have implications for trading hours. Trading hours in South Australia are also relatively restricted. Reviews of trading hours regulations are currently underway in these States. Tasmania's review is scheduled for 1999.

Studies have found a range of benefits from deregulation of trading hours, including increased consumer convenience and additional retail activity. Preliminary evidence from Victoria suggests that some of the disadvantages which opponents commonly attribute to deregulation of trading hours are not evident. For example, despite claims of increases in retail business failures, there has been no decline in net retail employment in Victoria since shopping hours were liberalised.

Liquor retailing

All States and Territories have examined or propose to examine their laws governing the sale of liquor through retail outlets. The extent to which these laws restrict liquor sales varies across jurisdictions. Some examples are provided below.

Queensland and Tasmania are the only States which limit the operation of take-away liquor outlets to hotels and associated premises. Queensland imposes an additional requirement on the operation of 'detached bottle shops', restricting approvals for these to hotels and limiting the number of bottle shops any one hotel can establish.

Box B3.4 Deregulated shop trading hours in Victoria

Deregulation of shop trading hours in Victoria commenced in December 1996. One of the outcomes is that some large supermarkets have chosen to remain open for 24 hours a day, seven days a week.

Studies have demonstrated a range of benefits associated with longer opening hours. For example, one study (Brooker and King 1997) projected that increased opening hours would generate, in the long term, a net benefit to consumers in terms of increased convenience valued at about $330 million (or $65 per person) per year, additional retail demand of 0.6 percent and a rise in retail employment of around 2.0 percent (around 6 000 jobs in Victoria). The study projected the increase in trading hours in Victoria, if extrapolated nationally, to translate to 25 000 additional jobs.

Other studies have identified other benefits, including wider product choice, longer opening hours and lower prices. For example, a recent *Choice* survey (Australian Consumers Association 1998) found that prices for some items at late night supermarkets are almost half that of the same items in some late night convenience stores. *Choice* found prices for items sold in convenience stores to be, on average, around 43 percent higher than prices in supermarkets.

Deregulation of shopping hours may pose risks for some small retailers. For example, the Victorian Retail Confectionery and Mixed Business Association advised the Council that the failure rate among its members' businesses jumped in the six months immediately following deregulation in Victoria. Notwithstanding this, Australian Bureau of Statistics data do not indicate a decline in total retail employment in Victoria since deregulation.

The Victorian *Liquor Control Act 1987* restricts the sale of take-away liquor to hotel bottle shops and licensed liquor stores. Other retail outlets, such as supermarkets, convenience stores and petrol stations, are not permitted to sell liquor. In addition, the Victorian Act distinguishes between types of licence

holders. For example, hours of trading for holders of packaged licences are more restricted than for holders of general licences.

The Victorian Act also limits the total number of general licences or packaged licences held by a person or corporation to no more than eight percent of all such licences. This imposes a restriction on larger businesses. The Western Australian Government recently considered and rejected a similar amendment to its *Liquor Licensing Act 1988*, which would have had the effect of imposing a 15 percent limit on an individual liquor retailer's market share.

As with other aspects of the NCP legislation review program, the obligation on governments considering liquor retailing laws is to remove restrictions where reviews find that this would provide a net community benefit. This does not mean open slather for liquor retailing, particularly given the strong community demand for licensing arrangements which help to minimise the harm caused by inappropriate distribution and consumption of alcohol. It does mean, however, identifying the social policy objectives in this area, determining whether current controls help achieve these objectives, and assessing whether the objectives can be achieved by alternative, less anti-competitive means. In particular, reviews should examine whether restrictions such as limits on the number of licences available to an individual liquor retailer or distinctions between types of outlets in relation to who can sell liquor and when they can do it, help achieve community objectives on alcohol consumption.

Monopoly provision of certain services

Over the past 12 months, governments have begun to examine a range of legislation providing statutory monopoly status to service providers in areas such as public sector superannuation, compulsory third party insurance and legal professional indemnity insurance. In some of these areas, the monopoly provider is a government agency.

There has been a high level of interest in these areas from private sector bodies directly affected by such legislation. The Law Society of NSW, LawCover, Law Institute Victoria, Insurance Council of Australia (ICA) and Jacques Martin Industry Funds Administration Pty Limited have all raised concerns with the Council.

Governments' review and reform action in relation to legislation establishing statutory monopolies in these areas will be matters for consideration by the Council in future assessments of progress in this area of NCP.

Public sector superannuation schemes

Legislation relating to some public sector superannuation schemes either appoints government sector administrators as the sole administrator of the scheme or provides a government authority with the discretion to appoint an administrator. Where legislation appoints a sole government administrator, it restricts competition from private sector administrators. Where legislation establishes a discretion as to the appointment of an administrator, the manner in which the discretion is exercised may have the potential to restrict competition.

Some jurisdictions, such as the Commonwealth, NSW and Queensland, have taken, or propose to take, action to review the monopoly status of government sector scheme administrators. The ACT is currently reviewing how superannuation can be provided to new entrants in accordance with NCP requirements. Victoria has excluded its legislation, the *Public Sector Superannuation (Administration) Act 1993 (Vic)*, from NCP review on the basis that it does not restrict competition in the market for superannuation administration services because the current government sector administrator has the power to engage private sector administrators and the exercise of that power represents a commercial decision for the administrator.

Compulsory third party insurance

All States and Territories are reviewing their legislation governing compulsory third party arrangements.

At present, arrangements vary across jurisdictions. In NSW and Queensland, the provision of compulsory third party insurance is open to competition, although in Queensland the government, on recommendation, sets premiums. Recommendations are made by a government agency, the Motor Accident Insurance Commission, following consideration of actuarial advice and submissions from insurers.

However, in Victoria, Tasmania, Western Australia, South Australia and the Northern Territory, compulsory third party insurance services are provided by government-owned statutory monopolies. In the ACT, the sole provider of compulsory third party insurance is a private insurer, the National Roads and Motorists Association (NRMA).

Legal professional indemnity insurance

Legal professional indemnity insurance in each jurisdiction is compulsory for solicitors. The compulsory nature of the insurance is said to reflect a policy objective of protecting consumers and promoting the community's confidence in the legal profession.

Legal professional indemnity insurance in each jurisdiction is delivered via arrangements approved under legislation. The legislation gives the Law Society or Attorney General in each jurisdiction the power to approve the legal professional indemnity insurer. This has resulted in only one insurer approved to provide legal professional indemnity insurance in each jurisdiction (except the ACT), namely, the insurer associated with the particular Law Society.

In the ACT, amendments to the *Legal Practitioners Act 1970* that came into effect this year have led to the approval of a second provider, LawCover, in competition with the existing statutory provider. Victoria introduced legislation in 1996 that provides for competition in the provision of professional indemnity insurance services. The relevant sections of the legislation are due to come into effect on 1 January 1999.

Competition questions for governments

The task for governments under the NCP program is to determine whether the monopoly arrangements in the above cases are justified in terms of a benefit to the community as a whole. This involves considering the objectives of the legislation and alternatives to the current monopoly arrangements. For example, for compulsory third party insurance, more competitive markets operate in both NSW and Queensland.

A range of justifications have been raised in support of retaining the existing monopoly arrangements in the context of compulsory third party insurance and legal professional indemnity insurance including:

- the cost of monopoly provision is cheaper than it would be in a competitive market;
- monopoly provision provides greater financial security;
- the existing monopoly provider offers more comprehensive cover and better protection to consumers than the cover that would be available in a competitive market;
- the existing monopoly provider is better at managing risks and claims handling due to a comprehensive centralised database;
- in a competitive market, commercial insurers would determine who could practice as a lawyer by refusing to cover lawyers with a high claims record; and
- the monopoly provider is in a better position to conduct programs aimed at preventing claims, for example campaigns aimed at encouraging better practice management for lawyers and encouraging safer driving activities.

Against this, many private sector companies have provided evidence of a benefit from more competitive arrangements.

The ICA has questioned the analytical approach of some reviews currently underway as focusing on the costs and benefits of having compulsory third party insurance rather than assessing the net community benefit associated with retaining the monopoly delivery of such insurance. The ICA was also critical of some review processes. For example, in the case of Western Australia, the ICA noted that third party insurance legislation was reviewed by the Insurance Commission of Western Australia, the body being reviewed, rather than by an entity with nothing to gain or lose from competitive entry by other businesses. The ICA also stated that failure by Western Australia to make material available to the public had reduced the scope for consideration of key issues.

The Law Society of NSW advocated a more competitive approach to the provision of professional indemnity insurance. It suggested that governments

could achieve the objective of requiring all solicitors to be insured under a multi-provider arrangement by imposing minimum standards for providers of legal professional indemnity insurance.

Gambling/casino legislation

Over the last 25 years, the Australian gambling industry has enjoyed increasing growth. One of the major drivers of this growth is the expansion of gambling opportunities provided by casinos and electronic gaming machines. There are now casinos in every State and Territory, and some 14 casinos in operation Australia-wide. Most currently operate with an exclusive (monopoly) licence, which gives exclusive market access by preventing competing casinos from setting up within a certain geographic range.[8]

Traditionally, gambling has been far more regulated than most other industries, and free competition has not been an objective of governments' policies. The approach of governments has reflected their views that there is significant community concern about the potential economic and social costs associated with a more competitive gambling market. Rather than fostering competition, governments focus on protecting consumers from dishonest operators, minimising social costs such as under-age gambling, problem gambling and social disruption, and preventing criminal activity. The promotion of economic development and tourism through gambling, and securing taxation revenue, are also objectives for governments.

Most States and Territories have scheduled legislation regulating gambling activities, including casinos, in the early part of their review programs. The more complex competition policy questions confronting governments in reviewing gambling legislation relate to the exclusive licence available to casinos and to regulation of the number and distribution of electronic gaming machines. Under NCP, the major task for governments is to determine whether these restrictions provide the best way of achieving outcomes which maximise the net community benefit. That is, the NCP review is not intended

8 For some casinos, the exclusive geographic licence protection has now expired.

to examine the justification behind community standards but rather how best to impose those standards where a restriction on competition is involved.

There has been considerable review activity over the past year. Victoria commissioned consultants to produce a framework for reviewing gambling legislation and completed a preliminary scoping study of its *Casino Control Act 1991*, *Casino (Management Agreement) Act 1993* and associated regulations. Responding to the Council's first tranche assessment that restrictions on competition contained in casino legislation should be examined, Queensland reviewed its four casino agreement acts and South Australia undertook a clause 5(5) assessment of its new *Casino Act 1997*. Western Australia, Tasmania, the ACT and the Northern Territory all scheduled reviews of casino control arrangements in their June 1996 legislation review programs. On a related matter, NSW examined the justification for providing a monopoly licence arrangement for the NSW TAB.

At a broader level, the Commonwealth has established a comprehensive national review of the social and economic impact of gambling, to be undertaken by the Productivity Commission. The ACT Government recently completed its own study of the social and economic impacts of gambling in the ACT.

Outcomes of reviews

All review work to date has supported the exclusive licence arrangement for casinos. While not convinced about several of the justifications, the Council acknowledges that the reviews raised some valid considerations. At a minimum, the reviews emphasised the complexity of the questions facing governments in determining the net community benefit from the monopoly licence restriction.

All reviews pointed to the responsibility on governments to address community concern about the social impacts of gambling and the perceived attraction of casinos for organised crime. Governments considered that allowing for multiple casinos would not reflect the strong support of their constituencies for limits on the level of gambling.

The reviews also pointed to the importance of the contribution made by gambling to State and Territory revenue. Keeping in mind community views about the desirability of limits on the amount of gambling, the reviews found that financial returns to the community (licence fees and taxation) are maximised through a single licence arrangement. In effect, this is a function of the advantage available to the casino operator from the monopoly arrangement. The reviews also found there would be a cost to the community in 'buying out' exclusive licence contracts.

The reviews also argued that the cost to the community of maintaining probity is minimised with a single licence because the cost of regulating one large venue is less than the cost of regulating many small venues.

The reviews also identified some costs from imposing monopoly licensing. These include a reduced incentive for the casino operator to improve the games available to casino patrons or to offer additional services such as free drinks for players to enhance the overall product. More generally, the period during which casino operators are protected from competition could create customer loyalties to the incumbent operator which may work against potential entrants to the casino (and substitute products) market.

Overall, the preliminary studies led governments to a view that it is probable that the current arrangements provide a net community benefit. Moreover, because most monopoly licences include provision for compensation for early termination, the approach favoured by governments is to consider the need for less restrictive arrangements as exclusivity arrangements expire.

The Council's view

Noting the complexity of issues associated with gambling regulation (and particularly casinos) revealed by the work undertaken by jurisdictions, the Council considered it sensible to examine the restrictions on competition contained in gambling legislation outside the first tranche assessment process. The Council considers that the Productivity Commission review of gambling policy/arrangements presents a suitable mechanism.

Tariff protection: the textiles, clothing and footwear industries

The Commonwealth Government's review of the *Customs Tariff Act 1995 - Textiles Clothing and Footwear Arrangements* was subsumed into the Industry Commission inquiry into the textiles, clothing and footwear (TCF) industries. The independent inquiry took place over a nine month period, addressing a terms of reference that required it to recommend on assistance arrangements for the TCF industries post 2000, consistent with the aim of improving the overall economic performance of the Australian economy and having regard to NCP legislation review commitments. The inquiry received 272 submissions and consulted widely with the TCF industries and others through meetings and public hearings.

The inquiry committee reported in September 1997 (IC 1997b). It recommended a package of policy changes for TCF, which it considered would create incentives to develop sustainable, prosperous and internationally competitive TCF industries in Australia, with benefits for Australian consumers and taxpayers. On the matter of tariffs, the review committee provided a majority recommendation for phased reductions to 5 percent by 1 July 2008, without pause from 1 July 2001, and an alternative view supporting a pause in the tariff reduction program between 2000 and 2005. The review unanimously supported a program of adjustment assistance to accompany the tariff reductions, including for workers and for regions if there is a significant displacement of workers in non-metropolitan regions, and funding for technology development.

The Commonwealth's response to the review, announced in September 1997, provided for:

- maintenance of the current phased reductions in TCF tariffs until 2000;
- maintenance of tariffs at year 2000 level until 2005 at which time they will reduce from 25 percent to 17.5 percent for clothing and finished textiles and from 15 percent to 10 percent for footwear; and
- a review in 2005 to take account of trade commitments and progress on market access.

The Commonwealth stated that its September 1997 TCF package is designed to assist in securing jobs in the TCF industries by encouraging additional investment and promoting the development of an internationally competitive TCF sector in the lead up to the free trade environment beyond 2000 (Commonwealth of Australia 1998). In July 1998, the Commonwealth announced structural adjustment and investment assistance for the TCF industries.

The Commonwealth's decision did not reflect the majority recommendation, which concluded that continuing the program of TCF tariff reductions would improve Australia's overall economic performance and increase the welfare of all Australians. Neither did the Commonwealth provide a sufficiently robust community benefit case to support its decision to disregard the majority review recommendations. While the tariff freeze may attract investment to and support employment in the TCF industry, the evidence from the review is that there would be a greater benefit to Australia as a whole from faster and deeper tariff reductions. This indicates that the Commonwealth's decision to introduce a freeze in the TCF tariff reduction program over the period 2000-2005 represents a failure against the CPA objective of maximising the net benefit to the whole community.

Digital terrestrial television broadcasting

Digital terrestrial television transmission allows the broadcast of widescreen, cinema quality programs with surround sound (High Definition Television) into the home. It provides for clearer pictures than the current analog transmission, especially in hilly or built up areas. It also allows more efficient use of spectrum than analog transmission, enabling multiple standard television services within the same spectrum and/or multiple information streams (datacasting) to be received by digital television reception equipment.

On 8 April 1998, the Commonwealth introduced the *Television Broadcasting Services (Digital Conversion) Bill* and the *Datacasting Charge (Imposition) Bill* into the House of Representatives. The Bills establish the framework for the conversion of free-to-air television broadcasters to digital broadcasting, which is scheduled to commence in 2001 in metropolitan areas, and the basis for charging non-broadcasters for access to the spectrum.

The *Television Broadcasting Services (Digital Conversion) Bill* provides for a simulcast period of at least eight years (to 2008), with a review in 2005 to consider extension. During the simulcast period, no new commercial television licences will be allowed, providing the existing broadcasters with exclusive access to the Australian television market.

In addition, the Commonwealth is to provide all incumbent broadcasters with the additional 7 Megahertz (MHz) of spectrum required for High Definition Television free of charge. At the end of the simulcast period each of the broadcasters (who would have used two 7 MHz of spectrum to transmit in analog and digital) would be required to return 7 MHz of spectrum to the Government. Spectrum not required by the free to air broadcasters is to be made available for datacasting services (internet style data transmission) on a competitive basis. This means that the non-broadcasters will have to compete amongst themselves in an auction for available spectrum.

The Commonwealth's Bills raise two significant competition policy questions. First, the *Television Broadcasting Services (Digital Conversion) Bill* protects incumbent operators from competition from new commercial free-to-air entrants for a substantial period, giving these operators privileged access to Australian consumers and a headstart to introducing the new television technology. Second, if technological developments enable High Definition Television to be broadcast using less than the full 7 MHz, the existing broadcasters will be able to use part of their spectrum allocation for datacasting in competition with non-broadcasters which are required to buy spectrum.

The Commonwealth considers that restrictions on competition at this stage in the transition to digital television broadcasting and transmission are required to achieve its policy objectives. It considers its approach is necessary to ensure a smooth, timely transition to digital terrestrial television broadcasting built on the experience, expertise and infrastructure of existing television broadcasters, and that it is necessary to take account of the increased costs of investment and providing dual digital/analog services. The Commonwealth argues that it has satisfactorily addressed potential concerns about the 'neutrality' of competition between the broadcasters and the non-broadcasters by providing for an appropriate charge for datacasting use, prohibiting multi-channelling services and specifying high definition

television requirements.[9] The Senate Environment, Recreation, Communications and the Arts Legislation Committee, which inquired into the Bills, also concluded that these restrictions are appropriate (Parliament of the Commonwealth of Australia, Senate 1998).

As with all new or amending legislation which restricts competition, the Commonwealth addressed its CPA clause 5(5) responsibilities through a RIS (Parliament of the Commonwealth of Australia, House of Representatives 1998a). The RIS examined three options for introducing digital terrestrial television broadcasting in Australia, including:

- no limit on new free-to-air television broadcasting entrants and no limit on competition in broadcasting and related services;
- no limit on new free-to-air television broadcasting entrants but provision of digital spectrum to existing commercial and national broadcasters to replicate their analog services, and no restrictions on competition in broadcasting and related services in residual spectrum; and
- restrictions on competition (as proposed by the Commonwealth) with the objective of enhancing the standard of existing free-to-air television broadcasting services and providing access to new services while minimising consumer disruption.

The Council will examine this matter in the context of its next assessment of Commonwealth NCP progress in 1999. In line with CPA clause 5(5), central considerations for the Council will be whether the options for achieving the objectives of the legislation have been rigorously examined and whether the available evidence demonstrates that the restrictions provide a net community benefit. In this regard, the Council is mindful that the ORR – which has a central role in ensuring the integrity of processes aimed at ensuring more effective, less intrusive regulations – has endorsed the analysis contained in the RIS.

9 Multi-channelling describes the ability of broadcasters to transmit multiple programs within the one channel.

B3.6 Looking forward

The legislation review program will stretch to the end of the year 2000 and sometimes, where governments substantiate a community benefit case for phasing of reform, beyond. Completion of the program and implementation of pro-competitive reforms represents a considerable task for governments.

The Council's experience of the first two years of the program emphasises the importance of open and rigorous review processes aimed at genuine reform. In this respect, it is important to ensure that review panel members are clearly impartial and that appropriate public consultation processes are adopted. Processes which become captured by vested interests or which stymie objective consideration of relevant evidence will not facilitate achievement of the benefits envisaged by COAG when it introduced NCP.

Strong leadership from governments in rejecting unjustified special pleading from interests hitherto protected from competition is vital in achieving the benefits available from properly harnessed competition. In this respect, the Council will continue to place considerable weight in its assessments on maintaining the integrity of the community wide approach of the CPA. This means demonstrating that any continuing restrictions on competition provide a net benefit to the whole community, not just a special section of it. It also means timely implementation of pro-competitive reforms recommended by review bodies.

The Council is required to conduct its next formal assessment of NCP progress prior to July 1999. Apart from the need for jurisdictions to maintain momentum with review programs consistent with the year 2000 target, the Council will look for outcomes consistent with the competition tests in emerging priority areas. These include areas such as agricultural marketing arrangements, professional and occupational regulation, government monopoly arrangements and shop trading hours.

B4 COMPETITIVE NEUTRALITY

B4.1 Background

Government business activities use a significant proportion of the country's resources to provide a wide array of goods and services to both businesses and consumers. Consequently, how well government businesses operate has a significant effect on both the Australian economy and on the community.

Improving the performance of government businesses has been an ongoing focus for all Australian governments since the late 1980s. Many studies and reviews provided widespread evidence of poor performance, including poor capital and labour productivity, overstaffing and excessive use of material inputs, inappropriate management practices, poor quality goods and services, inappropriate pricing practices and poor financial performance.

In the face of this evidence, and because of the importance of government businesses to Australia, all governments have been considering a range of measures to help them improve the ways in which they provide services. Initiatives to achieve this have included structural changes ranging from corporatisation through to introducing prices that reflect a full attribution of costs. These reforms, coupled with moves to introduce greater competition, have been designed to increase the commercial orientation of government businesses so that they provide the services consumers need as efficiently and effectively as possible.

Under NCP, governments have undertaken to extend these measures to all their significant business activities. They agreed to apply competitive neutrality principles, essentially removing any net competitive advantage arising from government ownership, where government businesses face actual or potential competition from the private sector. This allows the two sectors to compete on an equal footing and encourages efficient operation of public enterprises. The underlying aim is to ensure that the community's resources are used as efficiently as possible.

B4.2 Governments' commitments

Under the NCP Competition Principles Agreement (CPA), governments committed to do three things.

First, they agreed to introduce competitive neutrality principles to their significant business activities including those of local government. What this means is discussed further in Section B4.3 below.

Second, jurisdictions agreed to provide a mechanism whereby individual businesses can lodge complaints that competitive neutrality is not being implemented appropriately in relation to certain government business activities.

Third, each jurisdiction agreed to provide:

- a competitive neutrality policy statement by 30 June 1996;
- a local government policy statement which, among other things, specifies how competitive neutrality principles will be applied to significant local government business activities; and
- annual reports which outline progress with implementing competitive neutrality principles and allegations of non-compliance.

Satisfactory progress against competitive neutrality obligations is one of the conditions for receipt of NCP payments.

B4.3 Agreed reforms to government business activities

Identifying relevant business activities

The CPA says that the competitive neutrality principles should apply to the 'significant business activities' of government entities.

There are two types of significant business activities identified by the CPA:

- *government business enterprises* (GBEs) which include Public Trading Enterprises and Public Financial Enterprises and are defined as government undertakings which aim at recovering most of their expenses by deriving revenue from sales of goods and services (ABS 1994, 21); and
- *other significant business activitie*s which include activities that are commonly undertaken by government agencies as part of a wider range of functions. Examples of such activities are refuse collection, printing, construction, parking and maintenance operations.

For competitive neutrality purposes, the CPA distinguishes between the business activities of government and the non-business, non-profit elements of government entities. Competitive neutrality principles are to be applied to business activities only.

Some sectors of government contain elements which operate as businesses as well as undertaking wider policy functions. For example, some public hospitals undertake business activities such as cleaning, catering, pharmacy or pathology services. Often such businesses compete with private providers of the same or similar services. Introducing competitive neutrality for hospital businesses can encourage competition in these areas. It also ensures that the hospital is aware of the true cost of its in-house business activities which will assist in resource allocation decisions. Further, when combined with other reform initiatives such as competitive tendering, competitive neutrality may also lead to the hospital paying less for these services, which will allow them to spend more in other areas such as increasing the number of beds available.

A case by case assessment of the appropriateness of introducing competitive neutrality principles would ensure that as few as possible actual or potential competitors are placed at a disadvantage and the community receives the benefits arising from competition.

Applying competitive neutrality principles

The CPA sets out two broad approaches for introducing competitive neutrality to significant government business.

First, it recommends that GBEs be corporatised where appropriate. The model suggested by COAG involves the introduction of clear business objectives, management independence and accountability, independent performance monitoring, and an effective system of rewards and sanctions. As part of this, GBEs need to introduce:

- full Commonwealth, State and Territory taxes or tax equivalent systems;
- debt guarantee fees directed towards offsetting the competitive advantages provided by government guarantees; and
- those regulations to which private sector businesses are normally subject, such as those relating to the protection of the environment, and planning and approval processes, on an equivalent basis to private sector competitors.

Second, in situations where corporatisation is not appropriate, the CPA states that competitive neutrality should be achieved through introducing the above three reforms and action to ensure that prices fully reflect production costs.

The application of either of these two models is appropriate when the gains to the community are expected to be greater than the costs. While the benefits from enhanced competition would be expected to justify introducing competitive neutrality reform in many cases, there will be situations where the sum of financial, social, environmental and other costs outweigh the gains expected to result from reform. For example, for smaller government businesses or businesses in remote areas where competition is unlikely, the gains to the community may not be as great relative to the costs associated with making the necessary changes to legislation and management systems.

Full cost pricing

The underlying objective of competitive neutrality is to achieve an efficient allocation of resources; that is, resources are used where they are most valued by the community. Prices are the primary means the economy has of allocating resources. Consequently, introducing appropriate prices, is a key element of both of the above models. In the past, some government business activities have offered prices significantly below their cost of production, because, for example, they have not had to pay taxes or face the full cost of borrowing money. This has resulted in government providers being able to offer lower prices than their potentially more efficient private competitors.

Appropriate rate of return

Another important element of both of the above models is an appropriate rate of return on assets. Governments have invested very large sums of money in acquiring the assets (such as buildings, and machinery) necessary to undertake business activities. Because this money has competing uses, it is important that the financial return to the government on assets is at least as good as that of the next best alternative.

Introducing rate of return targets to business activities ensures that government businesses earn a sufficient return on capital. Generally speaking, the requirement to earn an acceptable rate of return is imposed on private sector businesses through capital markets. In the public sector, rate of return targets are used to encourage more efficient use of existing government assets and careful consideration of new investment proposals.

Privatisation

In considering how best to provide services to the community, governments have also adopted a number of approaches outside the scope of the NCP. One such approach is privatisation. In recent years, most governments have privatised certain of their business activities. For example, Victoria has sold much of its electricity sector and the Commonwealth has, to date, sold one-third of Telstra.

While not required by the NCP, privatisation is a means of achieving a competitively neutral outcome. Clearly, when a business is no longer in public ownership, any net advantage associated with public ownership will disappear. Before governments privatise monopoly activities, the CPA obliges them to review the structure and commercial objectives of the public monopoly to ensure that the gains to the community from privatisation are maximised (see Chapter B5).

Competitive tendering

As with privatisation, the NCP does not require the contracting out of particular government services. However, governments may choose to implement competitive tendering and contracting practices where they believe this will improve the quality and cost of publicly provided services.

Where governments do decide to tender for the provision of a service and they accept bids from a publicly owned business unit, it is important that the business unit cost its bid on a competitively neutral basis. Failure to do this will give the business unit an unfair advantage over its competitors and reduce the potential for competition.

Competitive neutrality complaints

Under the CPA, jurisdictions also agreed to establish a mechanism to receive and investigate complaints regarding the competitive neutrality of government businesses and report annually on allegations of non-compliance. The CPA does not specify the organisational structure or processes to be adopted by complaints mechanisms. The Council has encouraged jurisdictions to adopt processes which are independent of the government body responsible for competitive neutrality policy, and which are able to investigate all complaints including concerns that competitive neutrality principles are not being applied. For a discussion of the approaches adopted by jurisdictions, see section B4.4 below. The Council also considers that it is important that parties to a complaint receive a full explanation regarding decisions taken by governments in response to the recommendation of complaints mechanisms.

B4.4 Progress to date

Each jurisdiction prepared a competitive neutrality policy statement by June 1996. In all cases, policy statements identify a process for identifying significant businesses or actually list specific businesses to be considered for reform, outline the jurisdiction's approach to implementing competitive neutrality principles and provide a reform timetable. States and Territories and the Commonwealth have also provided annual updates on progress against their reform timetables.

Reform agendas

While all jurisdictions have prepared policy statements that reflect the broad principles outlined in the clause 3 of the CPA, their approaches to the practical introduction of these principles vary in terms of the size of businesses covered and timeframes adopted for applying competitive neutrality (see Box B4.1).

A range of approaches is used to identify significant business activities. The Commonwealth, NSW, Victoria, Queensland, Western Australia and South Australia all use size thresholds as a guide to market significance.

The Commonwealth is applying competitive neutrality principles to all GBEs, Business Units, share limited companies and competitive tendering and contracting activities regardless of their size. Other Commonwealth entities which have business activities with annual turnover in excess of the threshold level of $10 million will also have competitive neutrality principles applied. Furthermore, the Commonwealth will include smaller businesses on its reform program on the recommendation of the Commonwealth Competitive Neutrality Complaints Office.

Similarly, South Australia is initially targeting all businesses with an annual turnover in excess of $2 million or assets in excess of $20 million, before considering smaller business activities. Application of competitive neutrality to business activities not initially included on the State's list of significant businesses will be considered by the State's Competition Commissioner.

Queensland's significant business activities include three significant local government business activities that do not meet the size threshold set by the State. These activities are building certification services provided by the Maroochy Shire Council and the Logan City Council, and Ipswich City Council's Internet service business 'Global Info-links'. All three businesses will be commercialised from 1 July 1998.

Of the remaining jurisdictions, to date Tasmania has introduced tax equivalent, debt guarantee and dividend regimes to all GBEs except one, regardless of size. The ACT will review all government business operations to ensure that their structure, operational requirements and financial incentives promote efficient practices. The Northern Territory will apply competitive neutrality principles to all activities identified under the Financial Management Act as Government Business Divisions.

In its last annual report, the Council noted that size thresholds are useful in prioritising reform but should not be used to exempt business activities that have a significant impact on the market in which they operate. Where jurisdictions use size thresholds to establish priorities, the Council is encouraging them to extend, over time, the range of business activities considered for competitive neutrality reform. Queensland is moving in this direction, and the approaches adopted by the Commonwealth and South Australia should eventually see wider application of competitive neutrality principles.

State and Territory progress

The Council's 1996-97 Annual Report noted sound early progress in some areas, including electricity, port authorities and other large trading enterprises. More generally, however, early progress had been slowed by the need to undertake preliminary work, such as guidelines to facilitate a consistent and comprehensive basis for reform. The Council welcomed the opportunity to provide an input to the development of some of these guidelines.

Over the past 12 months, States and Territories have continued to advance their reform programs. For example, following an independent net benefit assessment, Queensland has announced that Sunlover Holidays (a business

Box B4.1 Coverage and timing of Commonwealth, State and Territory reform agendas

- The Commonwealth will consider for competitive neutrality reform all bodies established principally as business entities (including GBEs, Business Units, share limited companies and competitive tendering and contracting activities) regardless of their size, profitability or class of business. Other government bodies which have commercial activities with turnover in excess of $10 million will also be considered. Smaller entities may also be considered upon the recommendation of the Commonwealth Competitive Neutrality Complaints Office. All competitive neutrality implementation arrangements will be in place by 1 July 1998.
- NSW has a Financial Policy Framework (FPF) which involves: application of commercially based target rates of return, dividends and capital structures; regular performance monitoring; payment of State taxes and Commonwealth tax equivalents; payment of a risk related borrowing fee; and explicitly funded 'Social Programs'. All significant GBEs that are monitored on a quarterly or half yearly basis are subject to the FPF. Local government entities with annual gross operating incomes above $2 million will be corporatised.
- Victoria has developed corporatisation and full cost pricing models for application where appropriate to 32 GBEs and 32 other significant businesses. As a guide, the Government has recommended that business activities with a revenue base of less than $10 million or fewer than 15 employees should not be corporatised and careful consideration should be given to corporatising business activities with revenues between $10 and $20 million. Most 'other significant business activities' have applied appropriate competitive neutrality principles from 1 July 1997.
- Queensland has prepared a list of significant business activities and a timetable for their review. The Government has initially focused on applying competitive neutrality to business activities with annual current expenditure greater than

Box B4.1 …cont

$10 million but is considering smaller activities over time. Similarly, the State is initially focusing on applying competitive neutrality principles to businesses operated by its 17 largest councils. Size thresholds have also been used to identify three types of significant local government business activities.

- Western Australia has listed 38 significant business activities and has published a timetable for their review. High priority activities are being reviewed first but all reviews are scheduled to be completed by 2000. The State's policy statement noted that businesses with turnover or assets less than $10 million are unlikely to be significant. Local government businesses must have annual turnover of at least $200 000 to be considered for reform.
- South Australia has committed to apply competitive neutrality, where appropriate, to all business activities with revenue greater than $2 million or assets greater than $20 million by June 1998. South Australia also plans to announce decisions on remaining significant businesses by June 1998. All significant South Australian business activities will be subject to the same regulations as the private sector by June 2000.
- As of 1 July 1997, all Tasmanian GBEs, bar one, became subject to the full tax equivalent regime, dividend regime and guarantee fee. Tasmania has also identified a specific list of non-GBEs to be considered for reform.
- The ACT intends to review all businesses that produce goods and services that can be sold in the market place. Three business activities have been corporatised and 41 general government activities have been listed for review.
- Competitive neutrality principles have been applied to all 12 of the Northern Territory's government business divisions. The Northern Territory stated that the three largest (the Territory Insurance Office, the Power and Water Authority, and the Darwin Port Authority) are all fully corporatised. A comprehensive review of all aspects of the Power and Water Authority is being undertaken in 1998-99. Commercialisation principles have applied to the other business divisions from 1 July 1997.

Source: Jurisdictions' July 1996 policy statements and annual progress reports.

division of the Queensland Tourist and Travel Corporation) will be commercialised by 1 July 1998.

Queensland has also completed public benefit tests for its four urban water boards, and an 'in-principle' government decision on commercialisation is expected in 1998. Independent public benefit assessments have also been commenced for the Public Trust Office and the Brisbane Market Authority. These assessments will be completed by June 1998. In most cases, public benefit tests have included public consultation.

Recent ACT competitive neutrality initiatives include the incorporation of CanDeliver, an ACT government business which offers corporate services such as financial and human resource management and information technology services. CanDeliver was incorporated in September 1997 in response to service provision opportunities created by the Commonwealth decision to outsource corporate services functions. CanDeliver operates on a full cost recovery basis. Also in the ACT, eight businesses units and 600 staff have been transferred from the Department of Urban Services to Totalcare, a Territory Owned Corporation. Full cost pricing is to be introduced to these businesses units by June 1998.

With the exception Port Arthur Historic Site Management Authority (PAHSMA), all Tasmanian GBEs became subject to the full tax equivalent regime, dividend regime and guarantee fees as of 1 July 1997. The PAHSMA will have its structure and funding reviewed as part of the State Government's 1998-99 budget deliberations. Tasmania has also established a list of non-GBE significant businesses activities to be considered for reform since its last report to the Council.

In South Australia, the State's tax equivalent regime policy now extends to 21 trading and financial enterprises and their subsidiaries as well as 16 government department business units. Debt guarantee fees now apply to over 36 business activities.

Victoria has indicated that progress with applying competitive neutrality principles to Victorian significant businesses since January 1997 has included establishing a number of transport corporations including Vic Track, V/line Freight, V/line. The Council has also been advised that 11 natural gas corporations have also been established.

In NSW, the Superannuation Administration Authority has been added to the State's list of significant business activities, with options for its reform currently being considered.

Commonwealth progress

The Commonwealth released its first report on progress with competitive neutrality early in 1998. The report covers the period to July 1997. A summary of early progress is contained in Box B4.2

The Council considered competitive neutrality issues relating to Australia Post as part of its review of the *Australian Postal Corporation Act 1989* (see Chapter B13). Submissions to the review claimed that Australia Post had significant advantages over its competitors because the Act does not permit competition in some of Australia Post's business activities. These activities are known as reserved services.

The Council recommended introducing strict and transparent accounting separation and some limited access regulation to reduce the ability of Australia Post to use profits from its reserved services to subsidise its activities in competitive markets. Apart from this, the Council saw no case for further constraints on Australia Post's ability to adopt normal commercial practices.

The Council also recommended a number of changes to the *Australian Postal Corporation Act* 1989 to remove or reduce regulatory advantages currently experienced by Australia Post so that Australia Post and other providers can compete on even terms.

Local government progress

In making its first assessment of State and Territory progress in June 1997, the Council recognised that all relevant jurisdictions[1] had made some progress towards implementing the required competitive neutrality reforms

1 'Relevant jurisdictions' in this context refers to NSW, Victoria, Queensland, Western Australia, South Australia and Tasmania. The ACT does not have a local government sector and the business activities of local government in the Northern Territory are not significant for the purposes of the CPA.

Box B4.2 Progress with introducing competitive neutrality to Commonwealth businesses

- The Commonwealth has identified 47 significant business activities (17 GBEs and 30 non-GBE businesses).
- By 1 July 1997, all 17 GBEs were effectively subject to the same taxes as their competitors and started earning a commercial rate of return.
- Legislation and articles of association establishing new GBEs will be consistent with competitive neutrality principles.
- Almost two-thirds of the Commonwealth's significant businesses have been, or will be, involved in some form of divestment.
- Medibank Private has been separated from the Health Insurance Commission to alleviate possible competitive neutrality concerns.
- No major competitive neutrality issues were identified for Artbank, the Special Broadcasting Commission or the Army and Air Force Catering Service.
- Of the remaining 15 significant business activities, corporatisation will be considered for three, competitive neutrality costing will be applied to five, and seven are under review.

Source: Commonwealth July 1996 policy statement and annual progress reports.

in co-operation with local governments. Jurisdictions had published local government policy statements which included their proposals for applying competitive neutrality principles, and had undertaken preparatory work such as developing implementation guidelines.

However, the Council's view at the time was that all jurisdictions needed to demonstrate greater substantive progress in order to be assessed as having met their first tranche commitments. In particular, the Council sought evidence from jurisdictions that local governments had identified their

significant business activities and determined how competitive neutrality would be applied to those activities. Accordingly, the Council undertook to reassess jurisdictions' progress prior to July 1998. Since that time, most jurisdictions have made good progress towards 'on the ground' reforms (see Box B4.3).

Competitive neutrality reform at the local government level is a complex and involved task. The number of local governments, their geographical dispersion and their diversity in terms of size, organisational structure and service responsibilities have made a consistent approach to reform difficult. Some local governments, particularly the smaller ones, may need to develop new skills or introduce new processes (such as accrual accounting) to facilitate effective competitive neutrality reform.

In addition, there are often significant public interest considerations associated with local governments, particularly in remote locations. In these areas, regional development and employment factors may mean that the social and economic cost of introducing competitive neutrality may outweigh benefits arising from increased competition between public and private providers.

Uncertainty within local government, particularly in Queensland, about the process by which local government corporations are exposed to Commonwealth taxes has been a significant constraint on local government competitive neutrality reform (see Section B4.5).

In some jurisdictions, local governments have also integrated competitive neutrality into broader reform programs. For example, Victoria has introduced compulsory competitive tendering, requiring local governments to tender 50 percent of their total expenses. In Tasmania and South Australia, the need to first complete council amalgamation programs have delayed the commencement of competitive neutrality but potentially will see more rapid reform later in the process.

Queensland, the State with the largest local government sector, has agreed to pass on $150 million over five years to local governments participating in NCP reform provided the State receives its full share of NCP payments. This approach provides an incentive for reform and assists with associated costs, such as conducting public interest tests and reviews of businesses.

Box B4.3 Progress with introducing competitive neutrality to local government

- By early March 1998, NSW councils had identified 90 Category One business activities (those with at least $2 million annual turnover) and 318 smaller Category Two business activities. Of the 90 Category One activities identified, 71 had established separate internal reporting and some, to varying degrees, had introduced full cost attribution and identified subsidies. Full cost attribution has been applied to 39 Category Two businesses, a further 68 have introduced partial cost attribution and 151 have made any subsidies explicit.
- In Victoria, 10 local government business activities have been approved for corporatisation. Victoria's local government businesses have been applying competitively neutral pricing principles to their significant business activities since July 1997.[a]
- In Queensland, 26 council businesses (with a combined annual expenditure of more than $700 million) are to have competitive neutrality reforms applied from July 1998. In addition, all councils are to decide whether smaller business activities that compete directly with the private sector should apply a voluntary Code of Competitive Conduct. The Code is based on the principle of full cost pricing.
- Western Australia has requested its largest 54 local councils to complete competitive neutrality reviews of their significant business. Of the 83 reviews of business activities completed by local councils at April 1998, competitive neutrality (most commonly full cost pricing) is to be applied in 44 cases. A further 90 smaller local councils have been requested to complete their competitive neutrality reviews by 1 June 1998.
- South Australian councils have identified all their significant businesses and determined which competitive neutrality principles are to apply to 'Category One' business activities (those with over $2 million annual revenue or assets worth over $20 million). Six Category One business activities were

Box 4.3 …cont

identified, one already operates on a fully commercial basis and five are to have full cost pricing applied. South Australian councils also identified 49 smaller 'Category Two' business activities and are considering how to apply competitive neutrality principles to these.

- In Tasmania, the Local Government Board has been reviewing all council boundaries, with a view to reducing the number of councils from 29 to not more than 15. Elections for the new councils have been set for August 25. The State intends to consider the application of full cost pricing to significant businesses from September 1998 in consultation with local government. It will review its corporatisation process with the aim of completing the program by July 1999, 12 months earlier than originally planned.

Source: Jurisdictions' policy statements and annual progress reports.

a Victoria has indicated that more detailed reporting on the application of competitive neutrality principles will be contained in the councils' annual reports for 1997-98, which are due to the Minister by 30 September 1998.

While noting that there is some variability in outcomes to date across jurisdictions due to the factors above, the Council is now satisfied that all jurisdictions have demonstrated progress sufficient to meet their first tranche commitments. Continued progress with the application of competitive neutrality reform will be important in the Council's second and third tranche assessments.

Complaints mechanisms

Mechanisms for handling competitive neutrality complaints now operate in all jurisdictions. The CPA does not require jurisdictions to adopt a particular approach to handling complaints. Consequently, jurisdictions differ in terms of the form of their complaints mechanism, the activities covered and the competitive neutrality issues addressed.

Broadly speaking, two different models have been adopted. Western Australia, Victoria, the ACT and the Northern Territory, have established complaints units within their Treasury or Premier's/Chief Minister's Department. Alternatively, in Queensland, South Australia, Tasmania and the Commonwealth, an independent body handles complaints. At present, NSW adopts the first model, with complaints investigated by the Cabinet Office. However, NSW is proposing that generic complaints be handled by the Independent Pricing and Regulatory Tribunal, while complaints about tendering processes will continue to be handled by the State Contracts Control Board.

In NSW, Victoria, South Australia, Tasmania and the Commonwealth, complaints mechanisms can investigate complaints that a government business:

- has not been exposed to competitive neutrality arrangements;
- is not complying with the competitive neutrality arrangements to which it has been exposed; or
- is complying with the competitive neutrality arrangements to which it has been exposed, but the arrangements are not effective in removing or offsetting the advantages arising from public ownership.

In other States and Territories, the complaints mechanism can investigate the second and third types of complaints. Consequently, all jurisdictions have established a complaints mechanism that will assist in refining existing reform areas. The Council's previous Annual Report noted that extending the coverage of complaints mechanisms beyond businesses already covered by competitive neutrality policy – in effect the approach of the Commonwealth, NSW, Victoria, South Australia and Tasmania – not only provides a check on

existing reform areas but also provides a means of identifying new areas requiring attention.

There is also some variation among jurisdictions in the handling of competitive neutrality complaints about local government businesses. In NSW, Queensland, South Australia, Tasmania and the Northern Territory, complainants are initially referred to the local government concerned. If the issue is not resolved to the satisfaction of the complainant, the complaint can be referred to either an independent referee, the State or Territory complaints mechanism or the State or Territory department responsible for local government, depending on the jurisdiction.

In Victoria, local government complaints are handled through the State complaints mechanism, although complaints about activities subjected to competitive tender are handled through the Office of Local Government. In Western Australia, all local council complaints are handled by the Department of Local Government.

The Council views competitive neutrality complaints and how they are handled as an important indicator of the effectiveness of jurisdictions' competitive neutrality policy and its application. The processes adopted by jurisdictions in responding to complaints will be an important element in future Council assessments of progress with competitive neutrality reform. Another important consideration will be jurisdictions' responses to the recommendations of complaints mechanisms. The Council will be interested in reform outcomes arising from complaints mechanism recommendations. The Council considers that a strong public good justification should be provided where governments decide not to act on complaints mechanisms recommendations.

B4.5 Implementation issues

During 1998, jurisdictions jointly established a Competitive Neutrality Complaints Roundtable. The aim of the Roundtable is to consider emerging competitive neutrality issues, policy matters and identify best practice. The Council supports the establishment of the Roundtable as a means of

addressing inter-jurisdictional competitive neutrality issues and promoting best practice.

The Council's involvement with the Roundtable, its bilateral discussions with jurisdictions and issues raised by members of the community have raised some often complex implementation issues. In particular, introducing full cost attribution, and identifying all relevant significant business activities, are areas that are proving to be challenging.

Introducing full cost pricing

Clause 3(5)(b) of the CPA states that jurisdictions will:

> ensure that the prices charged for goods and services will take account, where appropriate, of the items listed in paragraph 4(b), and reflect full cost attribution for these activities (clause 3(5)(b)).

Prices are the primary means the economy has for allocating resources among competing users. However, in the past, prices charged by government businesses have often not reflected their true cost, enabling government businesses to offer lower prices than potentially more efficient private competitors. In addition, artificially low prices have in some cases encouraged over consumption and investments that do not recover their cost. For example, in the water industry, extensive use of subsidies has lead to over consumption, over investment and environmental degradation. Introducing prices that reflect the cost of producing the good or service promotes more efficient allocation of resources, a key objective of the CPA.

Setting a competitively neutral price requires jurisdictions to address several technical matters. These include asset valuation and consumption, cost of capital and required rates of return, the allocation of joint costs, and the identification and estimation of subsidies and community service obligations, called 'CSOs'. Most jurisdictions have prepared, or are in the process of preparing, guidelines for introducing pricing reforms consistent with nationally agreed principles.

Defining full cost attribution

Where government businesses operate in a competitive market, prices will be set through the market. However, government entities are sometimes monopolists or face only limited competition. In these situations, the market is unlikely to yield efficient prices.

In the absence of effective competition, efficient prices may reflect a number of factors, including the nature of the business activity and its cost structure. In setting efficient prices, government business units should endeavour to recover all direct and indirect costs of production. Where a business unit shares assets with a parent department, a decision must be made on how the cost of these assets should be shared. A conceptually simple approach – the 'fully distributed cost' method – involves setting prices based on all costs directly attributable to the business unit and a pro-rata share of the overheads and capital costs.

However, in some circumstances fully distributed cost may lead to potentially worthwhile business activities not taking place. The reason for this is that fully distributed cost may overestimate the costs to a business activity of using the resources of the parent agency. For example, it may attribute a share of costs to the business unit for activities, say generic advertising, which would have been undertaken at the same level whether or not the business unit existed. This can be significant in relation to competitive neutrality. Where a business unit's revenue is less than its fully distributed costs, the business unit may decide to cease production when in fact it may be consistent with the efficient resource allocation objective of competitive neutrality for it to continue.

In principle, setting price on the basis of the long run marginal cost of producing a good or service may be more appropriate. Long run marginal cost is the cost of providing an additional unit of a good or service when productive capacity can be varied. It comprises operating costs and the capital costs associated with an additional unit. Conceptually, long run marginal cost represents the appropriate base for decisions on investment in new capacity.

Long run marginal cost is difficult to calculate in practice. Indeed, because of this it is likely that many private sector firms do not use long run marginal

cost as the basis for setting prices. One practical measure of long run marginal cost is long run incremental cost, the increase in the total costs of a business unit attributable to producing a particular good or service. Long run incremental cost includes the additional operating costs, additional costs of capital and additional indirect costs, but excludes those indirect costs which are unchanged whether or not the good or service is supplied. For example, if a business unit uses an asset that would have been purchased by the parent entity anyway, a share of its cost would not be included under the incremental cost methodology.

Another practical measure of marginal cost is avoidable cost, whereby price is set to reflect the costs that would be avoided if the activity is not undertaken. In practice, the long run incremental and long run avoidable cost methodologies are likely yield similar results and the terms are often used interchangeably. Incremental cost is commonly used in estimating the cost of third party access to infrastructure while avoidable cost is often used to measure community service obligations and in-house bids for tendered contracts.

For some activities, for example where many inputs are shared and the business activity's use of these shared inputs is significant, the difference between the fully distributed cost and long run incremental/avoidable cost methodologies will not be great. However, in other situations, there may be a substantial difference. For example, where excess capacity exists such as in off-peak times for electricity or urban transport, better resource allocation outcomes may be achieved if prices are set on the basis of long run incremental/avoidable cost. This would encourage an increase in usage, and enable otherwise unused capacity to make some contribution to recovering its cost.

Community service obligations

Ensuring that prices reflect a full cost attribution does not preclude government businesses from charging prices below cost, that is, subsidising the good or service, where there is a strong public interest justification. This can be done through what is known as a CSO.

CSOs arise when a government requires a business to carry out activities that it would not normally elect to provide, or would only provide commercially at higher prices, and the Government does not require other organisations in the public or private sectors to fund the activity. Examples of CSOs include where governments direct their businesses to charge prices below costs or use local inputs which are more expensive.

A CSO should be used to achieve a specific community outcome for a well defined target group. CSOs should not be used to provide generic operating subsidies to government businesses.

CSOs should also be funded directly from the jurisdiction's budget. Alternatively, governments may choose to 'purchase' CSOs by accepting a lower rate of return from the business which reflects the cost of providing the CSO. Where this is done, the CSO should still be costed as if it were directly funded and the adjustment to the businesses rate of return should be transparently recorded.

Separate funding of CSOs by the government removes potential conflicts between community service and profit maximisation roles of the business activity and increases transparency. Having clearly defined and separately funded each CSO, governments can then consider introducing competition to the provision of CSOs. This can result in the government's community objective being achieved at a lower cost. The corporatisation model recommended in the CPA encourages governments to make their CSOs contestable.

Rate of return targets

An important element of full cost attribution is an appropriate rate of return. Prices should be set at a level so as to provide for an acceptable return on the assets used to undertake the activity.

All jurisdictions have developed, or are in the process of developing, specific target rates for individual significant business activities, although the methods used to set target rates vary. For example, a weighted average cost of capital is used for South Australian significant businesses and non-GTE businesses in NSW. In Victoria, non-corporatised businesses must earn a

minimum rate of eight percent plus a risk premium where appropriate. Tasmania has a target rate of 10.4 percent for all GBEs.

Developing specific targets for individual government businesses leads to prices that more accurately reflect their cost of production. However, for smaller businesses, there may be instances where the costs of an entity-specific approach outweigh the gains. In these situations, a flat rate applied across all such activities may be a more viable approach.

Some jurisdictions (for example, the Commonwealth) consider that once debt guarantee fees, taxes or their equivalents and regulation akin to the private sector are introduced, competitive neutrality is achieved if the business as a whole meets its overall target rate of return. This approach does therefore not require each of the separate activities of the business to achieve the target.

Similarly, the Victorian Government pricing guidelines state that as long as the government business recovers its overall costs then some internal cross-subsidisation between outputs is acceptable. This type of approach will provide the government business with the freedom to make the same pricing decisions as private sector businesses. Such an approach may enable a business with monopoly and competitive elements to use profits from its monopoly elements to cross-subsidise its competitive elements. Thus, the Commonwealth and Victorian approach may require prices oversight arrangements to control anti-competitive behavior.

Debt guarantee fees

All jurisdictions, except Queensland, have introduced debt guarantee fees to their significant business activities. The aim of imposing a guarantee fee is to remove any preferential treatment with respect to borrowing money that may arise from public ownership. Queensland is currently developing its policy on debt guarantee fees.

Western Australia and the Northern Territory apply a fee of 0.2 percent to all government businesses. All other jurisdictions have introduced entity specific debt guarantee fees. These fees reflect the difference between the interest rate charged on loans to government businesses when guaranteed by

the government and the market rate that an equivalent private sector business would pay. Entity specific fees provide a more accurate means of introducing competitive neutrality, although as with target rates of return, there may be instances where the costs associated with an entity specific approach outweigh the gains.

Taxation neutrality

Just as private businesses must take account of taxes and other government charges in setting prices, so the CPA requires that government businesses incorporate relevant taxes and charges in setting a competitively neutral price.

Currently, Commonwealth, State and Territory trading enterprises pay taxes or tax equivalents in order to meet their competitive neutrality obligations.

In the interests of microeconomic reform, the Commonwealth, States and Territories recently agreed to investigate the merits of applying reciprocal taxation, on a revenue neutral basis, to their various commercial enterprises and activities. Reciprocal taxation is defined as each taxing authority (Commonwealth, State or Territory) applying all of its taxes to agreed activities within its geographical boundaries.

The taxation treatment of local government business entities will be considered within the context of the reciprocal taxation review and broader taxation reform. The Commonwealth has given local government a commitment that it will not be financially disadvantaged, at an aggregate level, from the corporatisation of its business activities.

Identifying significant business activities

Under the CPA, competitive neutrality principles are to be applied to significant government business activities. Jurisdictions' approaches to identifying such businesses are discussed in section B4.4.

During the past 12 months, the Council has received a number of inquiries from members of the community who believe that they have been affected by 'unfair' competition from government businesses. Commonly, these inquiries focused on the business activities of local governments and social services.

Local government

Many of the inquiries received by the Council have questioned the appropriateness of competition between local government and private sector businesses. The Council has also received claims that government subsidies enable local governments' businesses to lower prices below cost. The first of these issues is discussed below, the second has been discussed earlier in this section in considering appropriate use of CSOs.

The NCP is designed to promote competition subject to governments' social and economic priorities. Under the NCP, governments, including local governments, are not precluded from operating business activities that compete with local private sector businesses.

Consequently, the decision to allow councils to operate business activities falls outside the scope of the NCP and is a matter of State Government policy. However, where significant local government businesses compete with private providers, competitive neutrality principles should be applied to ensure that they do not have any artificial advantages arising from their government ownership.

Social services

The second reading speech accompanying the Commonwealth Competition Policy Reform Bill (1995) makes it clear that the business activities of sectors such as education, health welfare, community services and employment services are included within the scope of the NCP.

In 1996-97, governments spent more than $47 billion on providing social services, ranging from services for the homeless and the aged, to education, child care and justice services (SCRCSSP 1998). Even though government

spending in this area accounts for about 9 percent of Australia's gross domestic product, demand still significantly outweighs supply in many areas (SCRCSSP 1998). Australia's ageing population suggests that further increases in demand are likely.

To make the most of available resources, all governments have been examining how best to provide social services. Provided that appropriate standards are met, some services are provided by public and/or private providers. For example, child care is provided by government, private and community organisations. Further, the emergence of private providers in areas such as services for the homeless, child care and home care for the frail aged shows the potential for competition between public and private suppliers in these areas.

There are also competitive elements within government agencies that have a predominantly policy role. For example, public housing comprises property management services and the welfare component of public housing, tenancy management. Within fire services, Victoria and Western Australia have 'ring-fenced'[2] potentially competitive functions, such as alarm installation and maintenance, within public bodies.

The existence of competitors (or potential competitors) in these areas emphasises the need for appropriate competitive neutrality arrangements. Governments' role as a purchaser, rather than a provider of services, often necessitates a government business unit bidding against private suppliers or other government suppliers. For example, a recent in-house bid by the Queensland Corrective Services Commission was successful in securing a contract to build and operate the Woodford Centre correctional facility in spite of competition from private sector bidders. Where in-house bids or bids by other government providers are made it is important that this occurs on a competitively neutral basis.

Similarly, there is an increasing trend towards providing assistance to service clients directly rather than subsidising service provision, allowing clients to choose the service that best suits their needs. For example, recent increases in housing assistance payments enable public housing clients to choose their

2 Ring-fencing involves separating financial and administrative business units within a single entity.

preferred service provider. In these situations, competitive neutrality is important as the government now competes directly with community and private providers.

Most jurisdictions are now introducing competitive neutrality principles to government businesses providing public housing services. Other areas, such as health, education and justice are still under review. The importance of maximising community outcomes in these areas suggests reviews will need to remain high on governments' agendas.

Private sector service providers in these areas have raised a number of questions with the Council. For example, private child care services have stated that they are placed at a competitive disadvantage as a result of subsidies available to local government child care services. As discussed above, while the CPA does not preclude governments from subsidising activities transparently, providing funding through a contestable CSO may enable the government to achieve its desired outcome at the lowest possible price while maintaining quality.

Similarly, the Council has also received calls for the introduction of competition for government funds provided for industry research. At present, such funding is exclusively available to universities. Private sector research organisations argue that they are able to provide equivalent services and should be able to bid for funding.

In other areas, obligations arising from competitive neutrality commitments are less clear. For example, the Council received a complaint regarding alleged competitive advantages arising from public hospitals' exemption from fringe benefits tax (FBT). On this matter, jurisdictions noted that the exemption arises from public hospitals' status as public benevolent institutions and that similar exemptions are available to other not-for-profit organisations such as private charities. Given that any advantage experienced by public hospitals as a result of the FBT exemption is due to their status as public benevolent institutions and not their public ownership, this matter is a question of government taxation policy rather than competitive neutrality.

Similarly, the Council has received complaints regarding products made by prison-based businesses being sold at below cost. In this case, governments

have to weigh the benefits of facilitating competition between private and public providers against social objectives such as fewer repeat offences, lower containment costs and higher prisoner quality of life. The CPA provides for exemption from competitive neutrality principles where the community benefit arising from these factors outweighs the benefit from greater competition.

B4.6 The next steps

Over the past 12 months, jurisdictions have continued to push forward with competitive neutrality reform. A large number of competitive neutrality reviews of government businesses have been completed and preparatory work such as guidelines and workshops have helped in developing a consistent approach to reform. However, it is important that jurisdictions build on these early efforts and introduce timely reform so that the gains offered by competitive neutrality reform are realised. To do this, there are a number of areas that will require special attention.

Introducing prices that reflect full attribution of costs is proving to be a challenging task. The Council will be looking to see that where prices are set below the efficient level, governments are aware of the full cost of the activity and that any subsidies are provided through a clearly defined and separately funded CSO.

All jurisdictions have established a process for introducing competitive neutrality to local governments and have made progress in this area. While the Council recognises that there are some complexities associated with local government reform not experienced by other areas, this should not be a barrier to progress. The Council will be looking for continued progress with local government reform in conducting its next assessment in 1999.

In the area of social services, public providers often face actual or potential competition from private or community providers. Where government providers compete with other providers competitive neutrality is important to ensuring that the community receives the services it needs at the lowest possible cost.

Competitive neutrality complaints mechanisms provide an important safety net and indicator of the effectiveness of each government's competitive neutrality policy. Competitive neutrality complaints provide feedback on how well governments have removed competitive advantages arising from the public ownership of their businesses activities. Accordingly, the Council will be scrutinising competitive neutrality complaints and reform outcomes arising from complaints in conducting future assessments. The Council supports complaints mechanisms that encourage wide application of competitive neutrality principles.

B5 STRUCTURAL REFORM OF PUBLIC MONOPOLIES

B5.1 Background

In competitive markets, the structure of firms and industries evolves over time in response to changing market conditions, including shifts in consumer demand and changing cost structures. This flexibility and responsiveness to change can foster business and market structures that promote efficiency, minimise waste and allow customer requirements to be readily met.

For example, in the grocery retail market, the advent of better transport options and changing lifestyle patterns has resulted in a structural shift towards larger retail outlets which provide wider product choice, longer opening hours and lower prices. Likewise, many petrol stations now remain open 24 hours and stock a range of convenience items.

But in the case of some public monopolies, protection from competition through regulation or other government policies has allowed structures to develop that are less responsive to market conditions. Strategies that may rectify this include:

- ➤ removing the relevant regulatory restrictions on competition;
- ➤ applying competitive neutrality principles to the monopoly; and
- ➤ providing access to any infrastructure services supplied by the monopoly.

These reforms are discussed in Chapters B3, B4 and B12 respectively, but such reforms will not always be sufficient to establish effective competition.

Where a government business has developed into an integrated monopoly, structural reform might be needed to dismantle it. In essence, structural reform involves the introduction of competition or, at a minimum, the removal of barriers to new businesses competing in the market, and it often

involves splitting a monopoly (or parts of it) into a number of smaller, separate entities. Structural reform is particularly important where a public monopoly is to be privatised. If appropriate reform is not undertaken beforehand, privatisation will simply result in a private monopoly supplanting the former public monopoly, with fewer potential gains and some risks.

Governments have been undertaking structural reform of public monopolies since about the late 1980s.

Under the Competition Principles Agreement (CPA), governments agreed to apply certain procedures and principles before privatising their monopoly businesses or introducing competition to public monopoly markets. These principles seek to ensure that governments systematically consider regulatory and business structure issues before engaging in privatisation or introducing competition. Importantly, the principles do not require governments to privatise or introduce competition.

B5.2 Governments' commitments

Under clause 4 of the CPA, before introducing competition into a sector traditionally supplied by a public monopoly, governments agreed to relocate any industry regulation functions away from the public monopoly, to prevent it enjoying a regulatory advantage over its (existing or potential) competitors.

As well, before introducing competition or privatising a public monopoly, governments are to review:

- the appropriate commercial objectives of the public monopoly;
- the merits of separating potentially competitive elements of the public monopoly from the natural monopoly elements;
- the merits of separating potentially competitive elements into independent competing businesses;
- the best way of separating regulatory functions from the monopoly's commercial functions;

- the most effective way of implementing competitive neutrality;
- the merits of any community service obligations (CSOs) provided by the public monopoly, and the best means of funding and delivering any mandated CSOs;
- the price and service regulations to be applied to the relevant industry; and
- the appropriate financial relationship between the owner of the public monopoly and the public monopoly.

Governments can seek the Council's assistance in conducting such reviews.

Adherence to these principles is relevant for the Council's assessment of governments' performance in relation to each of the three tranches.

B5.3 Progress to date

State and Territory reforms

All State and Territory governments have expressed a strong commitment to the CPA structural reform principles. All indicated they have complied with the principles wherever they have introduced competition into markets traditionally served by public monopolies and where they have privatised public monopolies.

Governments have undertaken the most extensive structural reforms in the electricity, gas and water markets (see Chapters B7, B8 and B9), and the States and Territories have also reviewed and reformed the structure of public monopolies in a number of other areas. Some examples are outlined in Box B5.1.

Box B5.1 Some State and Territory structural reforms

As well as reforming their gas, electricity and water utilities, States and Territories have undertaken other structural reforms over the past few years.

- NSW has separated the operation of rail services from the ownership, provision of access and the maintenance components of the State Rail Authority. Four transport entities now exist: the State Rail Authority; Rail Services Authority; Rail Access Corporation; and FreightCorp.
- Victoria has substantially restructured its public transport sector. The Public Transport Corporation has been broken up into five separate businesses, providing country passenger rail, metropolitan passenger rail, rail freight, tram and bus services. Victoria has recently called for expressions of interest for the sale of its rail freight business, V/Line Freight.
- In Queensland, a comprehensive process of structural reform of the Totalisator Agency Board (TAB) is underway, involving changes to its commercial structure, the structure and level of wagering taxation, and the regulatory regime. The TAB's regulatory functions will be transferred to the Queensland Office of Gaming Regulation within the Treasury Department.
- In Western Australia, several of Transperth's operations relating to the provision of public bus, ferry and rail transport services in the Perth metropolitan area have been relocated to other bodies.
- Tasmania has separated the regulatory and commercial functions of its port authorities, and removed barriers to entry for the private ownership and operation of ports.
- In the ACT, responsibility for the regulation of public bus transport is being transferred from ACTION (the single service provider) to the Department of Urban Services.

Source: Jurisdictions' annual progress reports

The Commonwealth's reforms

The Commonwealth has restructured and/or privatised several of its business activities in recent years. In 1998, for example, Medibank Private became a Government Business Enterprise and the Australian National Line (ANL) was privatised.

In its 1997 Annual Report, the Council raised questions as to whether competition issues were being appropriately addressed in relation to changes in the structure and operation of: Commonwealth Funds Management; DASFLEET; ANL Limited; and the former Civil Aviation Authority (now Airservices Australia and the Civil Aviation Safety Authority). Following discussions with the Commonwealth, the Council is confident that the Commonwealth's approach with regard to the four businesses is consistent with clause 4 of the CPA.

The Council has also considered three other matters in the context of the Commonwealth's commitments under clause 4 of the CPA:

- the 1997 sale of part of Telstra;
- the restructuring of the Federal Airports Corporation (FAC) and the airports divestment process; and
- the forthcoming restructure and sale of the Australian Wheat Board (AWB).

Telstra

Telstra is a fully vertically integrated provider of telecommunications products and services, and prior to 1991, was a monopoly provider of all telephone services in Australia. While Telstra has been increasingly exposed to competition primarily from Optus, it retains monopoly control of its local fixed network.

The Commonwealth privatised one-third of Telstra in 1997. It is now intending to divest another tranche of Telstra that will take the level of private sector ownership to 49 percent. The Commonwealth has announced its support, in the longer-term, for divestment of the remaining 51 percent, subject to Telstra meeting prescribed service levels.

The Council considers that clause 4 placed a responsibility on the Commonwealth to have examined, prior to the partial privatisation in 1997, the appropriate treatment of the remaining monopoly element of Telstra's business, the local fixed network. Such an examination should have considered the merits of structurally separating the local fixed network from the non-monopoly elements of Telstra's business or, alternatively, arrangements for ring-fencing the local fixed network and Telstra's business units. The Council accepts that the framework for the regulation of the telecommunications sector is consistent with CPA principles, at least to the extent that responsibility for regulation is independent of Telstra.[1]

Whilst the Commonwealth has not undertaken a formal clause 4 review, it noted that industry regulation does not lie with Telstra. The Commonwealth also advised the Council that competition and regulatory matters were addressed in a series of reviews pertinent to both the partial sale of Telstra and the broader telecommunications sector. These reviews include the Telecommunications Policy Review, the Telstra Scoping Study, the Review of the Standard Telephone Service and the Senate Committee report *Telstra: to sell or not to sell?*

The Commonwealth stated that the pre-privatisation reviews had led to the development of the current regulatory framework and other arrangements relevant to clause 4, including delivery of the telecommunications universal service obligation through an industry levy.[2] The Commonwealth indicated that it did not pursue structural separation of the local fixed network, preferring to prohibit anti-competitive conduct by carriers or carriage service providers (Part XIB of the TPA) and to facilitate access to services provided by carriers or carriage service providers (Part XIC of the TPA).

Part XIB of the TPA includes provision for the Australian Competition and Consumer Commission (ACCC) to make 'record-keeping rules' which enable it to, among other things, require telecommunications carriers to furnish specific accounting information necessary for analysis of predatory behaviour and the cost of providing network access. This provision exists

1 The Australian Communications Authority deals principally with consumer protection, technical standards, and management of the radio communications spectrum, while the ACCC deals with market conduct.

2 The industry levy arrangement has been in place since 1991.

because of the potential for vertically or horizontally integrated telecommunications carriers to have internal cost allocation arrangements which are counterproductive to investigations of predatory behaviour and to determining the cost of providing access to a carrier's network.

Allied with its intention to increase the proportion of private ownership of Telstra, the Commonwealth recently proposed changes to the regulatory regime governing telecommunications, including amendments to the existing telecommunications-specific anti-competitive conduct and access provisions of the TPA. These changes were contained in the *Telstra (Transition to Full Private Ownership) Bill 1998* (as amended), which was defeated in the Senate on 4 July 1998.

The changes proposed by the Commonwealth would allow the ACCC to, among other things, disclose cost information kept by virtue of record-keeping rules and to establish a binding code of practice on how carriers provide other carriers with telecommunications network information, and use this information. Greater transparency of costs and certainty on use of commercial information should assist negotiations under the telecommunications access regime, which is designed to limit Telstra's monopoly power over its local fixed network.

The intended effect of the arrangements in place under Part XIB and Part XIC of the TPA is to limit possible anti-competitive behaviour arising from Telstra's local fixed network monopoly. The additional safeguards proposed in the *Telstra (Transition to Full Private Ownership) Bill 1998*, once in place, would go a considerable way to addressing the Commonwealth's responsibilities under clause 4 with respect to Telstra.

Federal Airports Corporation

In April 1996, the FAC adopted a new organisational structure in preparation for the sale of long-term leases to 22 airports. Many of these leases have since been sold. Once the current phase of airport divestments is completed, the Commonwealth will retain only Sydney's Kingsford Smith Airport, the two Sydney Basin general aviation airports, the second Sydney airport site and Victoria's Essendon Airport.

In the view of the Council, there were significant monopoly characteristics associated with the FAC. It was the operator of a number of localised monopolies including, importantly, the major passenger airports in all capital cities.

The Commonwealth stated that it had examined airport competition issues in 1994 as part of a major scoping study undertaken as a precursor to the airport sales process. It also pointed to a Department of Transport and Regional Development review of the regulatory regime for airports. The Council agrees that the current regulatory environment meets the objectives of clause 4, but on the basis of the information available, cannot be certain that other clause 4 considerations were appropriately addressed in the 1994 scoping study.

Acknowledging that the airports divestment process is well advanced and that the FAC's operational responsibilities cease this year, the Council considers it appropriate for the Commonwealth's attention to focus on the structure of the existing and proposed Sydney international airports. On the basis of recent discussions with Commonwealth officials, the Council is satisfied that the Commonwealth has put in place processes to enable clause 4 matters to be addressed in relation to the Sydney airports. The Council will consider this matter in future assessments.

Australian Wheat Board

The Commonwealth has prepared legislation to give effect to, among other things, the restructure and privatisation of the AWB, and the creation of the Wheat Export Authority (WEA). These changes will give wheat growers ownership and control of all commercial aspects of wheat marketing, with the Government's only remaining involvement being the provision of the export monopoly to the grower-owned company.[3]

The AWB currently holds a monopoly on the right to export wheat, and will retain this monopoly after the proposed restructure and privatisation. In these circumstances, the Council considers it is appropriate for the Commonwealth to examine the competition issues associated with the privatisation.

3 Continuation of these arrangements will be subject to the outcome of a legislative review in 1999-2000 in accordance with clause 5 of the CPA.

However, it appears that, as yet, the Commonwealth has not conducted a clause 4 review of the AWB. A review would need to consider a number of regulatory issues, including:

- the appropriate commercial objectives of the privatised monopoly;
- the implications of granting the wheat export monopoly to a privatised entity; and
- the structure of the export authority and its relationship with the grower-owned company.

The Council will consider this matter in future assessments.

B6 PRICES OVERSIGHT OF PUBLIC MONOPOLIES

B6.1 Implementing prices oversight

Legislated monopolies, and businesses that operate in markets with natural monopoly characteristics or where competition is weak, have considerable potential to engage in monopolistic pricing behaviour: that is, they may be able to restrict output and charge higher prices.

Exposing sheltered areas of the economy to enhanced competition can encourage greater efficiency in the supply of goods and services. To achieve this, governments have committed themselves under NCP to reviewing regulatory barriers to entry, implementing competitive neutrality arrangements, considering restructuring public monopolies and providing rights of access to significant facilities (as discussed in Chapters B3, B4, B5 and B12 respectively).

However, as effective competition may not always be achievable or may take time to develop, government oversight of prices can be an appropriate option.

The principal mechanism for prices oversight in Australia is the *Prices Surveillance Act 1983*. Under this legislation, the Commonwealth Treasurer may 'declare' private businesses and major Commonwealth agencies such that they must notify proposed price increases to the Australian Competition and Consumer Commission (ACCC).

Under the Competition Principles Agreement (CPA), the States and Territories agreed to consider establishing independent sources of prices oversight of their monopolistic business enterprises where oversight arrangements do not already exist. The States and Territories can establish their own process or, with the agreement of the Commonwealth, subject their business enterprises to a mechanism administered by the ACCC. All States and Territories, except Western Australia and the Northern Territory, have established independent prices oversight arrangements. Box B6.1 sets out current arrangements.

Box B6.1 State and Territory prices oversight arrangements

- In NSW, prices oversight has been provided by the Independent Pricing and Regulatory Tribunal (IPART) since 1992. IPART has pricing responsibilities in electricity, gas, water, waste and urban passenger transport, as well as for the Valuer-General.
- In Victoria, the Office of the Regulator-General provides independent prices oversight in electricity, gas, water, ports and grain handling.
- Similarly, the Queensland Competition Authority is responsible for independent prices oversight of declared public sector monopolies in Queensland.
- In November 1997, the ACT Government replaced the Energy and Water Charges Commission with the Independent Pricing and Regulatory Commission (IPARC). IPARC has the power to make pricing directions, access determinations and carry out other functions with respect to industries declared by the Minister. To date, IPARC has conducted or is conducting inquiries into the pricing of electricity, water, sewerage, taxi and bus services.
- In Tasmania, the Government Prices Oversight Commission regulates the pricing policies of the State's monopoly or near monopoly GBEs and government agencies, including the Metropolitan Transport Trust, the Hydro-Electric Corporation and a range of other government (including local government) businesses.
- In South Australia, the *Government Business Enterprises (Competition) Act 1996* establishes a prices surveillance mechanism for the State's monopoly or near monopoly government businesses, including those in the water sector.
- Neither Western Australia nor the Northern Territory has established an independent prices oversight body.

Source: Information supplied by jurisdictions.

With the extension of oversight arrangements to monopolistic State and Territory businesses under the CPA, the Commonwealth can also declare a State and Territory business for prices surveillance by the ACCC. It can do this without the consent of the owner government, provided it receives a recommendation to do so from the Council.

B6.2 Council recommendations for prices surveillance

Under the CPA, where a State or Territory business is not already subject to independent prices oversight, that business can be declared for prices surveillance by the ACCC without the consent of the owner government. For this to happen, the following criteria must be satisfied:

- a jurisdiction that considers it is adversely affected by the lack of prices oversight has consulted the owner government, but has been unable to resolve the matter;
- the affected jurisdiction has brought the matter to the attention of the Council, and the Council has decided that:
  - the enterprise is not already subject to independent prices oversight; and
  - the pricing of the enterprise has a significant impact on interstate or international trade or commerce;
- the Council has recommended that the Commonwealth Minister declare the enterprise for prices surveillance by the ACCC; and
- the Commonwealth Minister has consulted the owner government.

In 1997-98, no such matters were brought to the Council's attention.

B7 ELECTRICITY

B7.1 Background

The electricity supply industry is one of Australia's largest, with $57 billion in assets, a workforce of 35 500 people, 8.2 million customers and $12.6 billion in annual revenue (ESAA 1998). The industry provides the main source of energy for most households and is an important input to almost all businesses. For many businesses, including most large manufacturing plants, electricity prices are an important determinant of competitiveness, both domestically and internationally.

Historically, the electricity industry developed on a state-by-state basis, with one government-owned vertically-integrated[1] electricity utility dominating in each state and little electricity trade between jurisdictions. Cross-subsidies between different customer classes were common. There was little incentive to improve the level of services to customers, overstaffing was common and some states had built too many power stations and related infrastructure. This was because their utilities made investment decisions without the disciplines provided by competition. Even so, Australia has enjoyed a comparative advantage over most other countries in electricity prices because of factors such as abundant supplies of coal.

The industry is now undergoing dramatic change in terms of structure, ownership and regulation, with the prospect of improved efficiency and lower prices.

In July 1991, governments agreed to work cooperatively to improve competitiveness in the industry. The National Grid Management Council

1 'Vertical integration' refers to an industry structure wherein one business controls different elements of the supply chain. For example, in electricity, the supply chain can be broken into five segments: fuel supply; generation; transmission (that is, long distance transfer of electricity using high voltage wires); distribution (that is, short distance electricity transfer using lower voltage wires within a specific urban area); and retail. Vertically integrated businesses would undertake two or more of these functions: for example, electricity generation and transmission. In the past, some State utilities performed all four functions.

was established, with the ultimate aim being to replace separate State markets with a competitive electricity market covering southern and eastern Australia.

In June 1993, six governments — the Commonwealth, NSW, Victoria, Queensland, South Australia and the ACT — committed to undertake reforms necessary to allow a competitive electricity market to commence from July 1995. They agreed to establish an interstate electricity transmission network involving those States already inter-connected, together with Queensland. They also agreed to separate the transmission elements of their existing electricity utilities from the generation elements, and turn them into stand-alone corporations. The principles underlying these reforms were that:

- generators should compete for the right to supply electricity;
- there should be open access to the grid for new generation; and
- customers should be free to choose who supplies their electricity.

At the April 1995 COAG meeting, these reforms were extended and brought within the NCP process — with payments to the States and Territories depending partly on adequate progress in implementing the reforms, which is to be assessed by the Council.

The National Grid Management Council has since developed trading rules, network pricing principles, system controls and rules for access to networks, and other matters. These have been incorporated into an electricity Code of Conduct (the Code),[2] and submitted to the ACCC for approval.

Two institutional bodies have also been established: the National Electricity Code Administrator (NECA) and the National Electricity Market Management Company (NEMMCO). NECA will be responsible for enforcing the Code; dispute resolution; managing changes to the Code; and reporting on compliance with the Code and its adequacy. NEMMCO will be responsible for managing the power system, including national merit order dispatch of generation and controllable load, and operation of the spot and forward trading markets.

2 The Code comprises two elements: the wholesale electricity market arrangements and the arrangements for access to the transmission and distribution systems.

The Code includes derogations (exemptions) to allow some jurisdictional based arrangements that depart from the Code to continue. State and Territory governments will retain responsibility for environmental issues, retail arrangements and regulation. Independent State regulators have been established in some cases with responsibility for the economic regulation for transmission and distribution services, distribution and retail licence conditions and franchise customer pricing. Responsibility for the regulation of transmission revenue will be transferred from the States to the ACCC progressively from July 1999.

The Code has been endorsed by the participating jurisdictions which have agreed to enact parallel legislation, the National Electricity Law, to implement the regulatory arrangements that support the Code. This will enable the Code to have identical force and effect across jurisdictions.

B7.2 Governments' commitments

For the first tranche of competition payments under NCP, (relevant) governments agreed to take "all measures necessary to implement an interim national electricity market (NEM), as agreed at the July 1991 Special Premiers' Conference, and subsequent COAG agreements, from 1 July 1995 or on such other date as agreed by the parties, including signing any necessary Heads of Agreement and agreeing to subscribe to NEMMCO and NECA."

Relevant jurisdictions also agreed to the structural separation of generation and transmission, and to ring-fence[3] the 'retail' and 'wires' businesses within distribution.

3 'Ring-fencing' involves separating financial and administrative business units within a single entity.

For the second tranche, governments agreed to the effective implementation of all COAG agreements on the establishment of a competitive NEM. Relevant jurisdictions are to complete the transition to a fully competitive NEM by 1 July 1999.

For the third tranche, States and Territories are to fully implement, and continue to observe fully, all COAG agreements with regard to electricity. Queensland is committed to establishing an interconnection with NSW, after which it is to become a full participant in the national market.

B7.3 Progress to date

Some States have already undertaken significant reform, including the establishment of internal wholesale markets in Victoria, NSW and Queensland. For instance, the Victorian industry has been fundamentally restructured and re-regulated, transforming a publicly owned vertically integrated monopoly into privatised competitive markets with lower prices and improvements in services. All of this has been achieved in only a few years.

The major focus of *national* electricity reform has been the establishment of a competitive wholesale market encompassing eastern and southern Australia, and it is here that progress has been more problematic.

The national market was initially intended to commence in July 1995, but there has been significant slippage. This partly reflects the inherent difficulties involved in developing, and gaining agreement to, the national reforms in an area as complex as electricity.

In December 1996, the Prime Minister proposed a revised phased implementation timetable for national electricity reform. The timetable, which has been agreed to by all governments, sets out key reform dates, including:

- harmonisation of the NSW (including the ACT) and Victorian wholesale electricity markets (NEM1 Phase 1) by February 1997;

- authorisation of the National Electricity Code by the ACCC for the purposes of Part IV of the TPA and acceptance of the Code as an industry access code for the purposes of Part IIIA of the Act by April/May 1997;
- further harmonisation of Victorian and NSW markets (NEM1 Phase 2) by July 1997;
- passage of legislation to give effect to the National Electricity Law by participating jurisdictions by Autumn 1997; and
- full implementation of the market arrangements specified in the National Electricity Code by early 1998.

There has been some further slippage. NEM1 Phase 1 commenced in May 1997 — three months later than scheduled — with direct trade between NSW, Victoria and the ACT, and indirectly with South Australia.

The ACCC granted conditional authorisation to the arrangements under the Code governing the wholesale market in December 1997. The ACCC considered that, despite structural and other reforms at the jurisdictional level, the full benefits of reform depend on implementing the national electricity market and access arrangements under the Code. This was because the national arrangements have efficiency benefits in terms of better utilisation of infrastructure than provided for in existing State based regimes, as well as other benefits. However, the ACCC identified a number of elements in the Code that needed to be rectified, and granted authorisation subject to conditions. It expected NECA and NEMMCO to satisfy the conditions prior to the commencement of the national market, and the Council understands that this was finalised in July 1998. The second element of the Code – the rules governing access to and use of the physical wires infrastructure is not yet finalised, although a draft determination was released in August 1997. It is expected that these will be resolved by September 1998.

The deadline for implementing the national electricity market has been deferred several times, including twice in 1998. On 16 July, NEMMCO announced that the NEM is set to begin on 15 November, once the necessary systems that will enable the market to be operated in accordance with the Code are in place.

State by State developments

In relation to their other first tranche commitments:

- NSW, Victoria, South Australia and the ACT have subscribed to NEMMCO and NECA, as required. Queensland is only required to subscribe to these institutions upon interconnection with NSW, which is scheduled by 2000-01;
- NSW, Victoria, Queensland and South Australia have also structurally separated generation from transmission; and
- NSW, Victoria, Queensland and the ACT have ring-fenced the 'wires' and 'retail' functions of the distribution businesses. South Australia indicated in November 1996 that it would wait until the NEM is established in full before it elects to join the market.

Each of the (relevant) States and Territories have issued timetables by which users and consumers become eligible to choose their retail supplier, with large users first followed by progressively smaller business users and, eventually, households (on 1 January 2001 in most cases). Business customers will also have the choice of buying directly from the wholesale market (NEM). The ability of customers to switch retailers or participate in the wholesale market will encourage retailers to price competitively and improve services.

Very large users became eligible in Victoria in November 1994 and in October 1996 in NSW. These markets have been progressively opened up and, in July 1998, retail customers with annual electricity consumption of between 160 to 750 MWh became eligible. Large users became eligible in late 1997 in the ACT and in March 1998 in Queensland.

Details of developments in the States and Territories are contained in Boxes B7.1 to B7.7.

Box B7.1 Victoria

- Victoria was the first State to restructure its electricity supply industry and has progressed the most, providing a testing ground for other jurisdictions. The industry has experienced fundamental change over the past five years, mainly from the restructuring and privatisation programmes, but also from market pressures, including rapidly changing consumption patterns.
- The first stage of separating the vertically integrated State Electricity Commission into generation, transmission and distribution activities was introduced in 1993. Next, in 1994, transmission was split into a wires business and a trading business to administer the wholesale market and ensure system security. The distribution and retail sectors were disaggregated into five companies, each operating as a ring-fenced distribution monopoly and competitive retailer.
- The Office of the Regulator-General (ORG) was established in 1994 to ensure that restructured enterprises do not abuse their market power, to promote competitive market conduct and efficiency, to facilitate entry into markets, and to ensure that users and consumers benefit from the reforms. Distribution is regarded as a local monopoly and is regulated by the ORG. The retail market is progressively being opened up, with the ORG responsible for price and service regulation for a transitional period.
- The Government has privatised all five of the distribution/retail businesses and most of its generation businesses, with total returns reportedly approaching $23 billion. There were concerns that the prices realised with the sale of the distribution businesses would be reflected in the tariffs set by the ORG after the year 2000 when the Tariff Order (price path) set by the Government prior to privatisation expires. However, the Council understands that the ORG is required to only have regard to asset values prior to sale.

Box B7.1 …cont

- Competition in the Victorian electricity wholesale market was introduced in late 1994 when 47 very large users were able to choose their supplier. Choice was extended to a further 330 customers in July 1995 and a further 2300 a year later. From 1 July 1998, about 9000 smaller businesses that consume between 160 and 750 MWh a year became contestable. The final phase is scheduled for 1 January 2001, when all sites, including households, will be contestable.

Box B7.2 New South Wales

- The NSW Government restructured its electricity industry in 1994 and 1995, separating transmission activities from its generation utility, Pacific Power, to form a new corporation (trading as Transgrid). Pacific Power was subsequently split into three independent government-owned generation businesses (Pacific Power, Delta Electricity and Macquarie Generation). Moreover, 25 distribution bodies were amalgamated to form six large (government-owned) independents, but with monopoly network functions ring-fenced from retail services. The first phase of retail competition was introduced in October 1996 when large users were allowed to choose suppliers. As in Victoria, smaller business users became contestable from 1 July 1998.
- The State regulator, the Independent Pricing and Regulatory Tribunal (IPART), announced on 18 June 1998 a special reference to report on the appropriate pricing of government monopoly electricity transmission and distribution services for the five year period from 1 July 1999. IPART will also investigate the appropriate pricing of government monopoly services to franchise customers.
- Proposals to fully or partially privatise the NSW electricity industry have been debated for a number of years. The Council understands that privatisation is not currently the endorsed policy of the Government.

Box B7.3 Queensland

- Queensland separated generation from transmission and distribution in January 1995. There was further restructuring in mid-1997 to increase competition in the generation and retail sectors and to provide independent regulation of the natural monopoly transmission and distribution sectors. Several new corporations were established in generation (Stanwell Corporation, Tarong Energy and CS Energy); AUSTA Energy (engineering services); Powerlink Queensland (transmission); and Ergon Energy, Omega Energy and Energex (retail). Ergon and Omega have since merged. The seven regional distribution corporations were retained.
- The Queensland Competition Authority has been established to regulate transmission, distribution and non-contestable retail prices.
- Queensland is not yet interconnected to the southern States; this is planned for 2001, but may occur earlier in late 2000. During this transitional period, Queensland is progressively introducing competitive trading arrangements based on a local spot market, increased consumer choice and the entry of new retailers. In September 1997, the ACCC granted interim authorisation to the arrangements and, in January 1998, granted interim authorisation to vesting contracts between the government-owned generators and retailers. These are designed to restrain the market power of the generators until interconnection. The first tranche of contestable customers was introduced in March 1998. On the commencement of the national market, Queensland will adopt much of the National Electricity Code in line with other jurisdictions.
- The Council understands that the new Queensland Government is assessing current policy in this area. The Council notes that any decision to re-integrate the three generation entities would appear to be contrary to the findings of the review under clause 4 requirements of the Competition Principles Agreement (CPA) in 1996.

Box B7.4 South Australia

- In February 1998, the South Australian Government announced plans to privatise ETSA Corporation and Optima Energy (formerly the SA Generation Corporation). Associated bills were introduced into Parliament on 30 June 1998, including the establishment of an independent regulator.
- The Government also reviewed structural and regulatory issues prior to privatisation, as required under clause 4 of the CPA. On 1 July the Government announced that it proposed that ETSA be structurally separated into high voltage transmission and distribution/retail businesses. In the second case, the distribution and retail arms will be 'ring-fenced' with separate accounting structures and will be offered for sale together under a common holding company. Cross subsidies between distribution and retailing will be eliminated.
- The Government also proposed that Optima Energy be split into three generation businesses, one covering two gas-fired generators in Adelaide (to be known as Gas Co), the second covering the coal-fired station at Port Augusta (Coal Co), and four other generators producing peak power (Peak Co).
- It also understood that governments would not undertake the proposed 'Riverlink' connection between South Australia and NSW, although this does not preclude private development. Other options are the development of a 500 megawatt gas-fired power station in Adelaide by Peak Co and the upgrading of the current interconnection with Victoria.
- The Government intends that the new industry structure will be overseen by an independent economic regulator to ensure that efficient firms remain viable and customers benefit from competition, to prevent the misuse of market power and to facilitate new entry into the industry. The regulator will be responsible for licensing, access, distribution and retail pricing for non-contestable customers (those unable to choose suppliers) up to the year 2003, and for transmission pricing until the ACCC takes over this function. The arrangements also support rural customers, limiting price differences with corresponding city consumers to 1.7 percent after deregulation in 2003.

Box 7.5 Tasmania

- The Tasmanian Government announced in April 1997 an intention to join the national electricity market by way of an interconnection (Basslink) and to sell the transmission, distribution and retail businesses of the Hydro-Electric Corporation (HEC), a vertically integrated monopoly supplier operating a predominantly hydro system. The proposed privatisations and introduction of competition triggered a review into the appropriate structure and regulatory environment for the distribution/retail businesses as required under clause 4 of the CPA. The review committee recommended that the businesses should be conducted by single and separate legal entities when retail competition is introduced (post-Basslink), with ring fencing of a combined entity until then.
- However, the Government did not accept that distribution and retail should be conducted by separate legal entities when competition is introduced, although it appreciated the intent behind the recommendation to ensure that an integrated business would not inhibit the establishment of new retailers in Tasmania. The Government was not convinced that this could not be achieved by ring fencing. The Council has supplied the Government with some comments on a range of alternative structures and obligations under NCP.
- The Government Prices Oversight Commissioner (GPOC) commenced an investigation in April 1998 into the pricing policies of the HEC in regard to the generation, transmission, distribution and retailing of electricity and control of the system. In July, Transend Networks was established to provide transmission services and Aurora Energy was set up for distribution and retail services. The HEC continues to provide generation and system control. The price and non-price regulatory functions of the Tasmanian electricity supply industry are to be consolidated with the GPOC (the Regulator).

Box B7.5 …cont

- The Tasmanian Electricity Code came into effect in July 1998. The Code sets out the rules for the integrated operation of the electricity system to ensure security and reliability of supply, as well as requirements for network connection, and access to and pricing of network services.
- The Government called for expressions of interest in July to build, own and operate a submarine electricity link connection with the Victorian grid (Basslink), to be operational by the end of 2002. If this eventuates, Tasmania would be able to import electricity when required, as during a drought, and to export hydro-electricity to other States at peak periods. This would add another competitor and expand peak capacity in the NEM generator market and enable electricity users in Tasmania to participate in the benefits of competitive supply.

Box B7.6 Western Australia

- Western Australia is not part of the national electricity market reforms but is developing its own State-based competitive market, introducing a third party access system to both the high voltage transmission system and the distribution network. However, Western Power continues to operate as a vertically integrated monopoly in Western Australia's electricity industry.
- The Government announced in March 1998 that it would consider partially privatising Western Power after the next state election, due by early 2001. Under clause 4 of the CPA, the Western Australian Government is required in these circumstances to undertake a review into the structure of Western Power. The Council considers that it is essential that electricity generation and transmission functions are structurally separate to ensure that the anticipated benefits from a more competitive electricity market are achieved. Western Australia has advised the Council that it is currently examining this matter, and that it has not ruled out separation of generation and transmission.

Box B7.7 The Territories

- The ACT Government corporatised its electricity distribution utility in 1995, including separating out of the regulatory functions. The 'wire's and 'retail' activities within the distribution business are ring-fenced. Transition to a fully competitive market commenced in late 1997 when customers using more than 4 GWh a year became eligible to choose their own retailer. This was extended to customers using more than 160 MWh a year in mid 1998, to bring the ACT in line with Victoria and NSW. The Independent Pricing and Regulatory Commission was established in November 1997 with responsibility for the oversight of prices and to facilitate access to the network.
- The Council understands that the Northern Territory Government does not plan to restructure its electricity industry. The Power and Water Authority is a vertically integrated monopoly which holds regulatory control for electricity services.

Benefits of reform

While reform implementation could be proceeding faster, there is growing evidence that measures already put in place are reaping rewards. Indeed, much of the benefit originally expected to be achieved by large electricity users by the year 2000 may have already been realised, with the prospect of further efficiency gains to come.

In 1995, the (then) Industry Commission estimated that medium to large businesses could expect real price reductions of 24.7 percent in NSW over the period 1994-95 to 1999-2000, with savings for new customers in Victoria on par with NSW. The report argued that these savings would largely accrue from the flow-on effect of productivity gains under competition and, to a lesser extent, from the phasing out of cross-subsidies to the residential sector (IC 1995).

Two surveys of large consumers taken in mid-1998 indicate that prices appear to have already matched the projections of the Industry Commission, while other services have also improved. According to the Australian Chamber of Manufactures (ACM), which surveyed around 400 companies, savings in bills since deregulation were 30.6 percent in NSW and 23.2 percent in Victoria, with an overall average of 26.3 percent (ACM 1998). A survey of some 100 large companies by Deloitte Touche Tohmatsu (1998) found that 88 percent of firms achieved savings of more than 20 percent, with a quarter reporting savings of more than 40 percent. The findings of the two surveys are summarised in Box B7.8.

The survey findings suggest that there have been savings driven by the greater counterveiling power of customers made possible in a competitive market. Providing customers with the ability to change suppliers is likely to result not only in lower prices but also a fundamentally different attitude by suppliers. Whether customers actually switch may not be important, it is the threat that they may do so which can change behaviour and stimulate competition. Even so, the survey suggests a willingness by large customers to shop around and to switch suppliers if necessary.

Further, deregulation does not appear to have been detrimental to the quality of supply or to the provision of other services. Disruptions to supply and subsequent restoration times have not deteriorated, and the data on outage duration in Australia for all types of customers suggest that quality may be improving. The average time customers were without supply in 1996-97 was 157 minutes, 14 minutes down on the previous year. In Victoria, minutes off supply have fallen from 266 in 1993-94 to 218 in 1996. At the same time, distributors/retailers are offering a wider range of services.

Box B7.8 The experience of large electricity users in NSW and Victoria since deregulation

- Almost all firms (96 percent, Deloitte[a]) have reviewed their supplier arrangements since deregulation, even though most firms (69 percent, ACM[b]) spent less than 2 percent of total expenditure on electricity.
- The predominant issue in negotiations with suppliers was price.

Box B7.8 …cont

- In the ACM survey, average savings in electricity bills was 26.3 percent (30.6 and 23.2 percent in NSW and Victoria respectively) ranging from 2 to 60 percent across companies. Prices increased for a few remote rural Victorian users.
- In the Deloitte survey, 88 percent of firms achieved savings of more than 20 percent, with average savings of 30 to 35 percent.
- Average charges varied considerably between retailers and customers. Annual charges ranged from $40 to $120 per MWh with an average of $75 ($73 for NSW, $76 for Victoria, ACM). There is no statistical relationship between the price and volume of usage per firm.
- One third (ACM) to one half (Deloitte) of firms had changed their supplier. This high rate of 'churn' was accentuated by the relative short length of contracts (ACM). No firm opted for buying directly from the wholesale market (Deloitte).
- Reasons other than price for switching included better service and understanding of client needs. An important reason for not switching was the quality of the previous relationship with the supplier.
- 55 percent of firms reported an external disruption to power over the previous year (44 and 65 percent in NSW and Victoria respectively, ACM), although 65 percent considered this was no worse than prior to deregulation and most (78 percent) believed that restoration times were no worse.
- Overall, 88 percent of firms stated they were better off under deregulation, 2 percent said they were worse off and 10 percent saw no change (most of which have not changed retailers, ACM). Most firms which had switched were satisfied with their new supplier (81 percent, Deloitte).

a) Deloitte: Survey of 100 large companies by Deloitte Touche Tohmatso, May 1998

b) ACM: Survey of 410 large companies by Australian Chamber of Manufactures, June1998

The electricity supply industry is continuing to achieve significant gains in labour productivity and this is being reflected to some degree in lower prices. Employment levels exceeded 70 000 in the late 1980s, when governments first became concerned at over-staffing. This had fallen to 62 000 by 1990-91. In 1996-97, employment was 35 500. Sales per employee (in GWh) increased by 2.6 percent in 1996-97 and are now more than double the level in the late 1980s.

NSW and Victoria enjoyed the largest average real price reductions across all sectors in 1996-97, at 6.2 and 5.5 percent respectively. Tasmania also achieved a significant reduction (3.5 percent), but real prices increased in South Australia (2.5 percent).

For the industrial sector, average prices for Australia in 1997 were the third lowest of 16 selected OECD countries (ESAA 1998). The average price of 6.9 Australian cents per KWh here may be compared with the UK (8.9), Germany (12.5) and Italy (13.8). Only Finland (6.3) and Canada (5.4) were lower. Residential prices in Australia were also the third lowest of the 16 countries. Moreover, electricity prices for contestable companies in Melbourne and Sydney were reportedly about 4 cents per KWh in April 1998, suggesting that such businesses would have an advantage over domestic and international rivals (NUS 1998).

Whether such price levels are sustainable is unclear. On the one hand, the costs of supply may be reduced over time through the further restructuring of capital and product markets. In generation, factors such as improved capital investment decisions and the flow-on benefits of gas reform could also be significant. And in distribution/retailing, there could be economies of scale and of scope from areas such as the greater use of 'back offices' and call centres. On the other hand, there is also a view that current pool prices and retail margins in south-east Australia are unsustainably low.

While the price reductions in south-east Australia are due in part to the operation of the interim NEM and interstate trade, many of the gains are likely to be attributable simply to the introduction of wholesale trading arrangements. This is evident, for example, from the price reductions in Queensland since March 1998, where wholesale prices have fallen from $52 to around $40 per MWh (QERU 1998 as updated in August).

Deregulation was extended to cover small and medium businesses (with annual consumption of at least 160MWh) in NSW, the ACT and Victoria on 1 July 1998. The 1995 Industry Commission report referred to earlier estimated that this group could achieve a 51 percent reduction in real prices in NSW and 22 percent in Victoria between 1994-95 to 1999-2000. Anecdotal evidence from the ACM study suggests that the newly contestable customers are negotiating competitive deals and are prepared to switch suppliers.

The datelines for residential consumers to become contestable have been subject to revision but are likely to occur in most States by early 2001. The Industry Commission estimated in 1994 that real prices for the domestic sector could potentially decline by 10 percent in Victoria and 7.1 percent in NSW by 1999-2000, assuming the removal of all cross-subsidies and the pass-on of productivity gains.

The residential sector has already enjoyed price reductions. For example, a 'typical' Victorian household is estimated to have achieved a 9.2 percent real cut in the unit cost of electricity between November 1992 and May 1997. It is unclear how prices will change once households become contestable as there are some conflicting forces. For instance, the cost of metering may inhibit the spread of competition and cost pressures may arise from the further unwinding of cross-subsidies. On the other hand, there may be savings from the more efficient use of billing services. On balance, there are likely to be some gains to household consumers, but not at the level realised by business.

B7.4 The task ahead

The Council will be conducting its second tranche assessments over the year ahead. The reform specified by COAG at its August 1994 meeting for second tranche payments was that (relevant) jurisdictions complete the transition to a fully competitive national market by 1 July 1999. The four principal objectives for a competitive market set out by COAG were:

- the ability for customers to choose which supplier, including generators, retailers and traders, they will trade with;

- non-discriminatory access to the interconnected transmission and distribution network;
- no discriminatory legislative or regulatory barriers to entry for new participants in generation and retail supply; and
- no discriminatory legislative or regulatory barriers to interstate or intrastate trade.

Many of the reform mechanisms necessary for a fully competitive wholesale market to function successfully appear to be falling into place, and NEMMCO plans to implement the NEM from 15 November 1998. The ACCC conditionally authorised the Code relating to the wholesale market in December 1997 and those conditions have been satisfied, although the arrangements for access to the monopoly transmission and distribution wires need to be finalised.

That said, and while the Council's views about what particular issues will be drawn into the second tranche assessment process are yet to be finalised, there are some causes for concern. Most notably, the deadlines for enabling all customers the choice of supplier are moving outwards. The Council will monitor these developments and would be particularly concerned if there were to be any further slippage. One issue here is likely to be metering for newly contestable business customers, including delays in supply, the cost of meters and meter standards, and non-meter options for establishing load profiles. (Metering will also be an issue when all customers become eligible to choose their supplier, mainly in 2001). Another issue in the year ahead is likely to be the mutual recognition of electricity licences across jurisdictions, which would serve to facilitate new entry by retailers. Accordingly, in the second tranche assessment, performance will be closely monitored. This is a crucial area for the second round.

The Council will also be monitoring the progress of Queensland and Tasmania in respect of their commitments to inter-connect with the national market. As discussed, the Queensland reform process appears well on track, although there will be questions about the resolution of any differences between its market code and the national code. The recent announcements by the Tasmanian Government about implementing Basslink by the end of 2002 are encouraging (see Box B7.5).

B8 GAS

B8.1 Background

Australia's natural gas industry is undergoing significant reform aimed at promoting free and fair trade, and cheaper prices for customers. While much work remains to be done, the Council is pleased to report that a number of important steps were achieved in 1997-98. At the same time, the benefits of reform were evident in a number of significant price reductions for gas haulage.

Natural gas is Australia's fastest growing energy source. While currently satisfying around 18 percent of Australia's primary energy demand, this figure is expected to rise to about 28 percent by the year 2010.[1] As an alternative energy source to oil and coal, gas is an important business input. Major industrial users include the metals, chemicals, glass, brick and cement, and electricity generation industries. At the same time, gas is an energy source for over 2.9 million Australian households – mainly in Victoria and NSW.[2] Finally, gas is a major export earner – forecast to exceed $1.6 billion in 1997-98.[3] Overall, gas generates over $6 billion in annual sales, with a value adding contribution of $3 billion.[4]

On current trends, shortfalls in gas supplies are forecast in eastern Australia within the next decade. Investment in new infrastructure will be needed to address this problem. Indeed, plans for a number of new projects – including liquefied natural gas plants, pipelines, power stations and gas storage facilities – are well advanced. One of the biggest proposals is the Chevron gas pipeline from Kutubu in Papua New Guinea to south-eastern Queensland.

1 Data supplied by ABARE, July 1998.

2 Data supplied by AGA, July 1998.

3 Data supplied by ABARE, July 1998.

4 DPIE estimates prepared in 1997.

But barriers to competition within the gas industry have jeopardised – or at least, delayed – a number of these investment projects in recent years. At the same time, the absence of competition has been responsible for gas prices being considerably out of touch with underlying costs.

Historically, Australia's natural gas industry evolved as a series of State-based operations dominated by a few large enterprises. Within each State, a single transmission pipeline would connect a single gas basin with population and industrial centres. Competition was constrained by the dominance of a handful of producers over key gas basins. In addition, third party access to gas pipelines – where available at all – has typically been at tariffs set by the monopoly pipeline owners. At the same time, governments have supported anti-competitive arrangements in gas production and gas retailing to facilitate development of the industry.

The outcome has been highly integrated supply chains in each State supported by long-term exclusive contracts between producers, pipeliners and retailers. Consumers typically have had little choice but to buy a bundled package of gas and gas haulage services from a monopoly distributor supplied by other, 'vertically integrated' monopolies.

To address these concerns, the Council of Australian Governments (COAG) resolved in February 1994 to remove impediments to free and fair trade in natural gas. The underlying objective was to develop a nationally integrated and competitive industry in which consumers can contract directly with a gas producer of their choice for the supply of gas, and separately with a pipeline operator for gas haulage. This would encourage competition between gas basins and between producers within particular basins. To achieve this, COAG established several guiding principles and specific commitments for reform. In summary, it agreed by 1 July 1996 to:

- remove all legislative and regulatory barriers to free trade in gas;
- introduce a uniform framework for 'access' to gas transmission pipelines;
- reform gas franchise arrangements;[5]
- corporatise remaining government-owned gas utilities; and

5 No time-frame was specified for implementing this commitment.

- separate all government owned gas transmission and distribution activities, and 'ring-fence' privately owned transmission and distribution activities.

At the April 1995 COAG meeting, the above reforms were brought within the ambit of the National Competition Policy (NCP) process – with payments to the States and Territories being dependent in part on adequate progress in implementing the reforms.

B8.2 Governments' commitments

Governments committed in the 1995 Implementation Agreement to the effective implementation of all COAG agreements on the national framework for free and fair trade in gas. In summary, these commitments include:

- for the first tranche of competition payments, the effective implementation of all COAG agreements on the national framework for free and fair trade in gas between and within the States by 1 July 1996 or such other date agreed by the parties in keeping with the February 1994 COAG agreement;
- for the second tranche, the effective implementation of all COAG agreements on the national framework, including the phasing out of transitional arrangements in accord with a schedule to be agreed between the parties; and
- for the third tranche, participating States are to fully implement, and continue to fully observe, all COAG agreements with regard to gas.

B8.3 National Gas Access Regime

A central plank in the reform process has been the development of a National Access Code for the services of gas pipelines. The Code provides persons with the right to negotiate access to gas pipeline services on reasonable terms

and conditions approved by an independent regulator – with a right to binding arbitration to resolve disputes.

Customers can then buy gas directly from a gas producer or gas retailer of their choice, and purchase gas transportation separately from a gas pipeline company. The aim is to encourage competition between gas producers and retailers – which should result in better service provision and cheaper prices.

Under the national framework, infrastructure owners are required to submit access arrangements complying with the provisions of the Code to the regulator. Access arrangements must include reference tariffs for reference services (benchmark prices for standard services) which comply with specified pricing principles. Reference tariffs may be used to determine access prices or may serve as a basis for negotiation. However, the arbitrator must apply the reference tariffs in a dispute over pricing of a reference service.

Development of the Code began in 1995 when COAG established the Gas Reform Task Force to coordinate national gas reforms. By mid 1996, the Task Force had developed a draft National Code, originally to apply only to transmission pipelines. It was developed with significant involvement from government agencies and industry stakeholders. The draft Code was released for public consultation which led to a number of amendments. In June 1996, COAG agreed to broaden the scope of reform to apply to both distribution systems as well as transmission pipelines.

The initial target date for implementation – 1 July 1996 – was revised by COAG to 30 September 1996. In December 1996, the Prime Minister proposed a further extension to 1 July 1997. The slippage reflects the complexity of the Code and the delicate process of balancing the interests of infrastructure owners, gas consumers and the wider community. This process also revealed the need for a number of refinements to the Code, including a wider appeals process, amendments to the pricing principles and an optional competitive tendering process to set tariffs for proposed new pipelines.

In February 1997, the Gas Reform Implementation Group (GRIG) was given the task of finalising and implementing the Code. The GRIG comprised all State and Territory governments, the Commonwealth, peak industry/user associations[6], the Council and the ACCC. Following public consultation

involving some 1200 parties, the National Code was subject to a number of further refinements and signed off by Heads of Government in an intergovernmental agreement (IGA) on 7 November 1997.

The method for implementing the National Gas Access Regime is similar in most States to that used for the National Electricity Code – an 'application of laws' approach. South Australia acted as the lead legislator, with other jurisdictions then applying the South Australian law.[7] Each State's access legislation also covers matters such as the identity of the regulator and any derogations or transitional arrangements. Jurisdictions will then apply to the Council for certification of their regimes as effective under Part IIIA of the TPA.

Each jurisdiction agreed under the IGA to take all reasonable measures to ensure that its access legislation under the National Code is proclaimed and commenced by 30 June 1998. Governments further agreed to apply to the Council for certification of their access regimes within thirty days of enactment of their access legislation.[8]

South Australia, as lead legislator, enacted the *Gas Pipelines Access (South Australia) Act* in December 1997, and applied to the Council for certification of its access regime in June 1998. All other jurisdictions, with the exception of Western Australia, had enacted legislation giving effect to the Code by 30 June 1998. In the case of Western Australia, the relevant legislation had been introduced into State Parliament.

A number of Commonwealth legislative amendments were required to make the legislation enacted by the States and Territories operational. The Commonwealth's legislation – the *Gas Pipelines Access (Commonwealth) Act* – was passed on 9 July 1998.

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6 Australian Gas Association, Australian Petroleum Production and Exploration Association, Australian Pipeline Industry Association, and the Business Council of Australia.

7 The approach differs in Western Australia, which has agreed to a 'template legislation' approach – it will introduce legislation having an essentially identical effect to the South Australian legislation.

8 The timeframe differs for Tasmania, which currently has no natural gas industry. Tasmania has agreed to implement its access legislation – and seek certification – sufficiently before the first natural gas pipeline in the state is approved or any competitive tendering process for a new pipeline in the State is commenced.

Box B8.1 Gas reform: benefits in the pipeline

While the National Gas Access Regime – the centrepiece of the national gas reform agenda – has only just become operational, tangible benefits of reform are already emerging.

- Gas distribution prices for contract customers in NSW will fall by close to 60 percent in real terms, from $2.26 per GJ in 1995-96 to $1.05 per GJ in 1999-2000, under the AGL undertaking on gas distribution services. The AGL undertaking was approved by the NSW regulator in 1997 under an interim access regime closely modelled on the National Code. This will deliver major savings to more than 400 industrial and commercial gas users – with average costs of delivered gas expected to fall, on average, by around 20-25 percent (IPART 1997).
- In Western Australia, deregulation in the Pilbara region in 1995 resulted in a 50 percent price reduction for gas – providing major industrial users with some of the cheapest gas in the world outside the Middle East and Venezuela (Barnett 1996).
- Also in Western Australia, a transitional access regime for the State's pivotal Dampier-Bunbury pipeline provides for a 26 percent cut in gas transport prices – from $1.26 per GJ in 1997 to $1.00 per GJ by the year 2000.[a] The cut was implemented under a transitional price path adopted as an interim measure prior to applying the National Code to the pipeline from 1 January 2000 (Moran 1997, Farrant 1998).

a These tariffs are based on a load factor of 1.0 (and 98 percent probability of supply).

The Council's first tranche assessment

At the time of the Council's first tranche assessment – 30 June 1997 – it was apparent that the revised implementation timetable for the National Access Code – as proposed by the Prime Minister in December 1996 – could not be met. The slippage in the reform process caused the Council to reconsider what was necessary for jurisdictions to meet their first tranche commitments.

As most jurisdictions had agreed to the Prime Minister's revised timetable,[9] the Council considered this when assessing progress by jurisdictions in implementing the National Access Framework.[10]

The Council was also cognisant that the slippages in the reform program did not necessarily reflect a lack of genuine commitment to achieve reform. And it was aware that the GRIG was developing a new implementation timetable – expected to be endorsed in the IGA – with an expected implementation date of 30 June 1998.

The Council found that Tasmania and NSW were the only jurisdictions to have met their first tranche commitments in respect of the National Code.[11] It recommended that for other jurisdictions to satisfy their first tranche commitments, they would need to implement the Code in accordance with the timetable in the IGA.

In its supplementary assessment of 30 June 1998, the Council found that while the National Code had not commenced in accord with the IGA timetable, this was largely due to a delay in Commonwealth legislation necessary for the Code to become operational.[12] Accordingly, the Council considered that all States and Territories, with the exception of Western Australia,[13] had taken all reasonable measures to meet their commitments in relation to the National Gas Access Code.

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9 All jurisdictions other than Western Australia agreed to the proposals. Western Australia did not support the Prime Minister's specific proposals, expressing particular concern with the pace of deregulation and the proposed national transmission regulator.

10 While Western Australia did not agree to the proposals in the Prime Minister's letter, it indicated an intention to achieve consistency with the National Code by 2000. The Council recommended that for Western Australia to have satisfied its first tranche commitments in respect of gas reform, it must commit to adoption of the National Code and have a timetable for implementation.

11 NSW had already implemented a State-based regime closely modeled on the National Code. As noted previously, Tasmania's commitments under the National Code are yet to be activated.

12 The Commonwealth legislation was passed on 9 July 1998.

13 Western Australia was yet to enact legislation supporting the National Gas Access Code as at 30 June 1998, although the legislation had been introduced into State Parliament. The Western Australian Premier, in a letter to the Council, committed the Government to doing all in its power to ensure the legislation is passed before the end of September 1998. The Council relied on the assurance of the Western Australian Premier and recommended that a financial penalty not be imposed on Western Australia at this time.

The Council's roles under the National Code

The Council will play a number of roles under the National Code, including certification of state regimes, and several ongoing regulatory functions.

Certification of State regimes

Under the IGA, all jurisdictions have agreed to apply to the Council for certification of their access regimes as effective under Part IIIA of the TPA. Once a regime is certified as effective, the relevant services are immune from declaration under Part IIIA.

Following extensive public consultation in 1997, the Council found that, subject to a number of amendments – subsequently incorporated – the broad framework of the National Gas Pipelines Access Regime satisfies the TPA principles for an effective access regime. However, it noted a number of certification issues which remain to be tested. These will be considered by the Council in the context of the certification applications by each jurisdiction and will be subject to public consultation. The first certification application – from South Australia – was received by the Council in June 1998.

The central issues that the Council will examine include:

- whether state-based regulators and appeals bodies are independent and adequately resourced to fulfil their functions under the Code;
- whether transitional arrangements for phasing in the National Code are consistent with the principles agreed by jurisdictions in the IGA. In particular, the Council will need to be satisfied with the policy merit of any proposed derogations from the Code, and that the period of transition is no longer than necessary;
- whether a seamless process for access to interstate pipelines is in place; and

- whether Victoria's 'market carriage' framework for access is consistent with the CPA principles for an effective access regime.[14]

The issue of transitional arrangements is of particular significance. The Council accepts that transitional or 'phase-in' arrangements can provide a 'breathing space' for parties to adjust to the realities of competitive market conditions. Such arrangements might include:

- timetables to phase in the availability of access for different classes of customer; and/or
- arrangements to phase out cross-subsidies embedded in access tariffs.

The Council will seek to accommodate transitional arrangements where appropriate. That said, the Council will *not* recommend certification of access regimes which unnecessarily restrict access through the guise of transitional arrangements. For example, the Council cannot recommend certification in respect of services which are the subject of a total 'derogation' (exemption) from an access regime.

Where a pipeline service is derogated from a specific section of the Code, rather than the Code as a whole, the Council will need to examine whether the derogation alters the effectiveness of the Code as it applies to the pipeline service.

Coverage advisory body

The Council will play a number of ongoing regulatory roles under the National Code. Firstly, any person may seek coverage of a pipeline by the Code – or revocation of coverage – by applying to the Council. In considering coverage issues, the Council will conduct public consultation and convey its recommendation to the relevant State Minister.

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14 The Victorian access framework differs from the traditional 'contract carriage' framework to be applied in other jurisdictions. Under the Victorian model, gas users will pay gas haulage charges based on capacity and volume usage, rather for than contracted volumes. This issue will be considered in the context of Victoria's certification application.

In finalising the Code, the GRIG removed from immediate coverage certain pipelines where requests for access are considered unlikely, and coverage would therefore impose unnecessary compliance costs on the service provider. The Council supports this approach for certain dedicated pipelines, with potential access seekers remaining free to apply for coverage of the pipeline at any time in the future.

The Council understands the need for certainty as to the likely coverage of new infrastructure and will be available to advise investors on whether a proposed new pipeline would meet the coverage criteria. Alternatively, investors may seek coverage prior to construction of a new facility by adopting the Code's competitive tendering principles for new pipelines, or by submitting an access arrangement for the pipeline to the regulator.

On the revocation side, the Council expects that jurisdictions will have carefully considered the coverage criteria before determining the pipelines to be subject to immediate coverage – these are listed in Schedule A of the Code. The Council will examine whether the pipelines in Schedule A satisfy the coverage criteria when considering the certification applications by each jurisdiction. In the medium to longer term, however, revocation issues will naturally arise – resulting, for example, from technological innovation and changing market conditions.

Recommendations on cross-border pipelines

A related function conferred on the Council by the national legislation will be to recommend on the classification of cross-border pipelines (as transmission or distribution facilities) and the regulatory arrangements for cross-border distribution pipelines where agreement cannot be reached by jurisdictions. The Council's recommendation will apply unless the relevant Ministers unanimously agree to vary it.

B8.4 Removal of legislative and regulatory barriers

The Council noted in its 1996-97 Annual Report that the COAG deadline for removal of legislative and regulatory barriers to free and fair trade in gas had elapsed without completion of the task. The Council regards this as an ongoing commitment, and will take account of progress by jurisdictions in each of its future assessments.

During 1997-98, a number of developments occurred in this regard.

- In South Australia, a public review of the *Cooper Basin (Ratification) Act 1975* was undertaken. The Act provides concessions to the Cooper Basin Producers and exempts certain agreements from the operation of the TPA. The ACCC has previously identified the Act as a significant legislative barrier to free and fair trade in gas.

  The review, released on 28 May 1998, identified a number of restrictions on competition where the costs outweighed public benefits. The review noted that some of these restrictions arise because of the lack of a third party access regime to the Cooper Basin facilities, and because separate marketing by the Cooper Basin producers is effectively precluded. The review recommends that these restrictions be removed.

  The Council has entered dialogue with South Australia on an appropriate response to the Review and notes that the Government has sought further public comment.

- The Council also expressed concern during 1997-98 that regulatory barriers should not be used to unnecessarily delay proposals for new gas infrastructure – such as a second gas pipeline along the western seaboard.

  In this regard, the Premier of Western Australia has reaffirmed the State's commitment to seek expressions of interest for the construction of a second gas pipeline from the north-west of the State. The Government has informed the Council that it intends to initiate an open and competitive expression of interest process early in the September quarter of 1998. The Government has also assured the Council that there are no legislative impediments to the construction of a new pipeline, and that the Government does not intend to impose any such legislative impediments.

B8.5 Structural reform of gas utilities

Extensive structural reform of gas utilities has occurred in all jurisdictions since 1994 and continued to occur during 1997-98.

- In March 1998, Western Australia privatised the Dampier-Bunbury transmission pipeline, creating structural separation between gas transmission and distribution activities in that State. The Western Australian Government has also flagged the sale of the remainder of AlintaGas prior to the next election, due by early 2001. These developments follow the privatisation of several transmission pipelines nationally between 1994 and 1996, including the Moomba-Sydney pipeline (Commonwealth), Moomba-Adelaide pipeline (South Australia) and State Gas Pipeline (Queensland).
- In 1997-98, Victoria restructured its State-owned gas transmission and distribution activities in preparation for privatisation, expected to commence in the latter half of 1998. The new industry structure sees the disaggregation of the former Gascor into three stapled businesses, each comprising a gas distributor and a gas retailer, operating in non-aligned geographical areas. Transmission services have been split between a transmission business which owns and maintains existing pipelines, and an independent system operator.
- Rationally, privatisation and structural reform have resulted in full separation between all vertically integrated transmission and distribution activities in the public sector. And ring fencing between gas transmission and distribution activities in the private sector has been completed in most jurisdictions.[15]

15 The Council is aware of two exceptions – in South Australia and the Northern Territory. Firstly, South Australia's Riverland Pipeline System (transmission) is owned by Envestra Ltd and operated by Epic Energy Pty Ltd. Envestra Ltd also owns and operates the State's gas distribution networks. While in the Northern Territory, NT Gas Pty Ltd (AGL owned) operates both gas transmission services and gas distribution services to Darwin. The company's gas distribution role commenced in 1996.

- In NSW, AGL restructured its former gas distribution business in 1997 to ring-fence gas distribution from gas retailing business units. Structural separation between gas distribution and retailing functions has also occurred in Victoria and South Australia, and has commenced in Queensland. The Council notes that legislative implementation of the National Gas Access Regime will necessitate ring-fencing between gas pipeline businesses and gas retailing in all jurisdictions.
- All remaining State and Territory owned gas utilities have now been corporatised.

B8.6 The way ahead

The enactment of legislation giving effect to the National Gas Access Code in most jurisdictions by 30 June 1998 was a major step forward in national gas reform. But there is further work to be done. The Council's second tranche assessment in gas will address the following ongoing issues:

- continued effective implementation of the National Code;
- continued observance of industry structures conducive to effective competition – for example, the Council would be concerned by any moves towards structural re-aggregation of gas utilities; and
- reform of regulatory and legislative barriers to competition in upstream and retail gas markets.

The nature of upstream issues impacting on competition in natural gas markets is expected to be clarified by a Working Group currently working to ANZMEC and COAG. The Terms of Reference for the Working Group, which commenced operations in March 1998, identified the following issues:

- reform of tenement management policies to remove regulatory or policy barriers to new entrants and increase competition in exploration and development;
- access to upstream facilities in the light of Part IIIA of the TPA;

- contractual and marketing arrangements, including joint and/or separate marketing arrangements and take or pay contracts; and
- other issues which affect the ability of the natural gas industry to compete in a national energy market – such as fiscal issues, tariff barriers, taxes on business inputs and land access and environmental approval processes.

The Terms of Reference also require the Working Group to identify and develop options for reform. The Group, on which the Council is an observer, will deliver its report to ANZMEC and COAG by 31 December 1998.

The Working Group's program in the period to 30 June 1998 focused on the following issues:

- acreage management;
- access to upstream facilities; and
- joint marketing arrangements.

Given that extensive reform is underway in the downstream sector, the Council regards upstream reform as the remaining lynch-pin for delivering cheaper gas prices to consumers. In particular, the Council would regard legislative or regulatory barriers to competition in the upstream sector as significant assessment issues.

B9 WATER

B9.1 Background

Over $90 billion is presently invested in Australia's water infrastructure assets (in replacement cost terms) of which more than half is devoted to urban water services. Most water is used for irrigation purposes, with around 10 percent being required for household supply and waste water disposal.

Several factors have focussed attention on the need to improve efficiency of water delivery services. These include regional variations in water availability and consumption, the high costs associated with developing new water supplies, and the effect the health of the environment has on the quality and future availability of water to all users. Many of Australia's river systems are in deep crisis. Outbreaks of blue-green algae, excessive diversions of natural flows, increasing pollution and rising instream salinity are all taking their toll. Native fish populations, and wetlands and streams, have been affected. There are salinity problems in many farming areas such as those in the Murray-Darling Basin,[1] and water quality and reliability is at risk in some catchments. And the prices charged for water in most parts of Australia do not cover the costs of supply.

Recognising the need for action to halt the degradation of this natural resource, COAG agreed in February 1994 to develop a 'strategic framework' for the efficient and sustainable reform to address the problems of the Australian water industry. The package entails:

- pricing reform based on the principles of consumption-based pricing, full-cost recovery, and removal of cross-subsidies, with remaining subsidies made transparent;

1 The Murray-Darling Basin covers four states and one territory (Queensland, NSW, Victoria, South Australia and the ACT), supports over 20 cities, has a population of 3 million, and is Australia's most important agricultural region. The Basin produces annual agricultural output exceeding $10 billion or one-third of national rural output.

- implementation by States and Territories of comprehensive systems of water allocations or entitlements, including allocations for the environment as a legitimate user, backed by separation of water property rights from land title;
- by 1998, the structural separation of the roles of service provision from water resource management, standard setting and regulatory enforcement; adoption of two-part tariffs for urban water where cost-effective; and the introduction of arrangements for trading in water allocations or entitlements;
- by 2001, rural water charges reflecting full cost recovery (with subsidies made transparent), and the achievement wherever practicable of positive real rates of return on the written-down replacement costs of assets; and
- future investment in new schemes or extensions to existing schemes being undertaken only after appraisal indicates it is economically viable and ecologically sustainable.

COAG anticipated that implementation of the strategic framework would result in a restructuring of water tariffs, with cross-subsidies for water services being reduced or eliminated. COAG considered that the impact on consumers would be offset by cost reductions from more efficient service provision. In the case of rural water services, the strategic framework aims to generate the financial resources to maintain supply systems resulting in greater regional security for farmers. Similarly, systems of tradeable water entitlements are to be introduced to allow water to be reallocated to higher value uses subject to social, physical and environmental constraints. Water trading schemes will provide a financial benefit to farmers.

COAG recognised the importance of the health of water for country towns and cities alike, calling for reform to improve the environment and national water quality. Included in the agreement is a National Water Quality Management Strategy to sustain usage and the environment by protecting and enhancing water quality in a way that meets each jurisdiction's needs. The strategy contains guidelines to raise national drinking quality standards to 1987 World Health Organisation standards. Victoria, for example, will spend $1 billion to ensure that virtually all country towns have good clean water to international standards by 2001.

In April 1995, governments agreed to bring the water reform agenda within the ambit of the NCP process.

B9.2 Governments' commitments

Under the NCP Implementation Agreement, governments committed to progressing water reform as follows:

- for the second tranche of competition payments, the effective implementation of all COAG agreements on the strategic framework and future processes as endorsed at the February 1994 COAG meeting and embodied in the February 1995 *Report of the expert group on asset valuation methods and cost-recovery definitions*; and
- for the third tranche, full implementation and continued observance of all COAG agreements with regard to water.

Most reforms are required for the second tranche, and some (rural reforms) for the third tranche. Some reforms such as institutional reform, adoption of urban two-part tariffs, and implementation of trading arrangements for water allocations/entitlements, are to be implemented by the end of 1998.

B9.3 Progress to date

Work involving the Council

Efforts continue to focus on the requirements of policy and considering technical matters in relation to the proposed reforms.

In 1994, COAG requested that the Agricultural and Resource Management Council of Australia and New Zealand (ARMCANZ) oversee and report on the national water reform agenda.

In turn, ARMCANZ, through the Standing Committee on Agriculture and Resource Management (SCARM), appointed an intergovernmental task force to coordinate the COAG water reform program (the SCARM Task Force).

In July 1998, ARMCANZ agreed that the work of the SCARM Task Force be wound up by December 1998. In the interim, the work of the Task Force is to be incorporated into a planned approach under a Steering Group comprising the Chief Executives of the State water agencies to oversight the overall ARMCANZ water reform requirements. The Steering Group will be chaired by the Commonwealth Department of Primary Industries and Energy.

The Council has been represented on the SCARM Task Force for national water reform as a participating observer since March 1996. Work of the Taskforce during 1997-98 included:

- In June 1998, the Council wrote to Heads of Government to clarify the Council's interpretation of a number of technical matters contained in the 1994 Strategic Framework.

  This letter was in response to a series of questions that had been submitted to the Council by the SCARM Taskforce and individual jurisdictions. The Council drew on advice from the SCARM Taskforce in finalising its response to Heads of Government. Whilst the Council set out its views in an attachment to that letter, it is understood that some jurisdictions have specific concerns relating to the application of COAG water reforms and these would need to be the subject of bilateral discussions with the Council.

- the Task Force developed full cost recovery guidelines which have been endorsed by ARMCANZ Ministers as the basis of the Council's assessment.

  Full cost recovery requires the transparent disclosure and recovery of full economic costs by water supply agencies through pricing and transparent community service obligation payments. The full cost recovery guidelines develop a common framework for interpreting how to apply sections of the Strategic Framework and the report of the Expert Group dealing with asset valuation, the return on assets and asset renewals in the context of cost recovery and subsequent price determination.

  In summary, the guidelines transfer responsibility for full cost recovery to jurisdictional regulators who are required to ensure a

water business price between incremental costs[2] to ensure commercial viability and standalone costs[3] to avoid monopoly rents. Within this band, a water business should not recover more than operational, maintenance and administrative costs, externalities,[4] taxes (or tax equivalents), the interest costs on debt, and dividends (if any) set at a level that reflects commercial realities and simulates a competitive market outcome.[5]

ARMCANZ has recommended that COAG endorse the guidelines at its next meeting as the basis for the Council's assessment. The guidelines require COAG endorsement because the principles are a wider interpretation of the words contained in the Strategic Framework. Whilst COAG has yet to endorse the guidelines, the Council agrees in principle to use the guidelines to apply a consistent approach to determining whether full cost recovery requirements have been met in each jurisdiction.

- The Taskforce conducted voluntary reviews of jurisdictional progress that included representation from the NCC Secretariat.

  During 1997-98, the Task Force review team completed reviews for Victoria, NSW, South Australia, the Murray Darling Basin Commission and Tasmania.

2 With provision for future asset refurbishment/replacement made using an annuity approach to determine medium to long term cash requirements

3 Including provision for asset consumption and cost of capital, the latter calculated using a weighted average cost of capital.

4 ARMCANZ has defined externalities in this context as environmental and natural resource management costs attributable and incurred by a water business (albeit some of these will not be externalities as defined in the conventional economic sense). A further study is to be undertaken to determine the calculation of environmental costs for incorporation in cost recovery and asset valuation models.

5 Additionally, the level of revenue for a water business should be based on efficient resource pricing (preferably a two-part tariff) and efficient business costs incurred in providing a specific service. In determining prices, CSOs, contributed assets, the opening value of assets, externalities (including resource management costs), and tax equivalent regimes should be transparent.

In addition to its role on the Taskforce, the Council has also conducted the following activities:

- The Council released an information paper in December 1997 based on a consultancy undertaken by Tasman Asia Pacific on third party access and water, and whether water facilities are likely to meet the criteria for declaration under the National Access Regime.
- The Council is reviewing matters raised by the Australian Conservation Foundation (ACF) that Queensland is in breach of its national water reform commitments. A number of other environmental groups supported the ACF claims.

  The Council is examining progress with water reform and has been in discussion with the Queensland Government on several matters which include:

  - claims that the Queensland Government intends to initiate water investment projects (including new dam developments) prior to completing assessments of the ecological sustainability of the projects by way of Water Allocation and Management Plan (WAMP) studies;
  - whether projects subsidised under the Development Incentive Scheme will meet COAG's economic viability and ecological sustainability criteria; and
  - the possibility that Queensland will phase water pricing reforms beyond 2001.

The Council has recently visited Queensland and received extensive briefing on Queensland's approach to reform. All information available to the Council, including submissions on environmental issues, will be taken into account when the Council finalises the second tranche assessment in July 1999.

- The Council has recently commenced some water reform case studies for Victoria and NSW:
  - the initial Victorian project involves an examination of Melbourne's 1998 price reforms against the commitments.

- for NSW, the project will initially examine the pricing structures of Sydney Water Corporation and Hunter Water Corporation against the commitments.

The projects will reinforce key elements of the water agreements, identify areas that may need to be reviewed by all governments, and provide certainty in the Council's methods for assessing water reform. The projects will enable the Council to examine those elements of the water reform package that have been significantly developed or implemented against the requirements for the second tranche assessment. Where both parties agree that the commitments are addressed, these will be considered as having met the second tranche assessment obligations and will be signed off by the Council.

Progress by jurisdictions in 1997-98

The scope of the reform package governments committed themselves to in 1994 is large, and the impact of water reform is wide reaching. Consequently there are many elements of the reform package still to be put into place. Nevertheless, jurisdictions have implemented some of the reforms contained in the water agreements. For example, during 1997-98 jurisdictions have undertaken several reforms in relation to water pricing and provision for the environment:

- The Victorian Government announced a major water pricing reform package for Melbourne from 1 January 1998 (Box 9.1).
- In Queensland, ten of the seventeen largest local councils have implemented two part tariffs for water resulting in 20 percent average reductions in water usage in the first year (Box 9.2).
- The NSW Government announced two water reform packages in August 1997 and April 1998 which target clean, healthy and productive water use by addressing issues of better balance in sharing water between water users and the environment (Box 9.3).

Box B9.1 Water pricing reforms in Victoria

The 1994 Strategic Framework agreement requires reform of water prices based on consumption, full-cost recovery, cross-subsidies between customers being reduced, and remaining subsidies made transparent. A key element of the pricing reforms is the introduction of two part tariffs for urban water services consisting of an access fee which covers the fixed costs of supplying the customer including maintenance and environmental costs, plus a volumetric fee based on usage to send signals to conserve water.

In October 1997, the Victorian Government announced a new tariff structure to apply in Melbourne from 1 January 1998. The reform package delivered an 18 percent reduction in water prices across Victoria. The key changes for Melbourne are:

- abolition of water and sewerage rates based on property valuations for all customers;
- introducing a two-part tariff consisting of a flat fixed fee for each property connected to the water or sewerage mains, and a water usage and sewage disposal charge;
- introducing a sewage disposal charge for business and other non-domestic customers;
- removal of the rate-based allowance for the non-domestic sector; and
- different prices to be charged by different retail businesses to reflect their separate costs more closely.

Concessions on the access fee are available to schools, hospitals and not-for-profit organisations transparently funded by the government. The Victorian Government also funds rebates on water and sewerage bills for pensioners and other low income groups as community service obligations.

- Also in NSW, IPART set a two-year price path for bulk water charges toward full cost recovery. Prices for bulk water will rise by 11 percent and 15 percent for regulated rivers, and 5 percent and 8 percent for unregulated rivers for 1998-99 and 1999-2000 respectively. Prices for groundwater related services will also rise by 12 percent and 7 percent in 1998-99 and 1999-2000. (IPART July 1998)

Furthermore, the NSW Government has announced a new bulk water business, 'State Water', will be created and ring-fenced within the NSW Department of Land and Water Conservation (DLWC), to formally separate service provision from resource management.

- On 1 January 1998, the Murray Darling Basin Commission (MDBC) commenced a trial interstate water trading project in the Mallee Region in NSW, Victoria and South Australia (Box 9.4)
- South Australia's Water Resources Act came into operation on 2 July 1997. The Act provides for a comprehensive system of transferable property rights for water allocations, provision for water for the environment, incorporation of the principles of ecologically sustainability and provision for devolving greater responsibility for water resource management to local communities; and
- Tasmania completed a major community consultation round in late 1997 as the initial phase of the development of new water management legislation expected by December 1998. The legislation is expected to address issues of water pricing and allocations, tradeable water rights, allocations of water for the environment, and increased user involvement in the management of irrigation schemes.

Box B9.2 Water pricing reforms in Queensland

Queensland is in the process of implementing two-part water tariffs by the seventeen largest local councils. The Queensland Government's timetable requires local councils under the *Local Government Act 1993* to assess the cost effectiveness of introducing two-part water tariffs by 31 December 1998, and implement them where cost effective by 30 June 2000.

Ten of the seventeen largest local councils have already implemented two part tariffs resulting in demand for water being reduced by 20 percent in the first year of full application. The remaining councils have tariffs that include a fixed component and excess use charge that, as long as the fixed component is not too large, can provide price signals similar to those under two-part tariffs. Queensland is also in the process of implementing guidelines for use by local councils and metropolitan bulk water businesses to identify and remove cross-subsidies and inefficient forms of price discrimination.

The State Government has made incentive grants available to any local council that adopts two-part tariffs. The Council believes those local councils that have implemented the tariffs should be congratulated for introducing a difficult reform ahead of the State Government's timetable.

Box B9.3 Water reforms for the environment in NSW

The Strategic Framework requires environmental reforms such as recognising the environment as a legitimate user of water, establishing entitlements for the environment as a priority, and improvements in water quality.

To better balance river health and use, the NSW Government introduced water reforms in 1997 and 1998 that target explicit sharing of water between the environment and consumption, and establish water quality objectives to provide certainty in water use rights and a

Box B9.3 …cont

better foundation for investment. The package also promotes community involvement in water management.

The NSW Government has released a stressed rivers assessment report which classifies all unregulated NSW rivers according to low, medium and high environmental stress. The Report aims to ensure that river health meets the needs of individual rivers and minimises the impact on the rural community.

The Healthy Rivers Commission (HRC) conducts public inquiries and reports to government on environmental requirements for coastal rivers, including long term river health objectives to balance the environmental, social and commercial goals for each river. The HRC has completed inquiries into the Williams River and the Hawkesbury Nepean river systems.

For all remaining rivers, NSW is in the process of setting interim rules and objectives. For regulated rivers, River Management Committees are developing environmental flow rules and water quality plans for each subcatchment for the next five years. Priority subcatchment plans covering stressed rivers, high conservation streams and rivers at risk of stress through activating sleeper water licenses are to be in place by 2000-01. An embargo on issuing new water licenses is also in place on regulated rivers in NSW.

In April 1998, rules were announced for seven key rivers which provide an increased share (within 10 percent) of average annual diversions for the environment. Some key targets for 1998-99 include increased opportunities for native fish breeding and migration, improving the frequency and success of bird breeding in wetland areas, suppressing algal blooms and exotic species, improving the health of in-stream ecology, and greater long term certainty of volumes and water quality for water users.

Box B9.4 Benefits of water trading

The Agreements require arrangements for water trading to be introduced. In the past, water rights were permanently attached to land and thus could not be traded or shifted. This prevented farmers from responding to new market opportunities and impeded rural productivity. As the water reforms are introduced, these problems can be overcome.

Governments are at various stages in introducing intrastate trading regimes. In those States where trading exists, the benefits are significant. For example, in Victoria the benefits of intrastate trade are estimated at about $50 million a year in additional agricultural output, mainly in horticulture and dairy.

Trading between states is also being introduced. On 1 January 1998, the Murray Darling Basin Commission (MDBC) commenced a trial interstate water trading project. Initially the trial is to be limited to the permanent sale and purchase of high security water by private diverters in the Mallee Region in NSW, Victoria and South Australia.

While early implementation problems are currently being ironed out, interstate trade has the potential to provide further significant benefits to the rural economy. For example, given the majority of NSW rivers are over-allocated, NSW farmers would benefit from trade with Victoria and South Australia if next season's water allocations were very low on the Murray.

The MDBC for 1993-94 found that average gross margins per megalitre ranged from about $100-$120 for soybeans and lucerne respectively, to over $1000 for winegrapes (ABARE 1994). More recently, Victoria estimated the gross margin for winegrapes at $6800 per hectare, with stonefruit at $10,200-$15,900 per hectare (Department of Natural Resources & Environment, AgStats, 1998). At present, more than 40 percent of irrigation water currently goes to low value pasture activities. It is clear that water transferred out of broad acre cropping and into winegrapes or stonefruit, for example, is going to boost overall rural profitability. There is not infinite scope for doing this of course. But the substantial increase in wine exports in recent years gives an indication of what can happen when scarce water is used in those irrigation industries which generate the highest returns.

B9.4 The task ahead

Water reform is an area that extends beyond competition policy matters to embrace social policy issues such as recognising the environment as a legitimate user of water. The Council has said that full implementation of the reform package could do more to benefit the broad community than any other single NCP measure. The Council therefore intends to give high priority in the second and third tranche assessments to the timely implementation of agreed water reforms.

The Council's letter of 19 June to Heads of Government has sought to highlight some of the most important issues confronting jurisdictions, and the Council, in the lead up to the second and third tranche assessments. The Council is under no illusions as to the magnitude of the task ahead. Effective implementation of the agreed water reforms will be one of the most difficult and complex considerations of the second tranche and subsequent assessments. However, it is also likely to be one of the largest reform areas with regard to the size of the payments.

The Council recognises there are no easy answers in water reform. As such, it will continue to work with jurisdictions individually and collectively in an effort to overcome any remaining obstacles in the water reform process in the time remaining prior to the assessment. The Council is also likely to address issues of concern to individual jurisdictions increasingly on a bilateral basis. In this regard, jurisdictions are encouraged to approach the Council to address State-specific concerns.

B10 ROAD TRANSPORT

B10.1 Background

Australia is heavily dependent on road transport services for moving people and goods. People rely on a safe and efficient road network to travel to and from work, and to visit people, shops and entertainment venues. Businesses obtain raw materials and transport finished products. On a per person basis, Australia's road network is one of the largest of all OECD countries (IRF 1996). Road transport services are particularly important for communities in country areas, many of which depend totally on road transport.

The regulatory framework governing road transport is set by each State and Territory and as a result there are varying regulations across Australia. Charging systems for road users bear little relation to the costs that users impose on the road network. There have also been concerns about the past safety record of some sections of the industry.

In 1991, Australian Heads of Government agreed to a program designed to address these deficiencies. Heads of Governments signed an agreement (directed at vehicles over 4.5 tonnes gross vehicle mass) intended to improve road safety and transport efficiency and reduce compliance and administration costs. This agreement, known as the Heavy Vehicles Agreement (HVA), sought to achieve, among other things, uniform national arrangements for vehicle roadworthiness and driver licensing, and vehicle charges which reflect the full cost of providing road transport services.

The Commonwealth *National Road Transport Commission Act* 1991 (NRTC Act) gave effect to the HVA and created the National Road Transport Commission (NRTC) to oversee the development and implementation of the reform program. The NRTC Act also established the Ministerial Council of Road Transport (MCRT) – the inter-jurisdictional body that manages the implementation of the specific reforms developed by the NRTC. The MCRT is a sub-group of the Australian Transport Council (ATC).

In May 1992, Heads of Governments signed the Light Vehicles Agreement (LVA), extending the objective of national uniformity in road regulation to all other road users. The Commonwealth amended the NRTC Act to give effect to the LVA.

To facilitate reform, the MCRT agreed in October 1992 that the NRTC should implement the HVA and LVA reforms progressively through six separate modules. These six modules cover:

- uniform heavy vehicle charges;
- uniform arrangements for transportation by road of dangerous goods;
- vehicle operation reforms covering national vehicle standards, roadworthiness, mass and loading laws, oversize and overmass vehicles, and road rules;
- a national heavy vehicle registration scheme;
- a national driver licensing scheme; and
- a consistent and equitable approach to compliance and enforcement with road transport laws.

The model established by Transport Ministers envisaged that governments would phase in the six reform modules using 'template' legislation. Under this process, the Commonwealth Government was to enact legislation to apply the agreed reforms in the ACT. Other State and Territory Governments were to apply the Commonwealth template 'by reference' in their own jurisdictions.

B10.2 Governments' commitments

In April 1995, governments brought the MCRT road transport reforms within the ambit of the NCP process. Governments did this because they recognised that full implementation of the HVA and LVA would boost national welfare and that reform would reduce the cost of road transport services. As an example, an NRTC research paper has estimated that the national benefit

arising from the COAG road transport reforms, if all are fully implemented, is about $450 million per year (NRTC 1996).

Transport Ministers have reiterated the importance of achieving the road transport reforms on a number of occasions. For example, in November 1996, the Ministers emphasised the importance of the period up to the NRTC's then legislative sunset of 15 January 1998 for achieving the major aims agreed by governments in 1991 and pledged their support for ongoing reform over this period (MCRT 1996).

In signing up to the NCP, all governments committed to the effective observance of road transport reforms by 1999 and to having fully implemented and continued to fully observe all COAG agreements with regard to road transport by 2001. Thus, the HVA and LVA together form the benchmark objectives against which the Council evaluates road reform progress under the NCP.

The effect of bringing the MCRT program within the NCP framework is to set an explicit timeframe for completion of road transport reforms. Pursuant to the NCP framework, all governments will need to show substantial progress in road transport reforms by 1999, and full implementation and continuing observance of the reforms by no later than 2001.

Nonetheless, the 1995 NCP agreements did not link specific reform outcomes to the three tranches of NCP payments. Because of this, in the period leading to the first assessment of governments' reform progress in June 1997, the Council sought to define the NCP objective of effective observance of road transport reform. Following consultation with all governments, the Council concluded that effective implementation of road transport reforms over the three assessment tranches should involve the development and implementation of the reforms and timelines agreed to by the MCRT at its February 1997 meeting.

B10.3 Progress to date

Reform progress prior to the first tranche assessment

By the end of June 1997 – the time of the Council's first assessment – jurisdictions had implemented only the reform module, relating to standard heavy vehicle registration processes and charges.[1] In most instances, they implemented it later than originally envisaged. In addition, the NRTC's work to develop the remaining reform modules was not proceeding as quickly as expected.

In February 1997, the MCRT moved away from the template approach and agreed that jurisdictions could implement the reform modules, once approved by the MCRT, without waiting for the Commonwealth template. This new arrangement focused on national *consistency,* rather than national *uniformity.*

In addition to the new national implementation strategy, the MCRT also agreed to specified timeframes and processes for the national implementation of the remaining reform modules. The MCRT's objective was to overcome the delays in implementing agreed reforms. The key elements of the February 1997 package were:

- uniform arrangements for the transport of dangerous goods implemented by all jurisdictions no later than 1 January 1998;
- the Australian road rules regulations (part of the vehicle operations module) implemented no later than September 1998;
- a national driver licensing scheme implemented no later than 1 July 1998; and
- the remaining modules implemented no later than 1 July 1998 without waiting for the enactment of Commonwealth legislation, provided that the result is uniform and consistent with laws across jurisdictions.

1 The NRTC's first determination for heavy vehicle charges proposed that the existing concessions for primary producers not be maintained. However, most jurisdictions have maintained at least part of their existing concession regimes. The NRTC indicated that it would develop a second heavy vehicle charges determination in the second half of 1998.

The slippage in the reform program meant that the Council needed to consider what jurisdictions should do to meet COAG's 'effective observance of road transport reforms' criterion for the first tranche payments. After consulting with all governments, the Council considered that an appropriate benchmark would be implementation of the first reform module relating to heavy vehicle charging and commitment to link the implementation of the other road transport reforms according to the February 1997 MCRT timetable to future NCP payments.

However, the Council recognised that:

- the MCRT road transport reform agenda had not been endorsed by COAG, and any change to the program agreed by COAG would supersede the current arrangement;
- future changes to the reform program agreed by the MCRT may also amend the assessment framework; and
- the Commonwealth's legislative program may constrain implementation by the Australian Capital Territory.

In the course of the first tranche assessment, all jurisdictions gave an in principle commitment to this assessment framework, although they noted that it was still to receive COAG endorsement. The Council proceeded with its first tranche assessment on this basis, concluding that all States and Territories had satisfied the first tranche assessment criteria.

Progress since 1 July 1997

There has been some progress in the important area of mass limits. At its April 1998 meeting, the ATC agreed to increase general axle mass limits for trucks and buses fitted with 'road friendly' suspensions, subject to the Commonwealth agreeing to provide sufficient additional funding for upgrading bridges (NRTC 1998a).[2] According to the NRTC, increasing mass limits would reduce transport costs by between $260 and $300 million per year, even taking bridge upgrade and other costs into account. These savings would flow through the economy.

2 The Commonwealth is to report back on funding for bridge upgrading to the next ATC meeting later this year.

In addition, the NRTC is currently in the process of updating charges for heavy vehicles, as it is required to do under the HVA. It made its First Determination on heavy vehicle charges in 1992. The NRTC is currently seeking comments from interested parties on its work towards its Second Determination. It is unlikely that these changes will occur before July 1999. (NRTC 1998b)

On the whole, however, the slippage in implementing the road transport reform program has continued since the Council's June 1997 assessment.

In November 1997, the MCRT again deferred implementation dates for several reforms. In April 1998, the ATC acknowledged that even the November 1997 timelines would not be achieved, although there is evidence to suggest that some jurisdictions are implementing some of the reforms according to the November 1997 timeframe.[3]

Against the background of this increasing delay, the Council approached Heads of Government asking that they develop a firm reform program and implementation timetable. In the Council's view, this would increase the prospect that road transport reforms proceed on time. It would also provide a suitable framework against which jurisdictions' progress could be assessed for NCP payments. There has been broad acceptance by the States, Territories and Commonwealth of the need for a program endorsed by Heads of Government.

Amendments to the NRTC Act, arising from the 1996 review of that organisation, will have the effect of changing the reform arrangements set out in the HVA and LVA. The Council recognises that these amendments, as a result, will influence the assessment framework for road transport reform. The amendments include:

- merging the MCRT back into the ATC, the inter-jurisdictional body responsible for all transport matters;
- removing the need for template legislation to implement reforms; and

3 For example, NSW and Queensland have indicated that some of the reforms are already implemented in their jurisdictions or will be implemented by the dates set at the November 1997 MCRT meeting.

- establishing a formal timeframe for achieving nationally uniform or consistent integrated road transport law.

The amended NRTC Act is expected to be proclaimed when the Heads of all State, Territory and Commonwealth Governments have signed the amendments to the Heavy and Light Vehicle Agreements. It is anticipated this will occur before the end of 1998.

The Council also sought governments' agreement to a closer working arrangement between the Council and the NRTC. The Council's objective is twofold – first to ensure that it has access to up-to-date information on reform progress and, second, to ensure that it is involved, at least as an observer, in developing the road reform assessment framework. The Council has worked in this way in other related reform areas, for example, through the Gas Reform Implementation Group and the COAG Taskforce on Water Reform.

B10.4 The task ahead

In view of the heavy dependence of Australians on an efficient road transport system, the Council has set itself the objective of using the NCP process to encourage governments to implement reform as quickly as can reasonably be expected.

The Council's immediate priority is to encourage Heads of Government to reach agreement on a road transport reform package and implementation timetable consistent with the 1991 and 1992 vision and the NCP program. The formal timeframe for achieving nationally uniform or consistent integrated road transport law, set out in the NCP program and in the amendments to the NRTC Act and the HVA and LVA, should provide guidance to governments in determining the specific reforms and appropriate implementation timelines.

In addition, the NRTC will need to develop appropriate 'performance indicators' consistent with its role of advising governments on how effectively they have implemented the road reform program.

Should COAG not reach agreement on a road reform program prior to the Council's 1999 NCP assessment, the Council will need to determine its own framework for assessing whether the States and Territories have met the conditions for NCP payments.

There are a number of options available to the Council in determining an assessment framework in the absence of COAG agreement. The outcomes envisaged by COAG in 1991 and 1992 represent an overall target, noting that refinements to the assessment framework will be necessary given the delays recognised by the MCRT, most recently on 14 November 1997.

The Council will also need access to expert judgments on jurisdictions' performance against suitable indicators, using information made available by governments, national institutions such as the NRTC, and industry views on progress by governments with the road transport reforms. In particular, the Council will be looking for 'on the ground' implementation of the agreed reform package.

B11 RAIL

B11.1 Background

The national rail industry has evolved in an uncoordinated and fragmented manner, reacting to state priorities, rather than national objectives such as a uniform approach to infrastructure development, technology investment and safety management.

While the NCP agreements included specific arrangements to cover reforms in targeted industries such as gas, electricity and road transport, these agreements did not contain any specific reforms for the rail industry. Without a national rail reform agreement, the business community, in its attempts to gain improved service quality and lower prices, has had to rely on the general provisions of the CPA and, in particular, the National Access Regime included in Part IIIA of the Trade Practices Act (TPA).

To date, these provisions in the TPA have been used by the rail industry more than other industries. Three rail customers have made eight applications for declaration of certain segments of state rail infrastructure.

However, while this mechanism has assisted negotiation of access on particular intra-state line sections, it has not achieved national reform. This is probably due to the objectives of Part IIIA and its process requirements. Part IIIA provisions were designed to assist customers gain access to services denied them or offered on uncompetitive terms and conditions. The provisions require that each declaration process relate to only one infrastructure owner. Therefore, declaration of track that crossed state boundaries would require as many processes as the number of track owners involved. It would also require that each state agree to declare its own infrastructure. Failing such agreement, it would require a positive appeal outcome from the Australian Competition Tribunal on each declaration.

While the certification provisions encourage compatibility of access regimes across states, only two states – NSW and Queensland – have lodged regimes covering their rail line networks.

The need for less circuitous national reform was highlighted in submissions to the Council's rail service applications for declaration. Rail operators illustrated the costs of meeting differing safety standards and access conditions across states. For instance, operators argued that while a national agreement on safety arrangements was in place, it was not fully effective because the states imposed significant additional requirements. To conform to these requirements rail operators had to develop separate applications covering the differing technologies and practices used in each state. Further evidence regarding the fragmentation of the rail industry was also highlighted in the many submissions to the recently completed inquiry into the Role of Rail in the National Transport Network.

> Meeting the requirements of a multitude of regulatory regimes can impose substantial financial and administrative costs on rail operators. For example NR [National Rail Corporation] noted that the costs of safety regulation alone for trains operating across three jurisdictions – based on a different formula in each state – cost the company more than $140 000 (1997 prices) per annum. Often these regulatory requirements are inconsistent, or worse, contradictory, leading to multiplicity in compliance costs and constraints on operating ability. (Parliament of the Commonwealth of Australia HRSCCTMR 1998, 89)

B11.2 Progress to date

State and Commonwealth Transport Ministers have confirmed the need for a national approach to reform. When meeting in late 1997, they concluded that:

> Our interstate rail system has been managed as a discrete set of State based rail systems. This is no longer acceptable. We need a vigorous interstate rail system that supports port competition and is genuinely competitive with road transport and domestic shipping industries. (ATC 1997)

On 10 September 1997, Transport Ministers agreed to a series of reforms to apply to track that joined the State capitals and their ports, with connecting lines to the major regional ports of Whyalla, Port Kembla, Newcastle and Westernport. These reforms should reduce the cost of transporting freight by rail by increasing train speeds and tonnages, as well as standardising practices, technologies, and access conditions.

Box B11.1 Agreement on interstate rail reform (10 September 1997)

1. The parties agree:

(a) that there is a clear and urgent need to reform interstate rail;

(b) that the most urgent need is for the interstate rail network to be operated as a single network, including for investment and access;

(c) to the commencement of single management of the interstate track from Albury and Broken Hill to Kalgoorlie by 1 July 1998;

(d) to develop a plan for the extension of this network to Perth;

(e) to develop a plan for the provision of a dedicated freight track(s) through Sydney; and

(f) to settle the means of achieving these by 14 November 1997.

2. The parties will immediately commence an investigation of all relevant matters, including:

(a) the provision of track access as a single service to rail operators;

(b) the financial arrangements for investment in, and maintenance of, rail track;

(c) competitive neutrality issues affecting road, rail and sea transport; and

(d) the organisational arrangements required to achieve these objectives and harmonisation of technical standards.

3. The aim of these rail reforms will be to maximise benefits to the transport industry including inter and intrastate rail operators, and the community.

All States agreed to meet the following targets within 5 years:

- less than 2 percent of track subject to temporary speed restrictions;
- at axle loads up to 21 tonnes, a maximum speed of 115kph and an average speed of 80kph;
- at axle loads between 21 and 25 tonnes a maximum speed of 80kph and average speed of 60kph; and
- train lengths of 1800m on the east-west corridor and 1500m on the north-south corridor.

They also agreed in the longer term to achieve:

- at axle loads up to 21 tonnes, a maximum speed of 125kph and an average speed of 100kph, and at axle loads between 21 and 25 tonnes a maximum speed of 100kph and an average speed of 80kph; and
- increased clearances to allow double stacking.

The Commonwealth agreed to make available $250 million over four years on condition that satisfactory access arrangements and plans for investment and harmonisation of regulatory and operational requirements are in place. The States will also be making an investment commitment to achieve these objectives.

Ministers also decided to commission Maunsell Pty. Ltd to report on the Rail Standards and Operational Requirements in place on the designated network and recommend how these arrangements should change. The report was completed in February 1998. It confirmed the fragmentary nature of the national network. For instance:

> The interstate network has three differing forms of safe working systems involving seven types of systems, and with variations in each state, some twenty systems of safe working. Associated rules governing track work, signal failure, train failure and incidents as well as periods of certification vary between each. These variations did not cause concern when trains operated only within state boundaries. (Maunsell 1998, 6)

While this assessment is damning, the report was optimistic that solutions could be implemented relatively quickly and at minimal cost:

> An opportunity exists to establish a common standard for an enhanced communications based system before major investments are committed to differing systems. Much of the interstate, and intrastate, single track network services similar operator customers and has comparable traffic densities. A task specification for a safe working system will have more common ground than differences. There is an opportunity to define one communications based system that can be economically justified to meet the needs of the whole of the network. (Maunsell 1998, 16)

The report recommended a range of improvements to achieve the goals of the agreements and a task force was established to implement these recommendations. While some recommendations could be implemented quite quickly, others required substantial preparatory work or capital, and would therefore require a longer gestation period. (Maunsell 1998, xiii-xiv)

Improvements that can be implemented at a modest cost within 12 months are:

- extending the use of management information systems such as RAMS through the interstate network;
- introducing performance based standards for braking distances/train size;
- identifying priority crossing loop and gradient improvements;
- introducing a standard formula for axle load/speed rules;
- determining priority areas for improvement in track axle load/speed restrictions;
- expanding the Rollingstock Manual to include mechanical performance;
- obtaining agreement on the Rollingstock Manual and combine with RAC standard RSS001;
- identifying a potential corridor for double stack operation Melbourne-Brisbane;
- establishing the best return for incremental improvements in clearances;

- streamlining the accreditation process for interstate operators; and
- introducing a consistent pricing policy and insurance requirements.

Improvements that would require significant capital expenditure are:

- crossing loop and gradients improvements;
- improving areas with axle load/speed restrictions;
- providing 4.3 metre (trailer rail) clearance for the Melbourne-Sydney-Brisbane and Sydney-Parkes;
- providing double stack clearances for the Melbourne-Adelaide;
- extending double stack clearance through the interstate network; and
- improving train path capacity for high demand paths.

Complex improvements that are likely to take longer than 12 months to implement include:

- reducing the overlaps in occupational health and safety legislation and rail safety legislation;
- developing and implementing a uniform safeworking rule book (emergency working, trackwork rules);
- agreeing on and implementing compatibility standards for radio voice and data systems; and
- developing a national policy for clearances on priority rail corridors.

At the 14 November meeting of Transport Ministers, the Commonwealth agreed to establish a corporation that would be charged with providing a 'one stop shop' for national rail operators. For their part, the States agreed to enter into negotiations with the corporation to achieve arrangements over state track that would allow the corporation to operate as a 'one stop shop' over a national network.

Box B11.2 Agreement on Australian Rail Track Corporation (Excerpt 14 November 1997)

7.1 The Company will:

(a) own and manage the Commonwealth owned interstate track and related assets;

(b) manage, through a lease contract, Victoria's interstate track and related assets;

(c) manage, through a lease contract, any other interstate track and related assets agreed between the Parties;

(d) provide access to the track it manages under (a), (b) and (c);

(e) provide access for interstate operations by accredited rail operators to other track, through agreements with track owners;

(f) manage track maintenance and construction, train pathing, scheduling, timetabling and train control on track it controls under (a), (b) and (c);

(g) develop arrangements for the efficient interaction of interstate and intrastate track and traffic on track it controls under (a), (b) and (c);

(h) manage an interstate track investment program with commercial funding and grants from the Parties, in consultation with rail operators and track owners; and

(i) develop and promote uniform safeworking, technical and operating requirements, and work with other track owners to achieve this.

Box B11.2 …cont

7.2 The Parties agree that the company will have an exclusive right to sell access for interstate operations on the interstate network for the life of this Agreement. This may be achieved through its management of interstate track or by agreement with the track owner, consistent with the application of Commonwealth and State law. The principles underlying this right are that the company:

(a) will have access to uncommitted capacity on the interstate network;

(b) may negotiate with and between track owners and rail operators over the allocation of train paths (including for variations to the existing allocations of train paths) with the object of promoting efficiency in interstate rail operations;

(c) will have access to capacity reserved by a Party or Parties and their track owners for interstate rail on policy grounds; and

(d) will have access to capacity reserved on market terms and conditions (eg through the acquisition of options)

The agreements aimed to tackle many elements that have impaired the competitiveness of national rail transport relative to other modes of transport. These rail reforms are not part of the NCP package and, therefore, are not included in the Council's assessments and recommendations on NCP payments. However, the Council would like to note its support for reform efforts in this area. The Council would also note, given the potential for substitution between road and rail, the importance of the rail reform program progressing in step with that of road reform.

The commitments of State and Commonwealth Ministers have also enhanced reforms outside this process. For instance, a number of States have taken steps to give their rail service providers a more commercial focus in anticipation of increasing competition.

In train operations, increased competition should come from the government and private operators. A number of new operators have already entered the industry, including Specialized Container Transport and West Coast Railway. However, some states still appear to be constraining the extent of this competition. Entry to some markets has proved particularly difficult for National Rail Corporation (NR). Under its Memorandum of Association, NR needs each state to enact legislation and explicitly approve its carriage of freight within its state boundaries. Obtaining enactment of the necessary legislation and approvals from all states has still not been achieved. NR advises the following.

- In NSW, legislation in place. Explicit ministerial approval given on 6 February 1998. Before this date, NR was only allowed to carry non-bulk freight (and so was excluded from carrying coal).
- Victorian legislation is also in place. Explicit Ministerial approval given at the end of 1996.
- In Queensland, due to the change of gauge at Brisbane, NR is unable to carry intrastate freight.
- In 1997 the Western Australian Cabinet approved the necessary draft legislation together with legislation to cover an access regime for all operators on the Western Australian network. The legislation has been delayed as details of the access regime are still being developed with the assistance of the Council and the legislation will be in place late 1998 at best.
- As regards South Australia, in February 1996, NR unsuccessfully requested that the South Australian Government pass the necessary legislation. Legislation to support an access regime was enacted in mid 1997, but did not include the necessary provisions.

NR believes that it has lost substantial business in all State markets where it was not able to participate. Potential customers have confirmed to the Council that the participation of NR in their markets would no doubt have influenced prices and service quality. The Council is encouraged by the actions of NSW and Victoria as the maximum benefits from competition in rail transport services will be achieved when all potential suppliers of rail transport are given an equal opportunity to offer their services to customers.

B12 ACCESS TO INFRASTRUCTURE

B12.1 Background

Sectors such as transport, energy and communications, are major users of resources in their own right and the means by which consumer products and inputs are provided to other businesses. The efficiency and competitiveness of these key sectors thus affects the performance of the whole Australian economy.

These sectors largely depend on major infrastructure facilities — such as ports, aerodromes, roads, rail networks, gas pipelines, electricity grids, telephone lines, and radio communications networks — to provide their services and to help deliver their products. These facilities often tend to be natural monopolies, which means that it would be uneconomic for another business to build and operate facilities to provide a competing service.

In many of these industries, the facilities have been built and operated by public utilities. For example, electricity grids and railway lines traditionally have been built, owned and operated by government-owned bodies. Further, government-owned bodies have tended to provide infrastructure related services, such as supplying electricity and freight forwarding services, directly to the consumer. They have been, in effect, both monopoly infrastructure owners and monopoly service providers.

However, while the infrastructure facilities themselves may be, by necessity, monopolies, the supply of products that use these facilities need not be. For example, while it may not be economically feasible to build two rail networks in the one region, it may be possible to allow two or more different businesses to operate trains on the one network, in competition with each other (and with other forms of transport).

Unfortunately, when one body both owns the monopoly infrastructure and provides the related services, it can be difficult for other businesses to use, or gain access to, the services of natural monopoly infrastructure. Integrated

monopoly service providers have had little incentive to provide their competitors with access to their services, at least not on reasonable terms and conditions. Even where this conflict does not exist, the bargaining power of a business negotiating access with a monopoly service provider is weak.

As a consequence, the use of the infrastructure may be less efficient, and competition in other related markets discouraged. This means the prices paid by the consumer for the products and services in the related markets are likely to remain unnecessarily high.

To specifically address this problem, governments have been introducing, and continue to introduce, legislative access regimes. During the first half of the 1990s, governments introduced access regimes for telecommunications and certain gas pipelines, and also commenced work on national access arrangements for gas pipelines and electricity grids. These regimes set conditions of access, or specify processes for determining conditions of access, in relation to the relevant infrastructure services.

In addition in April 1995, governments agreed to establish national arrangements to provide access to monopolistic infrastructure services not already subject to other effective access regimes.

B12.2 Governments' commitments

Under clause 6 of the NCP Competition Principles Agreement (CPA), governments agreed:

- that the Commonwealth Government establish a National access regime for services provided by means of significant infrastructure facilities;
- to the conditions under which access should be provided under the National regime;
- that the National regime should not cover a service provided by an infrastructure facility already covered by an 'effective' State or Territory regime, unless substantial difficulties arise from the

infrastructure facility being situated in more than one jurisdiction, or its influence outside the jurisdiction; and

- to principles which State or Territory access regimes should incorporate to be deemed effective.

In essence then, governments agreed that the National regime should apply except if there is another regime, which provides effective access to the services in question. The agreement does not require that States and Territories introduce specific access regimes, nor that any regimes they do introduce must be effective under the clause 6 principles. However, for their specific access regimes to be the sole regime under which access can be obtained, the regimes must meet the effectiveness criteria.

B12.3 Progress to date

The *Competition Policy Reform Act 1995* introduced a Part IIIA into the TPA, providing for the National access regime.

Part IIIA provides three routes – declaration, undertaking and certification of access regimes – through which businesses can gain access to nationally significant infrastructure services (see Box B12.1).

The Council is responsible for assessing applications seeking declaration of a service and certification of access regimes.

Box B12.1 Routes to access significant infrastructure

Business can get access to national significant infrastructure services through:

- the declaration route, where businesses can apply through the Council to have an infrastructure service 'declared' and then, if the relevant Minister declares the service, enter into negotiation with the infrastructure operator, supported by legally binding arbitration, to determine the terms and conditions of access;
- the undertakings route, where an infrastructure operator has made a voluntary access undertaking to the Australian Competition and Consumer Commission (ACCC), and once the ACCC has accepted that undertaking, businesses can get access to the infrastructure services on the terms and conditions set out in the undertaking; and
- the provisions of other regimes, such as specific State or Territory regimes.

If an infrastructure service is already subject to an approved undertaking or an effective access regime, it cannot be declared under the National regime. Part IIIA provides for State or Territory governments to apply to the Council to have an access regime certified as effective in relation to a particular service. Decisions on declaration and certification can be appealed to the Australian Competition Tribunal within 21 days.

Overview of declaration activities

During 1997-98, the Council received five applications from one business seeking declaration of infrastructure facilities. Decisions have been announced on all those applications. The Council recommended for declaration in one case and against in the remaining four. The declaration applications made under the regime so far are briefly summarised in Box B12.2 and applications received during 1997-98 are discussed in Section B12.4.

Box B12.2 Declaration applications and their outcomes

To date, the Council has received a total of sixteen applications to have certain services declared. One application was withdrawn before the Council made its recommendation because the parties concerned reached an agreement. Of the remaining fifteen applications, the Council considered that seven satisfied the criteria set out in section 44G of the TPA and accordingly recommended those services be declared. The Council considered that eight applications did not satisfy the necessary criteria and recommended those services not be declared.

In response to the Council's seven recommendations to declare, the relevant Ministers decided to declare four services but to not declare the other three. All the Council's eight recommendations to not declare were accepted. Accordingly, of the fifteen applications considered by the Council, there were four decisions to declare, and eleven decisions not to declare, the services defined in the applications.

Eleven of those fifteen decisions were appealed to the Australian Competition Tribunal. One appeal was unsuccessful, six were withdrawn when the relevant parties reached commercial access agreements or other arrangements, and four have yet to be finalised.

A declaration application usually takes the Council sixteen weeks to consider. Of that sixteen weeks, six weeks is for public consultation and for interested parties to prepare submissions. The Council uses the remaining ten weeks to assess the application, relying on submissions received and other relevant information, and prepare its recommendation.

Some applicants have questioned the length of time it takes to finalise a declaration application and criticised the delays that arise when a decision is appealed. These occur for a number of reasons. One is the rigorous process adopted by the Council to ensure its recommendations are based on sound legal and economic analysis. Another is the sixty days the designated Minister has to reach his or her decision under Part IIIA. Finally, there is the delay generated by the length of time it takes appeals to be heard.

These delays, therefore, are a combination of the declaration process under Part IIIA and the desire by parties to test the new law.

However, in some cases, the threat of imminent declaration appears to have encouraged progress in access negotiations or the preparation of access regimes. For example:

- in one case, a private agreement was reached between the parties before the Council had finalised its consideration of the application;
- in two cases, appeals against Ministers' decisions were withdrawn after the applicant and the relevant service providers reached private access arrangements (see below);
- the possibility that some of its rail network might be declared under the National regime may have influenced the development of the NSW rail access regime and may have encouraged Queensland to develop its rail access regime (recently submitted to the Council for certification);[1] and
- the Treasurer's decision to declare certain services at Sydney airport, while still under appeal, may have increased the pace of reform here (see Box B12.4).

Specialized Container Transport (SCT), the applicant seeking access to rail services in NSW and WA, has advised the Council that the declaration process assisted them in their commercial negotiations. According to SCT, it:

> has benefited from the two NCC recommendations in respect of declarations concerning rail services provided by RAC [Rail Access

1 Likewise Western Australia is in the process of developing its rail access regime.

> Corporation] (in NSW) and Westrail (in WA). Although in each case the relevant Premiers have refused to declare the services in question, SCT was able to secure long term agreements from both Westrail and RAC following the commencement of appeals against the Premiers' decisions. (SCT 1998)

Overview of certification activities

In addition to declaration, several governments have developed their own access regimes dealing with specific infrastructure, such as gas pipelines, shipping channels, telecommunications services and rail networks. State governments have made five applications to the Council to have their regimes 'certified' as effective under the national regime. To date, two regimes have been certified and three certification assessment processes are underway. Two of these have just begun the process.

In conjunction with this, there have been national developments in respect of access to gas pipeline services and electricity network services.

On 7 November 1997, all governments signed the National Gas Pipelines Access Code. The legislation to implement the regime in each State and Territory has been introduced through what is called an application of laws approach. Under the agreement, South Australia enacts legislation containing all the critical elements of the National Code. The remaining States and Territories then enact their own natural gas access regime legislation by reference to the South Australian legislation.[2] In addition, each State and Territory's access legislation contains jurisdiction-specific matters such as the identity of regulatory bodies.

Under the agreement governments agreed to take all reasonable measures to ensure their legislation was enacted, proclaimed and commenced by 30 June 1998. While most States and Territories had passed their legislation by 30 June, proclamation was delayed partly due to delays in the passage of Commonwealth enabling legislation.[3] All States and Territories are

2 Western Australia intends to introduce template legislation that is essentially identical to the South Australian legislation.

3 Legislation was introduced to the Western Australian parliament by 30 June and is expected to be passed before the end of September 1998. The Commonwealth legislation was passed on 9 July 1998.

expected to seek certification of their regimes from the Council by the end of 1998 – with the South Australian application lodged in June 1998.

In respect of electricity, the national access regime will be enacted through undertakings being offered to the ACCC.

The developments in the electricity and gas sectors are discussed in more detail in Chapters B7 and B8.

Early in the development of Part IIIA and the development of other access regimes, there was some concern that increased focus on access would stifle investment in infrastructure. This has not occurred. At the same time as these developments in access, there has been significant ongoing investment in infrastructure in Australia, and the sale prices of affected assets appear to have held up. Investments of up to $40 billion in infrastructure assets are currently proposed (Parer 1998). Similarly, the privatisation of significant gas infrastructure has attracted considerable interest. For example, in the first half of 1998 the Dampier to Bunbury natural gas pipeline fetched a total of $2.4 billion. And in 1996, the sale of Victorian electricity generation, transmission and distribution businesses realised a total of around $23 billion, substantially exceeding expectations (VDTF 1997). These high sales prices in part reflect US tax and regulatory arrangements, which increase the value of foreign utility purchases to US utilities. Nevertheless, they (and further mooted investment) suggest that the prospect of access to previously locked-up markets has not discouraged investment in infrastructure, and that access arrangements are not causing undue uncertainty for infrastructure owners.

Overall, these developments in access indicate some of the benefits of greater competition and more efficient use of Australia's infrastructure.

B12.4 Council recommendations on declaration

This section provides details of the handling of specific applications under the declaration provisions of Part IIIA of the Trade Practices Act (TPA).

To date, there has been a strong interest in declaration with a large number of inquiries and a number of important applications. Applications have covered different types of services, including electronic payments systems, the use of facilities for offering cargo-related services at airports, and parts of rail networks. Most interest has been in the services offered by large infrastructure facilities. There also has been a variety of applicants — including a student union, and small and big businesses.

The applications received to date are:

- an application by the Australian Union of Students for a payroll deduction service provided by a Commonwealth Department;
- an application by Futuris Corporation Ltd for access to a high-pressure gas distribution system in Western Australia;
- applications by Australian Cargo Terminal Operators Pty Ltd for access to particular airport services at both Melbourne and Sydney international airports;
- an application by SCT for access to rail services provided by the NSW rail network;
- an application by Carpenteria Transport Pty Ltd for access to rail services provided by the Queensland rail network;
- an application by the NSW Minerals Council for access to rail services provided by the NSW rail network in the Hunter Valley; and
- applications by SCT for access to rail services provided by the Western Australia rail network.

In processing applications for declaration, the Council is required to make assessments against criteria set out in Part IIIA. These are set out in Box

B12.3. The Council usually undertakes public consultation processes. It advertises the application, seeks submissions, sometimes releases draft recommendations, and provides comprehensive analytical support to its recommendations. The Council's processes in relation to each application for declaration, considered during 1997-98, are summarised below as are the Council's reasons and recommendations. Previous applications considered by the Council and the Council's recommendations plus the relevant governments' decisions were summarised in previous annual reports. This information has been updated in this report where there have been relevant developments during 1997-98.

Box B12.3 Criteria for declaration of access

- Access would need to promote competition in an upstream or downstream market. For example, for access to an electricity transmission grid to be granted it would need to enhance competition in a market like electricity generation or retailing.
- It would need to be uneconomical to develop another facility to provide the service. It could be argued, for example, that an electricity grid satisfies this criterion because it would be a waste of resources to undertake the large investment needed to build a new grid when the subsequent use of both grids would be insufficient for them both to be viable.
- The facility to which access is sought would need to be of national significance, having regard to its size, its importance to Constitutional trade or commerce, or its importance to the national economy. This criterion puts relatively insignificant facilities outside the declaration framework.
- Access must not be associated with undue risk to health or safety.
- The service for which an application for declaration is made must not already be the subject of an effective access regime.
- Access must not be contrary to the public interest. Public interest considerations include economic efficiency and other objectives such as jobs, community service obligations, regional development, environmental matters, social welfare and various equity considerations.

B12.41 Certain payroll deduction services

On 24 April 1996, the Council received an application from the Australian Union of Students (AUS) seeking access to a service described by AUS as the "Austudy Payroll Deduction Service". AUS identified the facility to provide the 'service' as the computer network of the Commonwealth Department of Employment, Education, Training and Youth Affairs (DEETYA). Austudy is a form of financial assistance provided by the Commonwealth Government to approved students.

The service sought by AUS required DEETYA to establish a system of payroll deductions to enable the Applicant, AUS, to be paid membership fees directly from students' Austudy payments. The facility proposed to provide the service was DEETYA's computer network. DEETYA does not provide a payroll deduction service. In seeking declaration of the service, AUS requested that the Council require DEETYA to establish the service in the form outlined by AUS.

On 19 June 1996 the Council recommended to the Commonwealth Treasurer that the service sought by the AUS not be declared. On 14 August 1996, the Treasurer announced his agreement with the Council's recommendation and reasons. The processes used by the Council in considering the application, and the reasons for the Council's recommendation, were set out in the Council's 1995-96 annual report.

On 30 August 1996, AUS lodged an appeal with the Australian Competition Tribunal, seeking a review of the Treasurer's decision. On 28 July 1997, the Tribunal affirmed the Treasurer's decision not to declare the service.

B12.42 Sydney and Melbourne airport services

On 6 November 1996, the Council received applications from Australian Cargo Terminal Operators Pty Ltd (ACTO) to declare particular services at the Sydney and Melbourne International Airports. ACTO is a small business which provides cargo terminal services to international airlines. ACTO

breaks down and builds up freight, and transfers that freight to and from international aircraft.

The applications sought declaration of the following services:

- the service provided through the use of the freight aprons and hard stands to load and unload international aircraft at Sydney International Airport ('S1') and Melbourne International Airport ('M1');
- the service provided by the use of an area at the airport to: store equipment used to load/unload international aircraft; and to transfer freight from the loading/unloading equipment to/from trucks at Sydney International Airport ('S2') and Melbourne International Airport ('M2'); and
- the service provided by use of an area to construct a cargo terminal at Sydney International Airport ('S3') and Melbourne International Airport ('M3').

ACTO identified the Federal Airports Corporation (FAC) as the provider of the service.

On 8 May 1997, the Council forwarded its recommendations to the Federal Treasurer. It recommended that the services specified in the first and second applications should be declared (S1, S2, M1, and M2), but that those specified in the third should not be (S3 and M3). The processes used by the Council in considering the applications, and the reasons for the Council's recommendation, were set out in the Council's 1996-97 annual report.

On 14 July 1997, the Treasurer announced his acceptance of the Council's recommendations and the reasons supporting them.

The FAC subsequently lodged an appeal with the Australian Competition Tribunal in relation to declaration of services at Sydney airport (S1 and S2). The appeal has yet to be finalised.

The broader issue of access to airport facilities by third parties wishing to compete with the current users of services is currently before the ACCC. Under the *Airports Act 1996*, the ACCC may become involved in setting the

terms and conditions of access to services at airports, possibly including airfreight handling services.

Box B12.4 Airport freight handling facilities

The airport freight-handling industry consists of cargo terminal operators (CTOs) and ramp handlers. CTOs consolidate outgoing freight and break down incoming freight. Ramp handlers load consolidated containers of freight on to aircraft. For third parties to compete, they must have access to the freight aprons and hard stands on the airports to load and unload aircraft, and a place to store equipment and transfer freight to trucks.

According to a 1996 government inquiry (Parliament of the Commonwealth of Australia HRSCCTMR 1996), the freight handling market was experiencing significant problems that inhibited the creation of export markets. The report suggested that increased competition at airports could alleviate many of these problems.

According to industry participants, the declaration of freight handling services at Sydney and Melbourne International Airports helped progressed the development of competition in that industry – by publicising access to airports, forcing the pace of change, and increasing industry awareness of the relevant issues in handling freight through international airports.

For example, Sydney International Airport will appoint two additional ramp handlers to operate alongside the existing operators. As well, additional cargo terminal operations will be constructed and potential operators will be required to provide off-airport cargo terminal operators with access to terminal facilities. Finally, an interim common-user by-pass facility at the airport will be constructed, to facilitate the operations of approved off-airport cargo terminal operators. These developments will provide consumers a greater choice of CTOs and ramp handlers for their freight.

Box B12.4 …cont

Similarly, at Melbourne International Airport, a third on-airport CTO facility was established in February 1998, alongside Qantas, Australian Air Express, and Ansett, thus expanding consumer choice. No one has approached Melbourne Airport's operator, Australia Pacific Airports (Melbourne) Pty Ltd (APAM) seeking access to services under the declaration. However, APAM has encouraged investment and upgrading in freight handling services, which has attracted the attention of several freight handling companies.

B12.43 Brisbane to Cairns rail freight services

On 24 December 1996, the Council received an application from Carpentaria Transport Pty Ltd seeking declaration of specified rail freight services on the Brisbane-Cairns corridor. Carpentaria transports and warehouses freight in Queensland. It already moves freight along the coastal corridor extending as far as Cairns by dedicated trains operated by Queensland Rail (QR).

Carpentaria sought increased access to services provided by QR needed to run dedicated trains along the Brisbane-Cairns line. It specified a range of facilities – including narrow gauge track, rolling stock, shunting equipment, lifting equipment, and terminals – that it argued were necessary to provide the service.

On 3 June 1997, the Council forwarded its recommendation to the Queensland Premier. It recommended against declaration of the service. The processes used by the Council in considering the application, and the reasons for the Council's recommendation, were set out in the Council's 1996-97 annual report.

On 1 August 1997, the Queensland Premier announced his decision not to declare the service. The Premier's statement of reasons differed in several respects from the Council's (see the Council's 1996-97 annual report).

On 21 August 1997, Carpentaria lodged an appeal against this decision with the Australian Competition Tribunal. The appeal has yet to be finalised.

B12.44 Sydney to Broken Hill rail services

On 4 February 1997, Specialized Container Transport (SCT) applied to the Council for declaration of the Sydney-Broken Hill rail service provided by the NSW Rail Access Corporation (RAC).

SCT provides an interstate rail freight forwarding and distribution service. SCT was seeking to offer its own rail freight forwarding service between Sydney and Perth. It intended to carry freight on RAC track between Sydney and Broken Hill, for on-carriage to Perth via the transcontinental railway owned by Australian National, which traverses South Australia and runs into Western Australia.

In its application, SCT sought declaration of:

- standard gauge railway lines between Sydney and Broken Hill along the routes, Sydney-Lithgow-Parkes-Broken Hill and Sydney-Cootamundra-Parkes-Broken Hill; and
- services provided by rail infrastructure facilities which are integral to providing access to these lines.

RAC is a NSW Government agency that sells access to the state rail network to existing and new passenger and freight rail operators.

On 16 June 1997, the Council recommended to the Premier of NSW that the service to which SCT sought access be declared. See the Council's 1996-97 annual report for further details.

On 18 August 1997, the Premier announced that he had decided not to make a formal decision in relation to the Council's recommendation given work being undertaken between the Council and the NSW Government in relation to its application for certification of the NSW Rail Access Regime. As a result, the service was deemed not to be declared.

On 27 August 1997, SCT lodged an appeal against this outcome with the Australian Competition Tribunal. SCT later withdrew its appeal after reaching an agreement with the RAC.

B12.45 Hunter Valley rail service

The application

On 3 April 1997 the Council received an application from NSW Minerals Council Limited (Minerals Council) for declaration of the Hunter Rail Line service provided using the railway line and associated infrastructure facilities controlled by the Rail Access Corporation (RAC).

The Minerals Council represents 21 coal producing companies that use the Hunter Rail Line to transport their coal. The Hunter Rail Line has coal line unloading terminals at Eraring Power Station, south of Newcastle, Port Waratah and Kooragang Island, Newcastle, Ulan coal mine near Gulgon, west of Newcastle and Vickery and Gunnedah coal mines near Gunnedah, northwest of Newcastle.

In the application, the Minerals Council argued that the Hunter Rail Line has the characteristics of a natural monopoly and is of substantial importance to the Australian economy in that it is a vital conduit between mines and markets. It said that declaration should allow its members to negotiate directly with RAC and freight haulers, imposing competitive pressures on both services.

The application complained about the ability of the NSW Rail Access Regime to facilitate access to the Hunter Rail Line, pointing to the lack of alternatives to FreightCorp as evidence. The Minerals Council was also concerned at the pricing approach used in the regime, and argued that it is arbitrary, prescriptive and contains monopoly elements. Many of these issues are also relevant to NSW's application seeking certification of its rail access regime (see Section B12.53).

A threshold issue in considering this application is the interpretation of section 78 of the *Competition Policy Reform Act 1995*, which provides:

> 78(1) For the period of 5 years after the commencement of Section 59, a government coal-carrying service is not a service for the purposes of Part IIIA of the Principal Act [ie the TPA].
>
> (2) In this section:
>
> 'government coal-carrying service' means a service of carrying coal by rail, where the provider of the service is a State or Territory or an authority of a State or Territory.

In its application, the Minerals Council argued that, in this instance, section 78 did not apply. The basis of its argument was the distinction drawn in the definition of a service under Section 44B of the TPA between the use of an infrastructure facility ((a) – eg a railway line) and the handling or transporting of goods or people ((b) – eg railway haulage). The Minerals Council argued that the use of a railway line falls within the definition of service ((a) – eg a railway line) under paragraph 44B, where as the service referred to section 78 fell within the handling or transporting of goods or people ((b) – eg rail haulage).

In view of the importance of Section 78 to the Mineral Council's application, the Council sought independent legal advice concerning its ability to consider this application. This advice supported the views put by the Minerals Council and concluded that the Council could consider the application.

The process

In processing the application, the Council:

- notified the RAC and the NSW Premier of the application;
- placed advertisements in major newspapers in April 1997, seeking submissions from interested parties by 11 June 1997;
- released an Issues Paper;
- received five submissions; and
- held discussions with the Minerals Council, the RAC, NSW Government, FreightCorp, and other interested parties.

On 1 September 1997, the Council recommended to the NSW Premier that the rail service be declared. The basis for the Council's recommendation is summarised below.

On 3 November 1997, as the Premier had not made any formal decision on the application, the service was deemed not to be declared.

In November 1997, Minerals Council lodged an appeal against this outcome with the Australian Competition Tribunal. A preliminary question concerning the interpretation of section 78 is currently before the Federal Court. The appeal before the Australian Competition Tribunal can not proceed until the section 78 matter is finalised.

Criterion A: Access would promote competition in another market

The purpose of this criterion is to ensure that the Council only recommends declaration when tangible benefits, achieved through improved access in the market for the service, are carried through to consumers of products in other markets.

To determine if access in the market for the service would improve the terms and conditions of products in other markets, the Council adopted the following three step approach:

1. *Assess the current level of competitiveness in the market for the service*. If the market for the service is already a competitive market, introducing Part IIIA processes to it will not increase competition and hence provide an improvement in its terms and conditions sufficient to affect the competitiveness of other markets.
2. *Verify that nominated markets are additional*. Ensure that the products affected by access are in additional markets, not in the market subject to the application. Access to a service would also increase the competitive pressure on any of its substitute services. However, a close substitute would be in the same market and nomination of this product would not meet this criterion.

3. *Determine if access benefits are likely to be retained in the terms and conditions of products in other markets:*

   (i) The structure of the other market needs to be examined to see if the benefits flowing from access in the market for the service are likely to be retained in the terms and conditions applying to products in the other markets. The benefits are likely to be maintained if the other market is competitive. If the additional market is uncontested, the benefits from access are likely to be absorbed by monopoly pricing.

   (ii) If the subject service is an insignificant input into the other products, the benefits from access are unlikely to significantly alter the competitiveness of the other market.

1. Assess the current level of competitiveness in the market for the service

RAC is currently the only provider of rail line services in the Hunter region. The ability of another player to enter the market is significantly curtailed by the high sunk costs of entry, decreasing unit costs of operation and the current under-utilisation of parts of the Hunter Railway Line.

If the services of the Hunter Railway Line are subjected to competition from other modes of transport, competition may well be effective, despite RAC being a monopoly railway line supplier. The Minerals Council advised that coal haulage is restricted to rail as most of the coal mines using the Hunter Railway Line are required by their development consent and/or mine lease conditions to use rail for transporting coal. (Minerals Council 1997b)

The Council concluded that the existing competitive pressures are not effective on the service covered by the application.

2. Verify that nominated markets are additional.

The application argued that competition would be promoted in other markets including:

- rail haulage of Hunter Region coal; and
- the Australian coal market.

The Council was satisfied that these markets were separate to the market for rail line services.

3. Determine if access benefits are likely to be retained in the terms and conditions of products in other markets

Rail haulage of Hunter Region coal

(i) significance of rail line services as an input

In informal discussions, FreightCorp estimated that the cost of using the rail network ranges between 30 and 40 percent of the coal rail haulage charge. Currently the two products are bundled together and as some coal prices include a monopoly component, it is difficult to separate out the price of rail line use from the price of coal haulage and the monopoly rent. However, it can be confidently asserted that any changes in the cost of rail line services will have a noticeable effect on the costs of coal haulage.

(ii) market structure

It could be expected that there would be several suppliers in the rail coal haulage market, given that asset costs, such as locomotives and rolling stock, while not insignificant, would not be beyond the resources of many firms.[4] Contrary to these expectations, there was only one supplier of rail coal haulage in NSW – FreightCorp. Submissions pointed to the difficulties new entrants had gaining access to the NSW rail network. (SCT 1997; TNT 1997; NR 1997; and Minerals Council 1997a)

The Minerals Council saw access under the declaration process as the catalyst for the entry of further coal haulers and foresaw this resulting in a reduction in the price of both the rail line and coal haulage markets. The members of the Minerals Council were prevented from negotiating with RAC on the charges for the use of rail line services. They negotiated with FreightCorp for

4 In the US and Canadian markets, a 110 tonne capacity coal wagon currently costs $A87,000 while a 4400HP locomotive currently costs $A2.5 million.

a composite charge, which included the cost of using RAC's line and FreightCorp's assets and expertise. The Minerals Council argued that as a single supplier, FreightCorp could pass through any rail line charges and had little incentive to negotiate these charges down. (Minerals Council 1997a)

Effective access should provide the Minerals Council's members with the option of negotiating rail line charges directly with RAC and coal haulage charges directly with its hauler of choice, thus, introducing new operators into the coal haulage market. If permitted to conduct its operations in this way, the Minerals Council would expect at least one new operator on the Hunter Railway Line. (Minerals Council 1997b)

The Council considered the rail line service was a significant component of the costs of coal haulage and that rail line access should promote competition in the Hunter coal rail haulage market.

Coal market

(i) significance of rail line services

The railway line service was considered to be a significant component of total rail costs. Rail costs, in turn, were a significant component of delivered coal costs. Access should achieve a reduction in railway line service costs and a reduction in coal haulage costs, which would flow through to reduce the prices Hunter coal miners need to charge.

(ii) market structure

Queensland and NSW are the main competitors for export and domestic sales. While NSW produced 44 percent of Australian exports in 1995 (the majority from Hunter region mines), Queensland accounted for 56 percent. There are a plethora of mines in both states (70 in NSW and 45 in Queensland) (ABCS 1995), competing for domestic and export sales. However, the operating costs of NSW mines are considerably higher than those of Queensland mines. (Minerals Council 1997a) Any reduction in costs in NSW railway line services should increase the relative competitiveness of all affected Hunter mines vis-a-vis all other Australian mines, including those of Queensland.

The Council concluded that a reduction in Hunter rail costs would improve the trading position of all Hunter mines relative to other Australian mines, promoting competition in the coal market.

Criterion B and Section 44F(4): Uneconomic to duplicate all or part of the facilities

Criterion (b) is intended to apply to infrastructure services provided by natural monopolies – that is, to services provided by infrastructure facilities that are not commercially viable to duplicate.

In assessing these criteria, the Council observed that natural monopolies characteristically require large fixed cost commitments (in the form of assets that are difficult to sell for another purpose), providing large quantities of capacity and involving relatively small operating costs. In the case of the Hunter Line:

- the capital costs of duplicating the Hunter Railway Line would be prohibitively high;
- there would be significant difficulties obtaining the necessary land due to, among other things, the lack of compulsory powers of acquisition of a non-government entity;
- there was significant spare capacity on all parts of the Hunter Railway Line; and
- substitute haulage modes were uneconomic.

The Council concluded that, given these natural monopoly characteristics, it would be uneconomical for anyone to develop another facility to provide either a Hunter Railway Line service, or part of that service.

Criterion C:
National significance

The Council considered that the rail service facility is nationally significant. While the Hunter Railway line is only a small proportion of the Australian rail network, the Council notes that the estimated total cost of duplicating these lines is between $400 and $825 million.

Regarding the rail service facility's *importance for interstate commerce and trade*, the Council observed that approximately 41 million tonnes of coal are carried on this line each year and that 80 non-coal trips per day operate on the most heavily utilised segment of this line – Maitland to Port Waratah. The monetary value of this volume is considerable.

Regarding the rail service facility's *importance to the national economy*, the Council observed that the contribution of Hunter coals to exports and domestic coal sales is considerable.

Criterion D:
Health and safety

In this and previous inquiries, the Council received comments that expressed some concern that safety and credit-worthiness requirements could be used as a barrier to entry. (SCT 1996; NR 1997)

The Council was satisfied that access to the service could be provided without undue risk to human health or safety and so met criterion (d). It was however, concerned that prospective entrants may be deterred by the costs of inconsistent accreditation standards and processes.

Criterion E:
Effectiveness of NSW Rail Access Regime

The criteria for judging the effectiveness of State and Territory regimes are set out in clauses 6(2)-(4) of the CPA. In assessing the SCT (NSW) Application for Declaration, the Council concluded that the NSW Rail

Access Regime did not meet these criteria (see the Council's 1996-97 annual report for a detailed summary). The Council considers that this application meets this criterion for the same reasons as set out in the SCT (NSW) Application for Declaration.[5]

Criterion F: Public interest

The Council has noted previously that the term 'public interest' is not defined in the Act and will therefore need to be assessed on a case-by-case basis. (NCC 1996)

This criterion has been expressed in the negative – "not contrary to the public interest" – rather than the positive – "in the public interest". This reflects the fact that criteria (a) to (d) already address a number of positive elements in the public interest.

The Council considered the various arguments raised by submissions but could not see costs sufficient to negate the benefits indicated above in criteria (a) to (d). It therefore concluded that declaration of the Hunter Rail Line was in the public interest.

Duration of declaration

The Council considers the period of declaration on a case-by-case basis. Relevant considerations include the need to balance the benefits of long-term certainty for businesses against the potential for technological development, reform initiatives, or other industry changes which could undermine the grounds for declaration. Balancing these considerations, the Council considered that the duration of declaration should be 15 years.

5 Progress on the NSW Rail Access Regime is outlined later in Section B12.53.

B12.46 Western Australian rail and freight support services

The application

On 25 July 1997, the Council received five applications from Specialized Container Transport (SCT) for the declaration of certain Western Australian rail services.

SCT currently carries freight on Westrail track between Kalgoorlie and Perth continuing on from the transcontinental railway owned by Australian National.

The five applications sought declaration of the following services:

- the Westrail railway network service and associated infrastructure between Kalgoorlie and the Perth metropolitan area including access to the Forrestfield yard and the branch from the yard to the SCT terminal at Welshpool and access to the proposed Canning Vale terminal of SCT (rail service);
- particular arriving and departing services at the Forrestfield yard (arriving/departing service);
- particular marshalling and shunting services operated on Westrail track (marshalling/shunting service);
- particular Westrail network services and associated infrastructure to enable SCT to undertake its own marshalling and shunting activities in respect of SCT freight trains operated on Westrail track (marshalling and shunting access); and
- fuelling service operated on Westrail track including such services at and between Kalgoorlie and the Perth metropolitan area and within the Perth metropolitan area (fuelling service).

Where appropriate the arriving/departing service, marshalling/shunting service, marshalling/shunting access and fuelling service are referred to collectively as 'freight support services'.

SCT identified Westrail as the provider of the services. Westrail is a statutory authority established under the *Government Railways Act 1904* (WA) and is directly responsible to the Minister for Transport in Western Australia.

The process

In assessing the application, the Council:

- notified the Premier of Western Australia and Westrail of the applications;
- placed advertisements in major newspapers including the Daily Commercial News and the Western Australian;
- released a Discussion Paper in August 1997;
- received three submissions; and
- held discussions with SCT, Westrail and the Western Australian Government.

On 21 November 1997, the Council recommended to the Western Australian Premier that the rail service be declared but that the freight support services *not* be declared. The Council's recommendations are summarised below.

On 20 January 1998, the Westren Australian Premier announced that he had decided not to declare Westrail's rail line service and its freight support services. The Premier decided not to declare Westrail's rail line service because he determined that an access regime, drafted last year by the Department of Transport, was an 'effective access regime' for the purposes of the Part IIIA criteria. In his decision, the Premier indicated his intention to ask the Council early in 1998 to recommend to the Commonwealth Treasurer that the access regime be certified as an effective access regime under Part IIIA.

Western Australia is in the process of developing this rail access regime. However, the regime has not been formally submitted to the Council for it to consider its effectiveness, although the Council Secretariat has provided Western Australia with informal comments on a preliminary draft. Western Australia had not passed the legislation necessary to give effect to the regime.

On 10 February 1998 SCT lodged an appeal against the WA Premier's decision with the Australian Competition Tribunal. SCT later withdrew its appeal after reaching an agreement with the Westrail.

Criterion A: Access would promote competition in another market

In assessing the application against this criterion, the Council followed the three-step approach it adopted in its assessment of the Minerals Council application (see Section B8.45).

1. Assess the current level of competitiveness in the market for the service

In assessing the current levels of competition in the freight forwarding market, the Council considered other modes of transport including air, sea and road in the bulk and non-bulk markets and in the interstate and intrastate markets. The Council concluded that:

- air transport was not a substitute for rail; and
- practically, sea transport was not a substitute for rail although it was theoretically possible;

but that:

- road transport was a possible substitute for rail particularly in the non-bulk market.

In the interstate and intrastate non-bulk market, the Council noted that the competition between road and rail transport, means that the provision of access to rail would not necessarily increase competition significantly in relation to all products. However, the Council noted that that rail is the preferred transport mode for some non-bulk freight, for example, steel products. This could provide rail operators with a substantial degree of market power in this segment of the freight market. In turn, this means that competition from road would not significantly reduce any gain in competition from increased access to rail in these segments.

2. Verify that nominated markets are additional.

The application argued that access to rail and freight support services would promote competition in the market for freight forwarding services. The Council considered that access to rail and freight support services and freight forwarding services were in different markets because they were both:

- economically separable as the costs involved in providing the separate services are not so great as to not make it worthwhile; and,
- in different markets because the specific assets needed for use of the rail and freight support services also cannot be readily transferred to freight transport or forwarding services.

3. Determine if access benefits are likely to be retained in the terms and conditions of products in other markets

The Council considered the freight forwarding market to be a highly competitive market but it agreed with submitters that competition in rail could be improved. The Council did not receive any evidence indicating that the distributors of products are not competitive.

Accordingly, the Council considered that the benefits derived from access would likely flow on to those products available in different markets.

Rail service

The Council considered that the application met this criterion. The increase in competition, through increased access, was unlikely to be large but it would be more than trivial. The Council agreed that declaration of the service would promote competition in a market other than the market for the service by improving the prospects for entry, innovation and market structure in the freight forwarding market.

Freight support services

The Council considered that these applications did not meet this criterion. It argued that while access to the freight support services would promote competition in the short term, in the long term competition could be discouraged as investment in the necessary facilities to provide those services would be discouraged.

Criterion B and Section 44F(4): Uneconomic to duplicate the facility to provide the service or part of the service

Criterion (b) requires the Council to determine whether it would be uneconomical for anyone to develop another facility to provide the service as a whole. Section 44F(4) requires the Council to consider whether it would be economical for anyone to develop another facility to provide part of the service. Criterion 44F(4) is discrete from criterion (b), however because the analysis required by both criteria is similar, the analysis of criterion 44F(4) follows immediately after that of criterion (b).

Rail service

The line from Kalgoorlie to the Forrestfield yard is 655 kilometres long and a further 15 kilometres from the Forrestfield yard takes the line to Canning Vale. The line to the SCT privately owned siding branches off in the Forrestfield yard and is about 4 kilometres in length.

The track involves substantial fixed costs (many of which are sunk), and relatively low variable costs. ('Carpentaria QR rail application – Reasons for Decision' provides details of what costs are involved in constructing a rail line.) The Council accepted the view that the Kalgoorlie-Perth rail line and associated infrastructure facilities were uneconomic to duplicate as a whole for the service. Accordingly, the Council concluded the application met criterion (b).

The Council, however, considered that the branch line leading off from the main line to SCT's privately owned siding was a separate facility to the main

rail line. Section 44F(4) required the Council to consider whether it would be economical for anyone to develop another branch line to provide that part of the rail service.

The Council concluded that the branch line to SCT's privately owned siding at Welshpool was both difficult to duplicate and integral to the service to which SCT sought access. This was because SCT could not provide its freight forwarding service unless it could access its siding, and the only way SCT could access its siding was by way of the branch line. The branch line, in effect, was a natural monopoly.

Accordingly, the Council concluded that, in these circumstances, it would not be economical for anyone to duplicate the branch line, and therefore, the application met criterion 44F(4).

In addition, given the wording of section 44F(4), the Council considered that even if the branch line was found to be economic to duplicate it could still recommend declaration.

Freight support services

The Council examined whether or not some of the facilities used to provide freight support services were economic to duplicate in Carpentaria's QR rail application – 'Reasons for Decision'. Its analysis concluded that facilities such as locomotives and terminals were economic to duplicate.

In its freight support services applications, SCT argued only that it was uneconomic to duplicate the facilities within the time available to it. The Council, therefore, limited its examination of economic to duplicate to the question of timing.

The Council noted that the issue of timing was not included in the Part IIIA criteria. Further, that declaration of such a service on that basis, even for a short period of time, would expose that service to a third party seeking access rights even when that party was able to readily duplicate the facility providing the service.

The Council noted that there was a potential for access regulation to diminish incentives for businesses to invest in freight support facilities and thus limit, rather than enhance, overall competition and economic efficiency.

The Council did not accept SCT's contention that the test includes whether or not it is economic to duplicate within a specified period of time. Accordingly, the Council considered that the freight support services were economic to duplicate and that the applications did not meet criterion (b).

Criterion C: National significance

Rail service

The Council considered that the rail service facility is nationally significant in terms of *size.* In this context, it noted that the Kalgoorlie-Perth line is the sole rail route linking the eastern and western states and is approximately 655 kilometres in length. It also noted that the estimated cost of duplicating this line is between $1.0 and $1.5 million per kilometre.

Regarding the rail service facility's *importance for interstate commerce and trade*, the Council observed that a significant volume of freight is transported between Sydney/Melbourne and Perth via the Kalgoorlie-Perth line. The monetary value of this volume is considerable.

The rail service facility is also *important to the national economy*, as the Kalgoorlie-Perth line provides a vital link between the important economic centres, many of which depend on rail transport for carriage of the commodities that they produce, in the eastern states and Western Australia.

Accordingly, the Council considered the application met this criterion.

Freight support services

The Council was not convinced that facilities such as terminals, shunting locomotives and locomotive fuelling stations or pads could be considered as nationally significant on the basis of their *size.*

Similarly, the terminal, shunting locomotives and fuelling station or pad were not important, in their own right, to *constitutional trade or commerce*. While those facilities do facilitate significant trade and commerce carried over the rail line facility, other facilities can provide the same service. The fact that the facilities could facilitate trade and commerce did not make them nationally significant.

Finally, in relation to facilities' *importance to the national economy*, the Council considered that while SCT's freight forwarding service contributed to competition in the rail freight market, the contribution to competition in the freight forwarding market was not so substantial. The freight support services were important to SCT's freight forwarding business, however, they were not so important to the rail freight market and even less so to the freight forwarding market.

Accordingly, the Council considered these applications did not satisfy this criterion.

Criterion D: Health and safety

Rail services and freight support services

The Council understood that Western Australia's safety accreditation regime was very similar to those of other states and that the safety accreditation regime can enforce safety standards.

The Council, therefore, considered that access to the Kalgoorlie-Perth service could be provided without undue risk to human health and safety. According, the Council considered that all the applications met this criterion.

Criterion E:
Effectiveness of Western Australia Rail Access Regime

Infrastructure services covered by 'effective' access regimes cannot be declared under Part IIIA of the TPA. The Council must assess whether a State or Territory regime is effective at the time it assesses an application for declaration, unless the regime has already been certified. The criteria for judging the effectiveness of State and Territory regimes are set out in clauses 6(2)-(4) of the CPA.

Westrail submitted that there was in place an "effective informal regime, under section 61 of the Government Railways Act ...". Section 61 gives Westrail the power to enter into an agreement with a person entitling that person to use a railway, or part thereof, to operate a rail service.

Section 61 of the Government Railways Act, however, does not incorporate any of the criteria set out under clauses 6(2)-6(4) of the CPA. Therefore, the Council determined that it could not be considered as effective for the purposes of criterion (d).

As Western Australia had not established a rail access regime applicable to the Western Australian rail network or associated facilities, the Council decided there was no regime that could be considered to be effective.

Criterion F:
Public interest

The Council's approach to the public interest criterion is discussed in Section B12.45.

Rail service

None of the submissions raised any issues in relation to this criterion. The Council used the approach it adopted in previous applications and considered the application was not contrary to the public interest. Accordingly, the Council considered the application met this criterion.

Freight support services

Some of the arguments put by submitters raised issues, such as timing, were addressed by the Council under criteria (a), (b) and (c). In addition, since the Council was not convinced the applications met criteria (a), (b) and (c), it could not recommend declaration of the services. Accordingly, the Council considered there was no need to extensively examine whether they satisfied this criterion.

Duration of declaration

The Council considers the declaration period on a case-by-case basis. Relevant considerations include the need to balance the benefits of long-term certainty for businesses against the potential for technological development, reform initiatives, or other industry changes which could undermine the grounds for declaration.

In this case, the Council recommended that the duration of declaration should be 15 years. In doing so, the Council noted that this period provides a greater level of certainty about rail access rights than currently enjoyed by private rail operators in Australia. It also noted that declaration of the Kalgoorlie-Perth service could be reconsidered at the end of the 15 year period. As access seekers are able to negotiate contracts that extend beyond the period of declaration, the period of certainty for individuals could be extended, while still allowing the application of the Access Regime to be reviewed.

B12.5 Council recommendations on certification

This section provides details of the handling of specific applications for the certification of State and Territory regimes as 'effective' under Part IIIA of the TPA.

To date, the Council has received five applications for certification, dealing with:

- the NSW gas distribution access regime;
- Victorian shipping channels;
- the NSW rail network;
- the QLD rail network; and
- the SA third party natural gas access regime.

In processing applications for certification, the Council is required to make assessments against criteria set out in Clause 6 of the CPA. The Council conducts a public consultation process. It advertises the application, seeks submissions, and provides comprehensive analysis to support its recommendation.

The Council's processes in relation to each application, considered during 1997/1998, are summarised below as are the Council's recommendations and analysis.

B12.51 NSW natural gas distribution

On 9 October 1996, the NSW Premier applied to the Council to consider the effectiveness of the NSW regime for access to the services of natural gas distribution networks.

The NSW regime comprises an access code operating in conjunction with the *Gas Supply Act (NSW) 1996*. It was developed as an interim measure until a uniform National Access Code for gas is implemented (see Chapter B7). The Council was asked to consider the effectiveness of the regime in relation to services owned by the AGL Gas Company (NSW) Limited[6] and the Albury Gas Company Limited.

6 In a recent corporate restructure, the gas distribution functions of the AGL Gas Company (NSW) Limited were relocated to a new company, AGL Gas Networks Limited.

By late April 1997, all amendments required to make the regime effective had been implemented. In addition, the NSW Government introduced other amendments to the regime, including amendments to the transitional arrangements and pricing principles, to satisfy its own policy concerns.

On 16 May 1997, the Council recommended to the Commonwealth Treasurer that the NSW Regime be certified as effective. The processes used by the Council in considering the application, and the reasons for the Council's recommendation, were set out in the Council's 1996-97 annual report.

On 18 August 1997, the Treasurer announced his acceptance of the Council's recommendation and the reasons supporting it.

B12.52 Victorian commercial shipping channels

On 24 December 1996, the Premier of Victoria applied to the Council to consider the effectiveness of the Victorian Access Regime for Commercial Shipping Channels (the Victorian Regime)

This regime applies to Victorian commercial shipping channels covering the ports of Melbourne, Geelong, Hastings and Portland. It is given legislative effect under the *Port Services Act (Victoria)* 1995 (the PSA) and is administered by the Victorian Channels Authority (VCA). The VCA is a public authority responsible for managing and maintaining the channels in Victorian port waters, which provide navigable access for shipping vessels between the high seas and port berths. The relevant channels are those in Port Phillip Bay providing entry into the ports of Melbourne and Geelong, and the channels providing entry into the ports of Portland and Hastings. The VCA directly manages the channels in Port Phillip Bay and has channel-operating agreements with the channel operators at Portland and Hastings.

The Council was asked to consider the effectiveness of the Victorian regime in relation to services provided by the channels leading to the Ports of Melbourne, Geelong, Portland and Hastings.

On 12 May 1997, the Council recommended to the Commonwealth Treasurer that the Victorian Regime be certified as effective, for a period of five years. The processes used by the Council in considering the application, and the reasons for the Council's recommendation, were set out in the Council's 1996-97 annual report.

On 18 August 1997, the Treasurer announced his acceptance of the Council's recommendation and the reasons supporting it.

B12.53 NSW rail services

The application

On 12 June 1997, the Council received an application from the NSW Government to certify as 'effective' a regime for access to NSW rail services under Part IIIA of the TPA. The proposed regime includes, among other things, the general framework for arbitration and negotiation of prices as well as the contract terms that would usually be offered by the Rail Access Corporation (RAC) to potential customers.

The NSW regime commenced operation in August 1996 and consists of the *NSW Rail Access Regime* operating in conjunction with:

- the *Commercial Arbitration Act 1984* (NSW);
- the *Transport Administration Act 1988* (NSW);
- the *Rail Safety Act 1993* (NSW);
- the *State Owned Corporations Act 1989* (NSW); and
- the *Independent Pricing and Regulatory Tribunal Act 1992* (NSW).

The process

To date, in processing the application, to date the Council has:

- placed advertisements in major newspapers on early June 1997, seeking submissions by 10 July 1997;
- released an Issues Paper;
- received seven submissions in response to the Issues Paper; and
- held discussions and consultations with the RAC, the NSW Government and other interested parties.

During its discussions with the NSW Government, the Council outlined areas where its process had identified concerns with the effectiveness of the regime. NSW considered these areas and proposed a range of changes to the regime.

By early 1998 the Council considered that the changes proposed by NSW were sufficient to allow the Council to make a Draft Recommendation. The Draft Recommendation, inviting further public consultation, was issued in April 1998. The Council received four submissions on the Draft Recommendation.

NSW has since indicated that it proposes to make changes consistent with the Draft Recommendation and the Council is now awaiting gazettal of the amended version of the regime.

The following is a summary of the Council's draft recommendations relating only to those CPA criteria where changes to the regime are required.

Clause 6(4)(a)-(c): Principles to be included in an access regime

The Council assessed the regime's compliance with Clause 6(4)(a)-(c) on the basis of its ability to facilitate access through the five following components:

- meeting safety requirements;
- obtaining a suitable timepath;
- obtaining agreement on price including arrangements for any necessary new investment;
- obtaining agreement on more general terms and conditions; and
- resolving disputes.

Safety requirements

To address the Council's requirement that the safety accreditation process does not inhibit access, NSW undertook:

> to ensure that [its] Department of Transport give effect, as far as is legally possible, to accreditation to rail operators in other states of Australia; and
>
> to review the issue of mutual recognition and particularly the question of its adequacy without the necessity for underpinning legislation. (NSW 1998)

To ensure a low cost, dispute resolution mechanism on accreditation decisions is in place, NSW stated that:

> Under the Administrative Decisions Legislation Amendment Act 1997, which was passed by the NSW Parliament in June 1997, s.44 of the Rail Safety Act 1993 was amended to provide for a person aggrieved by a decision of the Director General or an authorised agent under Division 3 or 4 to apply to the Administrative Decisions Tribunal (ADT) for review of the decision. The ADT is an administrative review body similar to the Commonwealth Administrative Appeals Tribunal. (NSW 1997)

The ADT was expected to commence operations on 1 January 1998. However, NSW advised that there have been delays and that the ADT is yet to begin operations.

Finally, the Council expressed concern to NSW over the reported allocation of costs across rail operators and the magnitude of fees charged[7]. To address this concern, NSW proposed to:

> refer the issue of the appropriateness of the level of accreditation costs to IPART for analysis. (NSW 1998)

Timepaths

Some submissions also criticised the allocation of timepaths on congested lines and there were suggestions that these allocations should be made more transparent.

In response to these concerns, NSW proposed to confer with the Council, RAC and the Independent Pricing and Regulatory Tribunal (IPART) over a period of three months, to develop a Capacity Transfer Policy.

In the Council's view this was a reasonable first step. The Council also shares the Minerals Council's view that there should be consumer input into the development of the policy.

Price including arrangements for new investment

Negotiations for new investment

The Council noted that the regime gives no guidance to negotiations on access requiring new investment. Accordingly NSW proposed to include a provision requiring RAC to negotiate in good faith with existing or prospective rail operators in relation to new investment subject to certain specified conditions.

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7 Confidential sources quoted amounts approximating $500 000 per annum for large consumers of rail track.

The Council considers that NSW's proposal satisfies the requirements on new investment but that the matter of new investment also should be taken into account when the independent third party reviews the capital cost requirements contained in the regime.

Prices

Pricing matters were further sub-divided into three topics.

(i) approach 'in principle'

The regime uses a 'Baumol floor/ceiling band' approach to define the price parameters within which RAC may offer access. The Minerals Council argued against this approach on the basis that:

- it is difficult to apply because of its extensive informational requirements; and
- it encouraged Ramsey pricing which, while theoretically sound, is impractical to implement and achieve efficient prices. (Minerals Council 1997)

The Council took the advice of its consultant on pricing matters in the regime – Dr Cousins of KPMG. Dr Cousins concluded that the RAC applied the Baumol approach in a pragmatic manner but with sufficient rigour to deliver efficient outcomes. (Cousins 1997, 50)

However, the Council also considered that alone the Baumol band approach did not provide the customer with sufficient information to negotiate and that this would deter access.

NSW will now provide customers with additional information covering costs, capacity, previous arbitration outcomes and timepath conditions. In addition, NSW intends to include cost definitions in the proposed IPART review of appropriate capital costs.

In response to the issue raised in some submissions, the Council noted the potential for inefficient production when prices are set inappropriately across producers of common goods. It concluded that the nominated arbitrator, IPART, could take these matters into account in relevant arbitrations.

As well, the price floor of the 'Baumol floor/ceiling band' has attracted some criticism. The floor is comprised of two limbs. While the first limb is less contentious, the second limb generated some debate.

The second limb provides that:

> ... and for any line section or group of line sections, the full incremental costs, including incremental fixed costs, must at least be met by revenue from the Rail Operators of those sections ...

It aims to ensure that all lines recover all incremental costs and that consequently no cross subsidies can occur. However, as Dr Cousins concludes, in as much as the ceiling requirements do not allow for monopoly profits, they will not allow cross subsidisation. (Cousins 1997, 37)

While the second limb of the floor test may be considered redundant, the Council considered that it may result in RAC pricing access inefficiently. For example, many network lines are under-utilised. Where governments are not willing to close railway lines, it is generally considered that it is preferable to charge a consumer only those costs incurred (first limb floor test), without necessarily requiring them to contribute their full proportion of line fixed costs (second limb floor test). Any price paid by a consumer that makes some contribution towards fixed costs will reduce the burden on other customers.

To address this area of concern, NSW has proposed that the recovery of incremental fixed costs be set as an objective rather than a requirement. The Council considers that this approach addresses its concerns.

(ii) constraints on price negotiation in relation to coal

The regime's coal pricing provisions are quite prescriptive. Coal prices are set (not negotiated) on an origin-destination specific haul basis according to three categories determined by RAC. Category 1 mines, the mines closest to the Port of Newcastle, pay prices to the ceiling plus a monopoly rent or

'adjustment component'. Category 2 and Category 3 mines, situated further away, pay below the ceiling price and pay no adjustment component.

The regime requires the arbitrator to effect these coal arrangements until 1 July 2000, when coal pricing comes under the general Baumol band approach.

The Council had an 'in principle' concern at the inclusion of a monopoly rent in an effective regime. NSW argued that it would be difficult to change its method of rent collection in the short term and noted that the rents would be phased out by 1 July 2000. The Council accepted the phased approach in the regime, given that it is to be effected within a relatively short time.

The Council asked that NSW allow Category 1, 2 and 3 mines the right to negotiate access prices now rather than waiting until 1 July 2000. The adjustment component would then be imposed on Category 1 mines separately.

NSW proposed amending the principles for pricing for the carriage of coal contained in the regime to the following effect.

(a) A per tonne rate based on the difference between FreightCorp's 1996-97 estimated coal haulage revenue less FreightCorp's 1996-97 estimated coal haulage costs including overheads and an appropriate return on capital, but excluding below rail costs.

(b) This per tonne rate may be such that RAC prices and revenues may exceed the ceiling test of the regime. Any such excess will be phased out in equal per tonne reductions on 1 July 1997, 1 July 1998, 1 July 1999 and 1 July 2000, so that at 1 July 2000 the excess will be zero.

(c) Where (b) is relevant, the per tonne rate will be deemed to be a 'base' and an 'adjustment' component. The base component is negotiable, however, in all cases the adjustment component will be such as to fulfil (a) and (b) above. (NSW 1998)

The Council is seeking to clarification of this proposal from NSW.

Box B12.5 Hunter Valley coal freight

Coal from mines in the Hunter Valley makes up a significant proportion of one of Australia's most important exports. The characteristics of coal limit its carriage to rail. Historically, State governments have used this limitation to extract monopoly rents. The coal industry has consistently argued that its expansion is constrained by the high costs of rail transport.

Competitive pressures on coal rail freight emerged in the Hunter Valley when the NSW Minerals Council lodged an application to declare the Hunter Valley Rail Line. Unfortunately, this application has met with considerable delays (see B12.45 for a summary of this process). Even with the delays, however, the pressures from efficient cost based arbitrations have precipitated reductions in rail access charges. For example, rail freight rates in the Hunter Valley fell by 25 percent between 1995-96 and 1997-98, and are scheduled to fall further to reflect a 10 percent reduction in access charges in 1998-99.

In the amended version of the NSW Rail Access Regime, currently under consideration by the Council, Rail Access Corporation proposes to:

- phase out monopoly rents charged to coal freight;
- absorb any costs associated with operating ineffiencies. Efficiency benchmarks will be set by Independent Pricing and Regulatory Tribunal (IPART);
- adjust capital costs to reflect market levels set by IPART; and
- negotiate access arrangements directly with coal miners, allowing coal miners to negotiate with the carrier they choose.

FreightCorp, the only carrier of freight on the Hunter Line, may come under significant competitive pressures over the next few years. National Rail is strongly rumoured to be negotiating with coal firms, following the lifting of a NSW Government constraint on its operation on intrastate lines. FreightCorp advised the Council that it had also reduced coal freight charges, reflecting its substantial improvements in labour productivity, operating costs and rail access charges negotiated with the Rail Access Corporation.

(iii) the appropriateness of components used to calculate prices

The approach and calculation of stand alone costs has critical implications for the level of prices charged to customers and to RAC's performance reporting. For instance, stand alone costs that are too high convey the perception that prices should rise to improve cost recovery. Consumers paying prices that are too high are paying monopoly rents. Coal mines are the consumers most likely to pay prices related to ceiling calculations (capital and operating costs).

In relation to *capital costs*, Dr Cousins concluded that RAC's calculations of stand alone capital costs were based on the inefficient costs of entry. Accordingly, given the monopoly nature of rail track services, unless a reasonable approach is taken to estimating such costs, including the range of assets included in the calculation, the stand alone approach would simply facilitate monopoly pricing.

The Council also considered that the capital costs, including depreciation, needed to be developed as a package. As such it considered that an independent body should examine the approach taken to asset valuation, the maximum rate of return and depreciation.

In relation to *operating costs*, the Council advised NSW of its concern that as a monopoly supplier, RAC could have operating costs, which are higher than those in a competitive environment.

NSW has suggest that IPART set efficient maintenance cost benchmarks so that RAC, and not the customer, bears the cost of inefficient maintenance practices. The Council expects that IPART would use efficient costs as a basis for all operating costs (not only maintenance costs) in its arbitration.

(iv) terms and conditions

Members of the Minerals Council currently negotiate rail access prices indirectly through their freight hauler, FreightCorp. If a coal miner wants to verify the rail track component in FreightCorp's charges it must encourage FreightCorp to seek arbitration on its behalf. The Minerals Council argues that this undermines its negotiating position with RAC. To address this

difficulty, the Minerals Council wanted its members to be able to negotiate access prices, terms and conditions directly with the RAC and then negotiate freight haulage separately with an existing or prospective rail operator.

The Council asked that the NSW Government consider allowing substantial customers such as coal miners, and the newly established national rail organisation ARTC, to negotiate directly on access prices with RAC.

NSW has advised the Council that the amendment to the *Transport Administration Act* 1998 (TAA) passed by the NSW Upper House in June 1998, will meet these requirements.

Clause 6(4)(i), (j) and (l): Arbitration

The IPART Act refers directly to these three clauses and requires IPART to take them into account in arbitrations. In addition, Section 19B(4) of the TAA requires that IPART effect the regime which means that, in order to recommend certification, the Council needs to conclude that all parts of the regime are set appropriately. The discussion under Criteria 6(4)(a)-(c) noted the need for:

- coal pricing principles to be phased out by 1 July 2000; and;
- the methodologies for asset valuation, determining the rate of return and depreciation, be verified by an independent expert.

This would also be necessary for arbitration under the regime to be consistent with the criteria in Clauses 6(4)(i) and 6(4)(j).

Recommended duration of certification

The Council wishes to ensure that the period of certification of the regime meshes with the establishment of the National Regime. At the time of the Draft Recommendation the Council suggested that a period of 12 months from certification of the regime by the Commonwealth Treasurer should coincide with the establishment of a National Regime. The Council will need

to assess this period again prior to its final recommendation, taking into account the estimated timing for the national process.

B12.54 South Australia natural gas access regime

The application

On 22 June 1998, the Council received an application from the South Australian Premier to certify the 'effectiveness' of the South Australian Third Party Access Regime for Natural Gas Pipelines (South Australian Regime) under Part IIIA of the TPA.

The application arises from the commitment, agreed by COAG in February 1994, to develop a uniform framework for access to gas transmission pipelines. This commitment was extended later to include distribution pipelines.

The Gas Reform Task Force was established by COAG in 1995 to identify the actions required to implement the COAG commitment. In July 1996, the Task Force released its exposure draft of the National Third Party Access Code for Natural Gas Pipeline Systems (the Code) for consideration by, and discussion with, stakeholders. The Council undertook an extensive public consultation process in its assessment of the National Gas Access Regime (which includes the Code), which was released in September 1997.

In November 1997 the Commonwealth and all State and Territory governments signed the Natural Gas Pipelines Access Agreement. The Agreement finalised the Code and a process for achieving a National Gas Access Regime. That process requires appropriate legislation being introduced through an application of laws approach with South Australia as the lead legislator.

Pursuant to the Code, therefore, the South Australian Regime establishes an access regime providing an avenue through which persons can negotiate

terms for use of the South Australian natural gas transmission and distribution networks.

The key elements of the South Australian Regime are the *Gas Pipelines Access (South Australia) Act 1997,* the *Gas Pipelines Access (South Australia) Law* (which is set out in Schedule 1 of the *Gas Pipelines Access (South Australia) Act 1997*) and the Code. The South Australian Regime has not yet been proclaimed.

The process

To date, in processing the application, the Council has:

- placed advertisements in major newspapers on late June 1998, seeking submissions by 27 July 1998;
- released an Issues Paper; and
- received four submissions in response to the Issues Paper.

This matter is still under consideration by the Council.

B12.55 Queensland rail access regime

The application

On 5 June 1998, the Council received an application from the Queensland Premier to certify as 'effective' the Queensland rail access regime under Part IIIA of the TPA. The Council received all the relevant material for the application from the Queensland Government on 19 June 1998.

The key elements of the Queensland regime are the *Queensland Competition Authority Act 1997* and the *Queensland Competition Authority Amendment Regulation (No. 1) 1998*.

The access regime establishes the conditions applying to access to rail transport infrastructure managed and operated by Queensland Rail. The access regime does not cover the standard gauge interstate rail infrastructure in Queensland. This infrastructure is to be covered by the proposed national rail access regime so as to provide a single process for interstate rail access.

On 25 April 1998, the Queensland Government announced that it would remove the moratorium on third party access to Queensland Rail's coal-hauling rail infrastructure. That infrastructure is now open to access under Queensland's rail access regime.

Queensland is seeking certification of the regime as effective for a period of 2 years, or other period as recommended by the Council.

The process

To date, in processing the application, the Council has:

- placed advertisements in major newspapers in June 1998, seeking submissions by 7 August 1998;
- released an Issues Paper;
- received seven submissions in response to the Issues Paper; and
- held discussions and consultations with the Queensland Government, Queensland Rail, the Queensland Competition Authority and several major rail customers.

This matter is still under consideration by the Council.

B13 THE COUNCIL'S REVIEW OF AUSTRALIA POST

B13.1 Background

As part of the NCP Agreements, in 1995 the Commonwealth and State Governments agreed to review all legislation which contains provisions which restrict competition. The *Australian Postal Corporation Act* 1989 is one of the pieces of Commonwealth legislation that is covered by this agreement. The Commonwealth requested the Council to conduct this review.

The main focus of the Council's considerations was directed at how Australia Post's social responsibilities can be maintained and strengthened, while maximising the benefits from competition. The Council viewed the social objectives as fully justified and dismissed options for increasing competition which compromised these objectives.

The Council's review was conducted consistent with guidelines in the Competition Principles Agreement. These guidelines recognise that the costs and benefits of restricting competition need to be assessed individually for each industry. For example, some competitive restrictions perform a necessary function, such as protecting people from dangerous products, while other restrictions may have been put in place for reasons which no longer hold. The agreement sets out some guiding principles for the legislation reviews.

In light of this, during this review the Council was asked to examine:

- the need for the provisions which restrict competition;
- whether the overall benefits to the community of restricting competition outweigh the costs; and
- whether there are other ways to achieve the identified social objectives without restricting competition.

These issues form the core of all legislation reviews.

For each of the legislation reviews, there will be some specific factors that need to be taken into account. With Australia Post these have included the social responsibilities of Australia Post: the universal service and the uniform letter price; its role in the communications infrastructure; and its effects on other parts of the sector and the community.

Current situation

The *Australian Postal Corporation Act* 1989 contains a number of restrictions on competition. The main restrictions arise from those sections of the Act that reserve certain postal services to Australia Post. With a few exceptions, only Australia Post can carry a letter for less than $1.80 if it weighs less than 250g. In addition, only Australia Post can deliver international mail in Australia.

The Act also requires Australia Post to provide reasonable access to postal services for all Australians – a universal service obligation. In addition, it stipulates that Australia Post must provide a letter service at a uniform rate across the whole country; so whether you want to send a letter from Bourke to Mount Isa or around the corner in a capital city, the cost to the sender is the same.

Because Australia Post must provide a universal service at a uniform rate, there may be some mail routes where it would not provide the service, or would only provide the service at a higher price, if this was not required by its legislation. The extra costs incurred as a result of servicing these routes are Australia Post's community service obligation (CSO) costs. Australia Post estimates that these currently stand at around $67 million a year.

The funds to pay for these CSOs are drawn from the profits Australia Post makes on the low cost mail paths such as around the corner in a major metropolitan area. To protect Australia Post's revenue on these routes, the Act restricts competition in the provision of letter services. If there were no restrictions and the requirement to cross-subsidise was retained, then competitors could cream skim – that is, service the highly profitable routes while leaving Australia Post to carry the CSO routes with a much reduced funding base.

The postal services review

The terms of reference asked the Council to consider the core legislation review issues of the need for restrictions, their net benefits and alternatives to restrictions. In addition, for each of the legislation reviews, there will be some specific factors which need to be taken into account. With the Australian Postal Corporation Act, these included the social responsibilities of Australia Post, its role in the communications infrastructure and its effects on other parts of the sector and the community, competitive neutrality issues and access. For example, the terms of reference included:

> ..the Council... have regard to
>
> (a) the Government's commitments to maintain Australia Post in full public ownership and provide a standard letter service to all Australians at a uniform price;
>
> (b) the Government's commitment to accelerate and strengthen the micro-economic reform process, including through improving the competitiveness of markets, particularly those which provide infrastructure services, in order to improve Australia's economic performance and living standards;
>
> (c) the Government's obligations under the Competition Principles Agreement... in relation to competitive neutrality...[and] access to services provided by means of significant infrastructure facilities...
>
> (d) the current obligations on Australia Post specified in s26, s27 and s28 of the *Australian Postal Corporation Act* 1989 to: perform its functions in a manner consistent with sound commercial practice; provide a letter service at a single uniform rate of postage for the carriage within Australia, by ordinary post, of letters that are standard postal articles; and meet any performance standards set for it;...

The terms of reference also requested the Council to examine, amongst other things:

> 4(c) the scope, extent and organisational structure of commercial activities undertaken by Australia Post other than the reserved letter service. The competitive neutrality issues that may arise including the associated benefits and costs from these activities, should be identified and addressed as necessary.

(d) the operation of the current letter mail interconnection arrangements and the possible application of the general interconnection arrangements under the Trade Practices Act 1974..."

B13.2 Method

The nature and scope of the review meant that the Council needed to hear as many views and take as much advice as it could. It needed to let the public know that the review was underway and how to go about making a contribution.

Accordingly, the Council advertised nationally in newspapers about the review. In the advertisements, the Council indicated that interested parties could request an issues paper and called for submissions. The Council stressed that it wished the process to be open and public and therefore requested that all submissions could be made publicly available.

Because of the Australia-wide interest in the review, the Council organised meetings with interested groups, businesses and individuals in all the State capitals and some regional and remote locations. By the end of the review the Council had participated in approximately 130 meetings.

In addition, the Council let three consultancies for work which it considered essential to the proper evaluation of the options for postal reform. These consultancies addressed:

- postal reform in other countries;
- impact of new technologies; and
- financial model of the impact of reform on Australia Post.

In October 1997, four months after the beginning of the review, the Council released an Options Paper for public comment. The Paper canvassed a wide range of options, from Australia Post's reform proposal to full deregulation. The aim was to draw comments on the implications of proceeding in particular directions, identifying benefits and costs, hindrances and advantages. It also highlighted issues that the Council was particularly keen

to hear about from interested parties. The Council called for further submissions, again, asking that submissions could be made public. During the course of the review, the Council received 138 submissions.

The Council convened three workshops which were attended by a wide range of participants. The workshop issues were:

- letter definition
- community service obligations; and
- access arrangements.

The proceedings of the workshops were summarised in the final report.

The final report drew on the consultations, workshops, submissions, the Council's consultants' reports and the Council's own research and analysis. It was released in March 1998.

The Australia Post review was of national significance. It has wide-reaching implications for nearly every Australian. The Council's process therefore aimed to attract participants with a wide range of views, experiences and opinions. The review also needed to be an open and public process.

The Council chose not to hold public hearings, as these can be costly and intimidating to some potential participants. Also, unlike parliamentary committees and the Productivity Commission, the Council does not have the power to guard against the provision of misleading responses or information during a public hearing or any other consultative process. Instead, it encouraged participation through consultations and submissions from interested parties and holding workshops. The process allowed the Council to speak with a wide range of parties in a cost effective manner.

The Council has made comments on the processes used in State and Territory legislation reviews. The process adopted for the Australia Post review fulfils all the Council's requirements for large reviews of national significance:

- it was conducted by an independent panel;
- it was a public process;
- it was widely publicised;

- it sought comment from interested parties;
- an interim report (Options Paper) was publicly released for comment; and
- the final report was made publicly available.

B13.3 Recommendations

The essential elements of the Council's package for the reform of postal services in Australia included:

- to retain the obligation on Australia Post to provide an Australia-wide letter service, with unprofitable parts of the universal service obligation (USO) subjected to community service obligation (CSO) funding from a mix of sources;
- that household letter services remain reserved to Australia Post, with a mandated uniform rate of postage;
- open competition in business letter services, with Australia Post free to discount against a maximum charge set at the same level as the uniform rate for household letters;
- open competition in all international mail services;
- the application of general pro-competitive regulation plus limited special arrangements to restrict monopolistic behaviour by Australia Post in the transition to fully competitive business letter services and to ensure access on reasonable terms to Australia Post's CSO-funded services and post office boxes;
- licensing of all letter service providers to maintain minimum standards;
- accounting separation for Australia Post's retail operations, reserved services and CSO-funded services;

- service standards for the universal service obligation be established in the legislation that will be monitored and enforced by the Australian Communications Authority and a service charter be used to explain these minimum standards to customers; and
- an effective competitive neutrality complaints mechanism.

B13.4 Objectives

In formulating its reform package the Council sought to maximise competition while guaranteeing the universal service and the uniform rate of postage. It was also designed to minimise the cost of postal services to customers, maximise growth in the postal industry, minimise regulation and maintain Australia Post's viability as a postal service provider.

Submissions received by the Council and issues raised during the Council's consultation process indicated that householders and private individuals were most concerned with a high quality service and the continued provision of the CSOs. In contrast, business indicated its preference for increased competition in the business mail segment of the market and stressed that price and customer responsiveness were driving factors. The Council's package delivers both these outcomes.

The Council was of the opinion that opening up the market for business mail would generate significant competition. Indications of this potential competition came from both competitors and postal service users. On the other hand, it was not obvious where or how such competition would arise for household mail.

Further, the Council noted the strong community support for the two social obligations of Australia Post, namely the universal service and the uniform rate. The Council recommended that these obligations be strengthened through guarantees to the community on minimum performance standards. The package of recommendations put forward by the Council would enable

these two obligations to be met, while encouraging competition in markets where it is most likely to arise and be of greatest benefit.

There was not enough information available to be able to judge the impact of extending the package to the household sector. It was therefore judged to be sensible to take the first step of deregulating business mail and then to assess the need for further reform later.

B13.5 Impact of the Council's package

Impact on Australia Post

The Council considers that many have underestimated Australia Post's ability to meet the challenge of competition reform and indeed prosper from it. Australia Post has demonstrated its ability to flourish in competitive markets. Already two thirds of its profit and half its revenue is generated from services open to full competition. Under the proposal for reform put forward by Australia Post, revenue open to competition would increase from 50 to 84 percent. This compares with the Council's package where the revenue exposed to competition would be 93 percent, albeit phased in over a shorter time-frame. The main difference lies in the targeting by the Council of deregulation of services where competition would provide the greatest benefits to the community and the least threat to the universal service obligation.

Consultant work for this review by Arthur Andersen suggested that even under a 'worst case' scenario for Australia Post, the Corporation would earn at or around a commercial rate of return on assets for its type of business until at least 2005. This 'worst case' scenario assumed full deregulation of letter services, no increase in prices, retention of the USO without compensation, no growth in the market as a result of increased competition, no additional cost-cutting, productivity or marketing measures and the retention of existing capital expenditure plans.

The funding methods for CSO costs as recommended by this review would ensure the continuation of Australia Post's viability and its universal service obligation.

Impact on the postal services industry

The Council considered that the industry would be likely to develop two distinct types of service provider. The first type would compete head-to-head with Australia Post, offering a full delivery service, albeit with different products and over geographic areas ranging from local to near-nationwide networks. The second type would provide some processing services but utilise the network services of others. Both deregulation and the access arrangements (covering CSO services and post office boxes) recommended by this report would eliminate the current competition bottlenecks in postal services.

Australia Post would be likely to remain an important participant in the market (it is capable of competing strongly and would be unlikely to sacrifice market share easily. But regardless of the market penetration of other service providers, the level, quality and prices of postal services would be more responsive to customer needs. Price competition in high-use segments of the market would be likely to be fierce, while the take-up of new technology and product diversification would be likely to increase across the board in response to different providers trying to distinguish their services from services offered by others.

Impact on customers

Australia Post argues that 45 cents offers good value for its letter service and that reducing this rate would have little impact on consumers. This may be true for individual and household consumers, but not for services to business. The use of postal services for the marketing and delivery of, and payment for, consumer products is growing rapidly. Competition in business letter services would provide a significant fillip to this activity, by increasing the range and quality of services, reducing prices and increasing the responsiveness of business to the needs of customers.

The effect of the Council's reform package on rural and remote customers would be minimal. Customers would still have access to the uniform rate of postage and the industry codes of practice would mean that there would still be mechanisms for dealing with mail redirection and return mail. However, the service charter would mean that rural and remote customers would be given greater certainty in their CSOs. Not only would the CSO be better defined, but customers would know what to expect from the postal service. The delivery of CSOs would be monitored and the results made public.

The Council's recommendations called for the funding for CSOs to be based on the services outlined in Australia Post's service charter. Even where competitors decide to provide a limited service, Australia Post would still be funded to provide the CSO at the agreed standards. This would ensure the maximum benefits from competition while guaranteeing the availability of affordable services.

The Council made several recommendations designed to address problems specific to the bush. They included: changing Australia Post's approach to community polling on service levels; abolishing the fees on private and locked bags for those receiving less than three deliveries a week; and remuneration for the work done by communities to distribute mail received in a community bag.

Impact on employment

As in telecommunications, employment in the postal service industry is likely to be closely linked to the level of activity in the market. Maintaining a healthy and growing sector will improve employment prospects.

While reform may mean that Australia Post will reduce staff numbers in the short term, growth in Australia Post's volumes as Australia Post gains its share of the market growth will counter this effect in the longer term.

In addition, there is likely to be increased employment flowing from the growth of existing service providers and new entry to the industry. This is

supported by historical evidence. Since limited deregulation in 1994, employment levels at Australia Post have been nearly static while Australian Bureau of Statistics' figures indicate total employment in the industry increased by 15 percent in the two years to 1997.

The retention of the infrastructure necessary to service the rural and remote CSO would ensure that any reduction in regional employment levels will be negligible.

Moreover, a healthy, competitive postal services industry will be better equipped to meet the challenge of competition within the broader communications market, and thus provide more stable, reliable employment.

B13.6 The Government's decision

On 16 July 1998, the Government announced its response to the Council's review.

The Government's reforms are to apply from 1 July 2000.

The key features of the response are:

- Australia Post's monopoly on domestic mail will be reduced from 250g and four times the standard letter rate to 50g and one times the standard letter rate;
- incoming international mail will be open to competition; and
- a further review will be scheduled for 2003 to assess the effects of these changes and the need for further reform.

Australia Post will continue to fund its CSOs from-cross subsidies and the uniform rate will remain at 45 cents until at least 2003. Bulk mail customers will benefit from:

- a reduction in the volume threshold;
- aggregation, which will allow smaller volume mailings to be combined to generate volumes sufficient to attract larger

discounts;

- the development of a performance monitoring system for bulk mail; and
- Australia Post and its major customers will develop a Code of Practice to improve the commercial relationship.

A Service Charter, approved by the government, will be underpinned by regulations which require Australia Post to meet specified performance standards, including delivery times and a minimum number of postal outlets. The Council also recommended that the performance of Australia Post in delivering the CSOs be independently monitored and enforced.

The Government has also agreed to put in place an access regime and arrangements to assure competitors that Australia Post is not cross-subsidising from its protected monopoly services to its services which are in competitive markets. Details of the access regime are yet to be finalised, however, it has the potential to open the way for significant competition to arise.

Both the Government's reforms and the Council's recommendations recognise the importance placed on the universal service and the uniform rate and measures are included to preserve these. The effect of the Government's approach may also be to target business mail as the segment of the market where competition is most likely to arise. Instead of opening up business mail to competitors, the Government has chosen to direct Australia Post to make the bulk mail system more accessible, to improve relations with its largest customers and to put in place an access regime. It has also removed larger letters from the Australia Post monopoly.

The Government's reforms institute the Council's recommendation to open inwards international mail to competition. Because the Government has chosen a more regulated response, it will need to put in place arrangements to protect the Australia Post monopoly on domestic mail to address the problem of domestic mail being posted overseas for delivery in Australia to bypass Australia Post.

While the Government's reforms are in many ways similar or the same as the Council's recommendations, there is a difference in approach on how to inject more competition into the postal services industry. Until the detail of the Government's approach is finalised, particularly in areas such as access, it is not possible to fully assess the likely effects of this approach and compare it to the Council's approach.

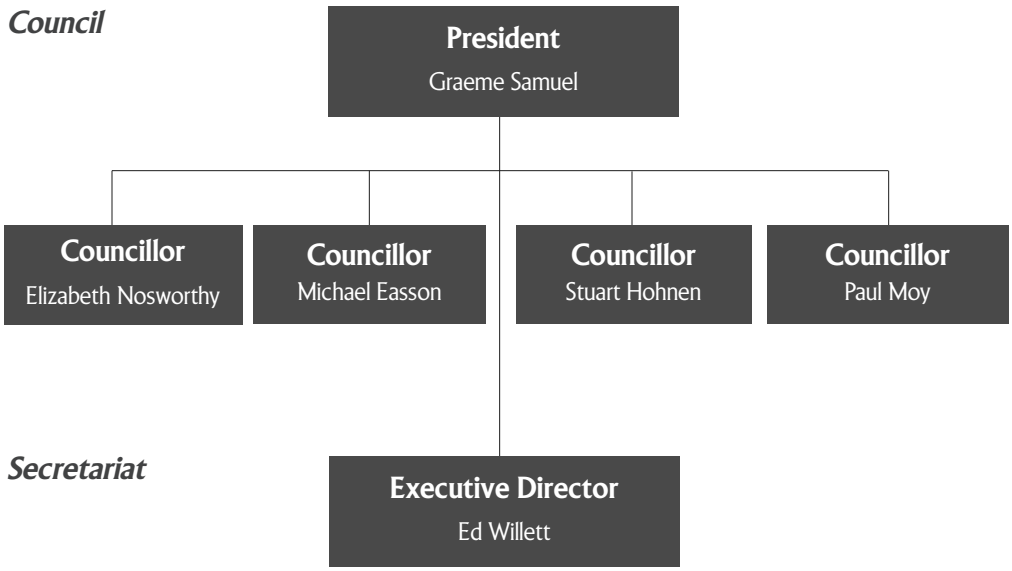
PART C CORPORATE REVIEW

C1 ORGANISATION

C1.1 Structure

The National Competition Council currently comprises four part-time Councillors, with a secretariat of 20 staff located in Melbourne. The structure of the Council at 30 June 1998 is illustrated in Figure C1.1.

Figure C1.1 National Competition Council organisation chart



C1.2 The Council

Councillors

The members of the Council are drawn from different areas of the private sector to provide a range of business skills and experience. The appointments are made jointly by the Commonwealth, State and Territory governments. The Councillors are: Graeme Samuel, President (who is resident in Melbourne); Michael Easson (Sydney); Stuart Hohnen (Perth); Elizabeth Nosworthy (Brisbane); and Paul Moy (Sydney). Each of the Councillors has been appointed for a term of three years.

Graeme Samuel

Graeme Samuel is a company director and corporate strategic consultant. He is Chairman of Opera Australia, the Inner & Eastern Health Care Network, and the Melbourne & Olympic Parks Trust, a Trustee of the Melbourne Cricket Ground Trust, a Commissioner of the Australian Football League and Director of the Docklands Authority. He is also a Director of Thakral Holdings Ltd. Mr Samuel holds a Bachelor of Laws (Melbourne) and Master of Laws (Monash).

Mr Samuel was Partner of the law firm Phillips Fox & Masel from 1972 to 1980, Executive Director of Hill Samuel Australia Ltd and subsequently Macquarie Bank Ltd from 1981 to 1986 and co-founder of Grant Samuel & Associates in 1988.

He was President of the Victorian Chamber of Commerce and Industry from 1993 to 1995, and President of the Australian Chamber of Commerce and Industry from 1995 to 1997.

Michael Easson

Michael Easson is a company director and business consultant. His current directorships include Stadium Australia 2000, ACT Electricity and Water Corporation, Australian Stationery Industries' Group, Infrastructure Trust of Australia, InTech, UNICEF Australia and York Mining.

Mr Easson's previous appointments include Adjunct Professor at the Centre for Corporate Change at the AGSM, University of NSW from 1995 to 1997, Chair of the Commonwealth Task Force on Payments to Statutory Authorities and Special Purpose Payments to States in 1995-96, Director of the NRMA Insurance Group from 1994 to 1996, Director of the NSW State Rail Authority from 1989 to 1993, Secretary of the Labor Council of NSW from 1989 to 1994, Past President of the Australian Council of Trade Unions from 1993 to 1994 and Member of the Economic Planning Advisory Commission from 1989 to 1994. Mr Easson has also been an Associate Commissioner on two Industry Commission inquiries.

Stuart Hohnen

Stuart Hohnen is a resource sector management consultant and a Director of Carnarvon Petroleum NL. He holds a Bachelor of Engineering (Hons) and a Master of Business Administration (Stanford).

Mr Hohnen's previous appointments include Chief Executive of the WA Department of Resources Development from 1982 to 1987, Executive Director of Anglo Pacific Resources PLC from 1987 to 1991 and Managing Director of the Cockburn Corporation from 1991 to 1993 and Deputy Chairman of the Gas Corporation of Western Australia (AlintaGas) from 1995 to 1998.

During 1992-93, Mr Hohnen was a member of the WA Energy Board of Review (Carnegie Review) and in 1993-94 was a member of the Energy Implementation Committee that was responsible for the restructuring of the WA energy sector.

Elizabeth Nosworthy

Elizabeth Nosworthy is a Director of Telstra Corporation Ltd and David Jones Ltd, Deputy Chairman of the Queensland Treasury Corporation, Chairman of the Port of Brisbane Corporation, Director of the Brisbane Airport Corporation Ltd, the Australian National Industries, General Property Trust Management Ltd and the Foundation of Development Cooperation Ltd and a Member of the Experts Group on Emissions Trading. She holds a Bachelor of Arts (Queensland), a Bachelor of Laws (Queensland) and a Master of Laws (London School of Economics).

Ms Nosworthy's previous appointments include a member of the Supervisory Board of General Property Trust, partner in the law firm Morris Fletcher and Cross from 1975 to 1989, and partner in the national law firm Freehill Hollingdale and Page from 1989 to 1995. During 1986-87 she was President of the Queensland Law Society.

Ms Nosworthy was a Director of the Federal Airports Corporation from 1991 to 1994. She is an ex-Chancellor of Bond University Ltd. During 1988-89, she was a member of the Companies and Securities Consultative Group appointed by the Commonwealth Attorney General.

Paul Moy

Paul Moy is a Director of Fay, Richwhite Securities Limited and Head of Investment Banking. He is also Chairman of the Funds Management Committee of the Commonwealth Innovation Investment Fund Program and a member of the Advisory Board of CRS Australia. He holds a BA Hons in Economics (Newcastle), Dip Ed (Newcastle) and PhD in Economics (James Cook).

Dr Moy has been a member of a number of public inquiries relating to competition policy and structural reform of the utility sector and has extensive experience in economics, corporate finance and public policy. He was formally a Deputy Secretary of the NSW Treasury.

Council meetings

Table C1.1 lists the meetings of the Council held during 1997-98. While the Council generally meets on a monthly basis, its workload sometimes requires more frequent meetings. During 1997-98, the Council met on a total of 13 occasions. The Council held 10 meetings in Melbourne, one in Adelaide, and two by teleconference.

Table C1.1 Council meetings 1997–98

Date of meeting
22 July
7 August
26 August
23 September
6 November
2 December
29 January
6 March
23 March
20 April
21 May
17 June
23 June

C1.3 The Secretariat

The Council is supported by a Secretariat that is located in Melbourne and provides advice and analysis at the Council's direction on matters related to the implementation of NCP. It represents the Council in dealings with Commonwealth, State and Territory government officials, other parties with interests in competition policy matters, and on several intergovernmental committees dealing with competition issues including the Gas Reform Implementation Group and the SCARM Task Force on Water Reform. Senior Secretariat staff also present conference papers on issues related to the Council's work program.

Overview of staffing developments

The number of Secretariat staff employed by the Council in 1997-98 remained relatively constant at around 20. At June 30 1998, the staff comprised the Executive Director, 16 research/policy officers and three administrative staff.

The Council is a small organisation that covers a diverse range of issues. It was always intended that it would draw on the expertise of people in other organisations. As well as engaging consultants, sometimes under contract to work within the Council offices, the Council has seconded officers to work on specific projects. Two temporary officers were employed to work on the review of postal services, one officer from the Commonwealth Treasury has been seconded to work on electricity reform issues, while another from the ACCC has been seconded to work on rail access issues. An officer has also been seconded for 12 months from a private law firm to work on access issues and the review of section 51(2) and 51(3) of the *Trade Practices Act*.

The majority of Secretariat staff are employed under the *Public Service Act* 1922 and located in Melbourne. Two officers have been employed on contract. The Council has no inoperative staff. Information on staff profiles is provided in Tables C1.2 and C1.3 below.

Table C1.2 Staff profile, 30 June 1998

Remuneration Level	Female	Male	Total
Senior Executive Service Band 2	0	1	1
Senior Executive Service Band 1	1	0	1
Senior Officer Grade A	1	1	2
Senior Officer Grade B	1	1	2
Senior Officer Grade C	3	5	8
Administrative Service Officer Grade 6	1	2	3
Administrative Service Officer Grade 5	0	1	1
Administrative Service Officer Grade 4	0	0	0
Administrative Service Officer Grade 3	1	0	1
Administrative Service Officer Grade 2	0	0	0
Administrative Service Officer Grade 1	1	0	1
Total	**9**	**11**	**20**

Table C1.3 Staff by employment status, 30 June 1998

Level	Female	Male	Total
Full-time permanent	7	8	15
Full-time temporary	1	2	3
Part-time staff	1	1	2
Total	**9**	**11**	**20**

Senior Executive Service information

In response to the build up in responsibility, staff and workload of the Council, as discussed in the 1996-97 Annual Report, the number of Senior Executive Service positions in the Council was increased to two, the Executive Director and the Deputy Executive Director. The Executive Director position is at the SES2 level and the Deputy Executive Director at SES1.

Consultants

The Council utilised the services of consultants in 1997-98 where it considered it was efficient and cost-effective to do so. Table C1.4 lists the number and value of consultancies engaged. Some of these projects are ongoing so that the total cost will not be paid until 1998-99. The value of consultants engaged in 1996-97, but paid in 1997-98, was $399 291

Table C1.4 Summary of consultants engaged, 1997-98

Purpose	Number	Contract amount ($)
Legal advice	10	47 958
Economic Advice	1	21 458
Publications and corporate services	5	83 450
Postal services review	1	3 200
Total	**17**	**156 066**

C2 FUNCTIONS

The Council has statutory responsibilities under both the TPA and the Prices Surveillance Act to make recommendations to relevant governments on:

- access to significant infrastructure services; and
- whether State and Territory government businesses should be subject to prices surveillance by the ACCC.

Apart from these statutory responsibilities, the three NCP agreements establish a role for the Council in the following areas:

- advice to the Commonwealth when considering overriding State or Territory exceptions from the TPA;
- advice on the progress made against the National Competition Policy Agreements; and
- other work on competition policy as agreed by a majority of the stakeholder governments. Some potential work program items are outlined in the CPA, including prices oversight of government business enterprises (subclause 2(2)), implementation of competitive neutrality principles (subclause 3(3)), structural reform of public monopolies (subclause 4(4)), and a review of legislation which restricts competition where the review has a national dimension (subclause 5(8)).

The Council also has an implied function of supporting the NCP process and appropriate reform more generally. This is reflected in its mission statement:

> To help raise the living standards of the Australian community by ensuring that conditions for competition prevail throughout the economy that promote growth, innovation and productivity.

It is also reflected in the Council's goals set out in Box C2.1.

The various functions and responsibilities of the Council are delivered through its work program areas. These are set out in Box C2.2.

Box C2.1 The Council's goals

- Facilitating timely implementation of effective and fair competition reforms by governments.
- Promoting better use of Australia's infrastructure.
- Building community awareness and support of National Competition Policy.
- Ensuring that the National Competition Council is a dynamic organisation, capable of providing a safe, healthy and professional work environment for its staff and developing their full potential.

Box C2.2 The Council's workprogram

- Facilitation and assessment of government's progress in implementing competition policy reforms.
- Provision of recommendations to governments on access to infrastructure.
- Undertaking work allocated to the Council's work program by governments.
- Ongoing improvement of the Council's operational standards in leadership, strategic direction, information systems support services, resource allocation and staff development.
- Promotion of community understanding of National Competition Policy.

More information about the Council's statutory and other responsibilities, and the Council's actions in relation to them over the past year, is presented in the following areas of this report:

- Chapter A3 presents an overview of what the Council has done to discharge each of its functions during 1997-98, and outlines the task ahead;
- Chapter A1 provides an overview of the NCP reforms and progress in implementing them. Chapters B1 to B10 and Chapter B12 explain these matters in more detail;
- Chapter B12 also outlines the Council's responsibilities regarding Part IIIA and discusses what the Council has done to discharge them over the last year; and
- Sections B2.2 and B6.2 presents more detail on the Council's responsibilities in relation to Section 51 exceptions and prices surveillance, and discusses relevant activity over the last year.

C3 MANAGEMENT

C3.1 Staff development and management

Training

Excluding salary costs of staff undertaking training, a total of $34 837, representing 2.6 percent of the Secretariat's salary costs, was devoted to staff training for 1997-98. All Secretariat staff received some training this year.

In-house training for all staff was held in occupational health and safety, stress management, Administrative Law and negotiating a Certified Agreement. In addition, eleven Secretariat staff spent 36 days in other training programs during the year. Nine staff participated in a variety of training programs in areas such as financial management, skills development, and professional development. In addition, nine Secretariat staff attended conferences on issues associated with competition policy and its implementation. Four officers are currently receiving assistance to undertake further tertiary education.

Industrial democracy

Industrial democracy plan

The Council's draft *Industrial Democracy Plan* was the basis of its industrial democracy practices during the year. This draft will be reviewed in 1998-99 to ensure it is meeting the needs of the Council and its staff. The Council's Deputy Executive Director will have formal responsibility for the implementation of industrial democracy principles and practices.

Consultative mechanisms

The Secretariat Executive, which includes the Executive Director, Deputy Executive Director and the two Section Heads, meets weekly. Minutes of these meetings are circulated to all staff. Section meetings are held to provide feedback and input into the Executive.

All staff meet weekly to review the work being conducted by the Secretatiat. After the monthly Council meetings this weekly meeting is extended to cover a broader range of issues. These staff meetings are the principal fora for informing Secretariat staff of Council decisions and inviting staff consideration of issues currently facing the Council. Proposed changes to research priorities, staffing arrangements, accommodation, office policies, information technology issues and training are discussed at these regular meetings. During 1997-98, all Secretariat staff participated in decision making regarding information technology requirements (including training), corporate planning and the process for negotiating a certified agreement.

Occupational health and safety

During 1997-98, the Council undertook or continued the following initiatives to ensure the health and safety of its staff and contractors:

- participation in Occupational Health and Safety (OHS) training;
- establishment of an OHS committee, including an elected health and safety representative;
- minutes of the meetings of the OHS committee are circulated to all staff;
- encouragement of staff participation in lunch-time and after-hours exercise programs;
- two-yearly eyesight testing for screen-based equipment users;
- appointment of fire wardens and fire safety training;
- the appointment of trained First Aid Officer;
- advice on ergonomic furniture usage and posture;

- purchase of ergonomic equipment where appropriate;
- training in stress management; and
- establishment of an Employee Assistance Scheme, providing confidential counseling to staff. A seminar was held to explain the operation of the scheme to staff.

The Council received no accident/incident reports during 1997-98. There were no notices lodged or directions given to the Council under sections 30, 45, 46 or 47 of the *Occupational Health and Safety (Commonwealth Employment)* Act 1991 during the year.

Comcare conducted a Workplace Investigation covering occupational health and safety policies and practices. This report reached the following conclusion.

> Overall, and given the generally low level of risk to the health and safety of employees, the National Competition Council (NCC) was assessed as satisfactory. While recognising the existence and effectiveness of informal systems and procedures in a small office environment, some details need attention and these are addressed in the attached assessment tables. The Primary Recommendations identify areas that will bring about the greatest improvement in performance as measured by this assessment method.

The Council has responded to Comcare by outlining the methods it will be using to implement those changes identified in the report.

C3.2 Equity matters

Social justice

Within its work program, the Council addresses social justice issues in three main contexts.

First, in conducting its functions in relation to the National Access Regime, the Council must consider public interest issues. Matters that the Council may consider include, although are not limited to, the following:

- policies concerning occupational health and safety, industrial relations, access to justice and other government services, and equity in the treatment of different persons;
- economic and regional development, including employment and investment growth; and
- the interests of consumers generally, or a class of consumers.

Second, as part of its role of assessing jurisdictions' progress in implementing the NCP reforms, the Council must consider the extent to which governments have undertaken bona fide reform processes. Chapter B3 discusses the Council's views on good review processes. The NCP agreements allow governments to take into account all of the costs and benefits of reform options including social, environmental and economic considerations. The agreements implicitly recognise that social justice considerations can warrant restrictions on competition, although it also calls for an examination of whether the social justice objectives can be met through ways which do not restrict competition. At the same time, the NCP agreements recognise that many restrictions, by advantaging specific groups at a cost to the broader community, promote neither social justice nor economic efficiency.

Third, where it conducts reviews under the NCP principles, the Council is also required to consider social justice issues. Chapter B13 outlines the Council's approach to its review of the *Australian Postal Corporation Act*. In that review the main focus of the Council's considerations was directed at

how Australia Post's social responsibilities can be maintained and strengthened, while still maximising the benefits from competition.

The Council has released a paper on *Considering the public interest under the NCP* in November 1996. This paper is available on the Council's web site. Chapter A2 of this report discusses further the interface between social objectives and the NCP reforms.

Access

Since its inception in November 1995, the Council has instituted open and transparent processes. For example, declaration and certification applications for third party access to essential facilities explicitly provide interested parties the opportunity to have their views considered by the Council, including through meetings with members of the Secretariat. The Council also used a public process to provide input into its review of *Australian Postal Corporation Act* the details of this process are discussed in Chapter B13. The Secretariat and members of the Council have met with representatives of local governments, community groups and the private sector on many competition policy matters during the year.

The Council has released publications designed to assist community understanding of its role and functions:

- *The National Access Regime: a draft guide to Part IIIA of the TPA* (August 1996);
- *Annual Report 1995-96* (August 1996);
- *Considering the Public Interest Under the NCP* (November 1996);
- *Competitive Neutrality Reform: Issues in Implementing Clause 3 of the CPA* (January 1997);
- *Compendium of NCP Policy Agreements* (January 1997);
- *Legislation Review Compendium* (April 1997);
- *Assessment of State and Territory Progress with Implementing National Competition Policy and Related Reforms* (June 1997);

- *Annual Report 1996-97* (August 1997);
- *Review of the Australian Postal Corporation Act, Options Paper* (September 1997); and
- *Review of the Australian Postal Corporation Act, Final Report, Volume 1 and Volume 2* (February 1998).

The Council also commenced distribution of a monthly newsletter that has a circulation of over 2000 copies and provides information on the status of current projects and articles on topics of interest.

In response to the specific needs of small business, the Council developed and distributed a plain English kit called *Competition Policy: what it means for small business*.

A web site was established at www.ncc.gov.au in 1997-98. This site contains all of the Council's publications and information on applications under Part IIIA of the *Trade Practices Act* and other reviews conducted by the Council.

Workplace diversity

The Council adopted the Commonwealth Department of Treasury's *Equal Employment Opportunity (EEO) Program* as its guide in this area. It is currently developing its own Strategy under the new Workplace Diversity guidelines.

A member of the Council Executive was allocated responsibility for EEO during 1997-98.

All recruitment conducted during 1997-98 included a selection criterion relating to understanding of the principles and practical effects of policies on EEO. Selection panels included at least one male and one female. At 30 June 1998, 11 Secretariat staff were members of an EEO group (see Table C3.1).

Table C3.1 Staff by EEO group, 30 June 1998

Level	Female	NESB 1[a]	NESB 2[a]	A&TSI[b]	Disabilities
Senior Executive	1				
Senior Officer Grades A-C	5				
Administrative Service Officer Grades 1–6	3	2			
Total	**9**	**2**			

a Non-English speaking background (first and second generation)
b Aboriginal and Torres Strait Islanders

The Council has identified and trained contact officers for both EEO and sexual harassment issues, and is examining further strategies to meet its specific needs as a small organisation.

There were no reported cases of workplace harassment during 1997-98.

C3.3 Internal and external scrutiny

During 1997-98:

- the Council did not undertake any internal reviews of its processes;
- there were no cases of fraud involving the Council; and
- there were no comments by the Ombudsman, or decisions by the courts or administrative tribunals on matters involving the Council.

There have been a number of appeals to the Australian Competition Tribunal against decisions made by the Treasurer or a Premier in response to

recommendations by the Council on applications for access to infrastructure services. The appeals have come from infrastructure owners, when the decision was to declare services, and applicants, when the decision was not to declare. Appeals have occurred when the decision maker has agreed with the Council's decision and when he has disagreed. Chapter B12 includes a full discussion of the status of appeals.

There are three Commonwealth Parliamentary Committees that have either completed reports that look at aspects of National Competition Policy or are commencing work on NCP issues.

In June 1998 the House of Representatives Standing Committee on Financial Institutions and Public Administration produced a report on a *Review of the National Competition Council Annual Report 1996-97*. This report included one recommendation.

> That the Commonwealth, State and Territory Governments and agencies involved in the implementation of national competition policy devote resources to ensure community understanding and debate about the contents of the policy and its outcomes.

The Report also concluded that:

> The NCC has made an encouraging start so far with its limited resources. The task however is becoming more challenging as possible difficult decisions on competition payments may have to be made; as the real work of the reforms begin, some in more politically sensitive areas; and as community questioning about the benefits and implications of reforms become more prominent particularly in the absence of jurisdictional rigour in selling the reforms. It is critical that the NCC's (and other competition agencies') public education role be improved. The Committee will continue to monitor the NCC's progress in this increasingly more difficult task.

In addition to identifying a need for more communication and community education the Committee's report also discussed the Council's approaches on assessing the implementation of reform, the review of the *Australian Postal Corporation Act*, the implementation of reform by local government and the Council's roles in advising governments and assessing the implementation of reform.

For some time the Council has recognised the need to provide accessible information on NCP, the benefits of reform and the role of the Council. With this in mind it has continued to produce a newsletter which discusses NCP issues, made as much of its work as possible available on its web site and increased the frequency and range of groups it meets with.

The Council, however, is a relatively small organisation that is only one part of the NCP process. It has recognised the need to increase its own communication effort and to encourage others to do likewise.

In response to the Committee's recommendation the Council is planning the following action:

- increasing its own efforts to meet and discuss NCP with a broad range of community and interest groups.
- preparing several plain English pamphlets designed to quickly explain aspects of NCP.
- undertaking work to encourage governments to both fund and increase their focus on work to explain and promote the benefits of NCP.

In June 1998 the Joint Committee of Public Accounts and Audit produced a report on *General and Specific Purpose Payments to the States*. This report contained some discussion of the National Competition Payments that the Commonwealth makes to State and Territory Governments after considering a recommendation from the National Competition Council. The primary purpose of this report was to consider the merits of conditional General Purpose Payments as a method of providing Commonwealth Grants to States and Territories. The Committee did, however, make some comments on the operation of the Council. These included:

- The Committee supports the recent efforts of the NCC to improve consultative arrangements with interested organisations in the community.
- It seems to the Committee that the NCC adopted a reasonable, commonsense approach in exercising flexibility and discretion in its assessment of State/Territory compliance. Its approach was consistent with the cooperative framework for national competition policy reform implementation.

- The Committee considers that the NCC had a structured and transparent assessment process that provided natural justice to the parties affected by its recommendations.
- The Committee sees merit in the Commonwealth and the State commissioning an external review of competition policy, independent of the key competition policy institutions – the ACCC, the NCC and the Australian Competition Tribunal.
- The Committee supports the proposal for an independent review of the NCC, but believes that the timing of the review warrants careful consideration. The Committee recommended bringing the review of the NCC forward to the first half of 2000.

On 1 July 1998, the Senate established a Select committee to report on the socio-economic consequences of National Competition Policy. The Terms of Reference require the review to look at the impact of competition policy on unemployment, changed working conditions, social welfare, equity, social dislocation and environmental impacts, including the differences between urban and rural communities and clarification of the public interest test.

The Committee is to report before the first sitting day in 1999. It has called for submissions, which close on 15 September 1998. The Council will participate fully in this review including preparing a public submission.

Beyond this, the Council is subject to external scrutiny through the publication of its recommendations to all governments on matters relating to access determinations and competition reforms, external publications and other work that may be placed on the work program from time to time.

C3.4 Other matters

Freedom of information

The Council received no requests for documents under the *Freedom of Information Ac*t during 1997-98.

The following information is provided in accordance with subsection 8(1) of the *Freedom of Information (FOI) Act* 1982.

Organisation of the Council

Details of the Council's organisational structure, role and functions are detailed in Appendices C1 and C2, Chapter A3 and elsewhere in this report.

Arrangements for outside participation

Persons or organisations outside the Council are encouraged to participate in the formulation of Council advice on access declarations, competition reform or other work program matters, by making representations in person or in writing to the Council.

Categories of documents held by the Council

The Council Secretariat holds the following three classes of documents.

First, it holds representations to the Council President and Executive Director. The Council receives correspondence covering a number of aspects of government micro-economic policy and administration.

Second, it holds policy and administration files relevant to the Council's responsibilities. The documents on these files include correspondence,

analysis and policy advice prepared by Secretariat officers. There are three main categories of working files:

- Council views on matters relating to competition reform implemented by Commonwealth, State and Territory governments;
- Council recommendations on applications for access declarations and certification of access regimes. The designated Ministers are required to publish their decisions on these applications. The Ministers must give reasons for the decision and provide a copy of the Council's recommendation to the service provider and the applicant. The Council makes its recommendations and reasons publicly available after the designated Minister has published a decision. If the designated Minister does not make a decision, the Council will publish its recommendation 60 days after it provided it to the Minister; and
- Material relating to other work assigned to the Council: for example, the review of the Australian Postal Corporation Act and the review of Sections 51(2) and 51(3) of the Trade Practices Act.

Third, the Council Secretariat holds documents on internal office administration. These include a broad range of documents relating to the personal details of staff and to the organisation and operation of the Council. These documents include personal records, organisation and staffing records, financial and expenditure records, and internal operating documentation such as office procedures and instructions.

Documents open to public access subject to a fee or available free of charge upon request

The following categories of documents are publicly available:

- the Council's Annual Reports to Parliament;
- speeches presented by Council and Secretariat staff;
- discussion papers and guides on specific competition policy issues;
- newsletter discussing competition policy issues;

- corporate plan;
- declaration or certification applications, and issues papers developed by the Council in response to access declaration or certification applications or other reviews;
- submissions made by interested parties on access declaration or certification applications, or other reviews, where information contained is not commercial-in-confidence; and
- the Council's recommendations on declaration and certification applications.

These documents are available from various sources. The Council has as much material as possible available on its web site – www.ncc.gov.au. Most publications are available through the Commonwealth Government bookshops. Other documents, publications and speeches are available by contacting the Council directly.

In 1997-98, Council and Secretariat staff presented the following conference papers, which are publicly available:

- Graeme Samuel, Changes on the Horizon – Challenges for Business and Commerce, presented to Institute of Chartered Accountants, 16 July 1997.
- Ed Willett, Public Interest in the National Competition Policy, presented to the University of NSW – Public Sector Research Centre, 24 July 1997.
- Graeme Samuel, Defining a Competitive Industry Policy, presented to ACCI National Industry Policy Conference, Brisbane, 15 August 1997.
- Graeme Samuel, Industry Policy, Competition and the Broader Reform Agenda, presented to the Australian Institute of Banking & Finance, Melbourne, 20 August 1997.
- Graeme Samuel, Australia's Competition Policy – Where is it and What Does it Mean for the General Insurance Industry?, presented to the Insurance Council of Australia, Canberra, 28 August 1997.

- Steven Ross, The Impact of Competition Policy Reform on Future Infrastructure Development, presented to IMR: Australian Infrastructure Forum, 28 August 1997.
- Ed Willett, The Council's review of the Postal Industry, presented to the Post Office Agents Association Ltd – 1997 National Conference, Hobart, 30 August 1997.
- Graeme Samuel, Competition: The Law, Business and Football, presented to the Law Society of South Australia, Adelaide, 2 September 1997.
- Graeme Samuel, Australia's Competition Policy – Where is it and What Does it Mean for the Property Industry?, presented to the Property Council of Australia, Melbourne, 4 September 1997.
- Trish Lynton, Coal Rail Freight, presented to IIR Conference, 22 September 1997.
- Graeme Samuel, Industry Policy: Strategic Direction or Business Welfare?, presented to CEDA Canberra Connection, Canberra, 25 September, 1997.
- Graeme Samuel, Trade Liberalisation, presented to Conference of Economists '97, Hobart, 30 September 1997.
- Ed Willett, Update on National Competition Policy, presented at IIR Conference, 8 October 1997.
- Deborah Cope, NCC Review of the Australian Postal Corporation Act, presented to Major Mail Users of Australia Conference, 9 October 1997.
- Graeme Samuel, Competition – How Far, How Controlled, presented to the National Public Sector Accountants Conference, Sydney, 20 October 1997.
- Ross Campbell, The Application of Third Party Access to Water Infrastructure, presented to AIC Conferences – 1997 Australian Water Summit, 20 October 1997.
- Graeme Samuel, Backsliding from Trade Liberalisation Commitments, presented to National Centre for Development Studies,ANU, Canberra, 24 October 1997.
- Ross Campbell, Competition in Health – Seminar, presented to Private Doctors of Australia, 1 November 1997.

- Ed Willett, Discussion Forum on Gas, Australian Pipeline Industry Association, 4 November 1997.
- Graeme Samuel, The Implications of National Competition Policy for the Professions, presented to the Australian Council of Professions, Canberra, 17 November 1997.
- Graeme Samuel, Leadership in Business and Government – Keeping Reform on Track, presented to the Louis Vuitton Business Sunday Awards, Sydney, 24 November 1997.
- Graeme Samuel, Leadership in Business and Government – Keeping Reform on Track, presented to the Baker and McKenzie Solicitors, Melbourne, 4 December 1997.
- Graeme Samuel, Politics and Public Policy Review, presented at 1998 Politics and Public Policy Review Conference (The Centre for Corporate Public Affairs), 5 February 1998.
- Graeme Samuel, The Challenges Facing Governments and the Council, presented to the New Market Culture Conference, Melbourne, 16 February 1998.
- Ed Willett, National Competition Policy, presented to the Competition Law Conference, 4 and 27 February 1998.
- Deborah Cope, Review of Postal Services, presented to Major Mail Users, 17 March 1998.
- Graeme Samuel, Access Regimes and Competition Policy Considerations, The Australia National Infrastructure Forum (The Economist Group), 17 March 1998.
- Graeme Samuel, Competition Policy and The Energy Industry, presented to Energy in WA Conference, Perth, 18 March 1998.
- Graeme Samuel, The Asian Turmoil and Lessons for Australian Business, Coopers and Lybrand, 19 March 1998.
- Ed Willett, Competition policy and the Energy Industry, presented at National Energy Industry Conference, 20 March 1998.
- Deborah Cope, National Competition Policy: rationale, scope and progress, and some implications for the ACT and the role of government, presented to ACT Department of Urban Services, 20 March 1998.

- Graeme Samuel, Keeping Reform on Track, presented to The CEO Circle, 24 March 1998.
- Graeme Samuel, Leadership in Business and Government – Keeping reform on Track, presented to CEDA Gold Series Dinner, Royal Exchange of Sydney, 26 March 1998.
- Ed Willett, NCP and Water Reform in Australia, presented to a Delegation of World Bank officials on Water Reform, Canberra, 15 April 1998.
- Graeme Samuel, Laying the Foundations for a More Productive Business Environment: some issues in competition reform, presented to Property Council of Australia, Adelaide, 21 April 1998.
- Graeme Samuel, Swinburne Speech to Business Graduates, 13 May 1998.
- Stuart Hohnen, National Competition Policy – Issues and Progress, presented to the Australian Society of Certified Practising Accountants, Perth, 13 May 1998.
- Jane Brockington, National Competition Policy and the Nursing Profession, presented to Australian Nursing Council, 20 May 1998.
- Graeme Samuel, National Competition Policy: being more competitive in an increasingly competitive marketplace, presented to Knox Rotary Club, 20 May 1998.
- Graeme Samuel, The Practical Operation and Implications of National Competition Policy in Australia, presented at Queensland 400 Conference, 29 May 1998.
- Graeme Samuel, The Progress of National Competition Policy Reform and its Implications for Retailing, presented to Australian Retailers Association Forum, 30 May 1998.
- Graeme Samuel, Progress on Reform Measures, presented to Master Builders Association, 16 June 1998.
- Stuart Hohnen, National Competition Policy: An Overview, presented to the Ministry of Fair Trading, Western Australia: Public Information Forum, Perth, 22 June 1 998.

- Ed Willett, The NCC and its Role in the Assessment of Progress in Water Reform, presented to AIC Conference – Australian Water, 23 June 1998.
- Graeme Samuel, National Competition Policy: fact and fiction, presented at Queensland Retailers Association, Brisbane, 30 June 1998.

In 1997-98, the following documents were also publicly release:

- Annual Report 1996-97 (August 1997);
- Specialized Container Transport Applications for Declaration of a Rail Service and Freight Support Services provided by Westrail: Issues Paper (August 1997);
- Review of the Australian Postal Corporation Act: Options Paper (September 1997);
- NSW Minerals Council Limited's application for declaration of a rail service provided by NSW Rail Access Corporation: Recommendation (September 1997);
- Specialized Container Transport Applications for Declaration of Services provided by Westrail: Recommendations (November 1997);
- Review of the Australian Postal Corporation Act, Final Report, Volume 1 and Volume 2 (February 1998);
- Application for Certification of the NSW Rail Access Regime: Draft Recommendation (April 1998);
- South Australian Access Regime for Gas Pipeline Services: Issues Paper (May 1998);
- The Queensland Access Regime for Rail Services: Issues Paper (June 1998).
- *NCC Update* newsletter, eight editions.

Facilities for access to Council documents

Applicants seeking access under the Freedom Of Information (FOI) Act to documents in the possession of the Council should apply in writing to:

Deputy Executive Director
National Competition Council
Level 12, Casselden Place
2 Lonsdale Street
MELBOURNE VIC 3000
Attention: Freedom of Information Coordinator

An application fee of $30 must accompany requests. Unless an application fee is received, or explicit waiver given, the request will not be processed. Telephone enquiries should be directed to the FOI Coordinator, telephone (03) 285 7484 between 9.00 am and 5.00 pm.

The Deputy Executive Director is authorised under section 23 of the FOI Act to make decisions to grant or refuse requests for access to documents. In accordance with Section 54 of the FOI Act, an applicant may apply to the Executive Director within 28 days of receiving notification of a decision under the Act, seeking an internal review of a decision to refuse a request. The application should be accompanied by a $40 application review fee as provided for in the FOI Act.

If access under the FOI Act is granted, the Council will provide copies of documents after receiving payment of all applicable charges. Alternatively, applicants may make arrangements to inspect documents at the National Competition Council office, Level 12, Casselden Place, 2 Lonsdale Street, Melbourne between 9.00 am and 5.00 pm, Monday to Friday.

Advertising and market research

The Council did not engage any advertising or market research agencies in 1997-98.

Annual reporting requirements and aids to access

Information contained in this annual report is provided in accordance with:

- Section 74 of the Occupational Health and Safety (Commonwealth Employment) Act 1991;
- Section 50AA of the *Audit Act 1901*;
- Section 8 of the *Freedom of Information Act 1982*;
- Section 29(O) of the *Trade Practices Act 1974*; and
- the guidelines issued by the Department of the Prime Minister and Cabinet.

A compliance index is provided overleaf.

The contact officer for inquiries or comments concerning this report, and for inquiries about any Council publications, is:

Deputy Executive Director
National Competition Council
Level 12, Casselden Place
2 Lonsdale Street
MELBOURNE VIC 3000
Telephone (03) 9285 7474
Facsimile (03) 9285 7477

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C4 FINANCIAL STATEMENTS

Financial statements
for the year ended 30 June 1998

Australian National Audit Office

INDEPENDENT AUDIT REPORT

To the Treasurer

Scope

I have audited the financial statements of the National Competition Council for the year ended 30 June 1998. The financial statements comprise:

- Statement by the Council President
- Agency statements of:
  - Revenues and Expenses
  - Assets and Liabilities
  - Cash Flows
- Schedule of Commitments
- Schedule of Contingencies, and
- Notes to and forming part of the Financial Statements.

The Council's President is responsible for the preparation and presentation of the financial statements and the information they contain. I have conducted an independent audit of the financial statements in order to express an opinion on them to you, the Treasurer.

The audit has been conducted in accordance with the Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards, to provide reasonable assurance as to whether the financial statements are free of material misstatement. Audit procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with Australian Accounting Standards, other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) and statutory requirements so as to present a view of the Council which is consistent with my understanding of its financial position, its operations and its cash flows.

The audit opinion expressed in this report has been formed on the above basis.

Audit Opinion

In my opinion,

(i) the financial statements have been prepared in accordance with Schedule 2 of the Finance Minister's Orders, and

(ii) the financial statements give a true and fair view, in accordance with applicable Accounting Standards, other mandatory professional reporting requirements and Schedule 2 of the Finance Minister's Orders, of the financial position of the National Competition Council as at 30 June 1998 and the results of its operations and its cash flows for the year then ended.

Australian National Audit Office

B.A. Kaufmann
Executive Director
Delegate of the Auditor-General

Melbourne
28 August 1998

GPO Box 1776P Melbourne VIC 3001
626 Bourke Street
MELBOURNE VIC
Phone (03) 9607 4444 Fax (03) 9600 1518

National Competition Council
Casselden Place Level 12 2 Lonsdale Street Melbourne 3000 Australia
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Office of
Council President

STATEMENT BY THE COUNCIL PRESIDENT

In my opinion the attached financial statements for the financial year 1 July 1997 to 30 June 1998 give a true and fair view of the matters required by Schedule 2 to the Finance Minister's Orders made under section 63 of the *Financial Management and Accountability Act 1997.*

Signed .....

Mr Graeme Samuel

President

Date 23/8/98

NATIONAL COMPETITION COUNCIL
AGENCY REVENUES AND EXPENSES

for the year ended 30 June 1998

	Notes	1997-98 $	1996-97 $
NET COST OF SERVICES			
Expenses			
Employees	3	**1,593,403**	1,038,270
Suppliers	4	**1,317,961**	969,455
Depreciation and amortisation	5	**99,926**	87,332
Net losses from sale of assets	6	**2,181**	-
Write-down of asset	7	**6,179**	-
Total expenses		**3,019,650**	**2,095,057**
Revenues from independent sources			
Sale of goods and services		**12,468**	1,835
Other revenues from independent sources		**452**	566
Total revenues from independent sources		**12,920**	2,401
Net cost of services		**3,006,730**	**2,092,656**
REVENUES FROM GOVERNMENT			
Appropriations used for:			
Ordinary annual services (net appropriations)		**2,948,187**	1,732,000
Resources received free of charge		**24,025**	21,000
Total revenues from government		**2,972,212**	**1,753,000**
Operating (deficit)/surplus		**(34,518)**	**(339,656)**
Accumulated results at 1 July		**126,352**	259,008
Change in accounting policy	2.7	**-**	207,000
Accumulated results at 30 June		**91,834**	**126,352**

The above Statement should be read in conjunction with the accompanying notes

NATIONAL COMPETITION COUNCIL
AGENCY ASSETS AND LIABILITIES

as at 30 June 1998

	Notes	30/6/98 $	30/6/97 $
PROVISIONS AND PAYABLES			
Employees	8	**366,487**	264,936
Suppliers	9	**53,420**	64,290
Other	10	**14,286**	50,751
Total provisions and payables		**434,193**	379,977
EQUITY			
Accumulated results	11	**91,834**	126,352
Total equity		**91,834**	126,352
Total liabilities and equity		**526,027**	506,329
FINANCIAL ASSETS			
Cash	500	**2,000**	
Receivables	12	**157,694**	31,040
Total financial assets		**158,194**	33,040
NON-FINANCIAL ASSETS			
Land and buildings	13,14	**195,409**	195,190
Plant and equipment	13,14	**143,276**	152,478
Inventories - held for sale		**6,453**	7,087
Other - prepayments		**22,695**	118,534
Total non-financial assets		**367,833**	473,289
Total assets		**526,027**	506,329
Current liabilities		**310,289**	255,462
Non-current liabilities		**150,422**	124,515
Current assets		**187,342**	154,052
Non-current assets		**338,685**	352,277

The above Statement should be read in conjunction with the accompanying notes

NATIONAL COMPETITION COUNCIL
AGENCY CASH FLOWS

for the year ended 30 June 1998

	Notes	**1997-98** **$**	1996-97 $
OPERATING ACTIVITIES			
Cash received			
Appropriations		**2,827,309**	1,908,878
Other		**452**	948
Total cash received		**2,827,761**	1,909,826
Cash used			
Employees		**1,461,211**	973,993
Suppliers		**1,274,926**	861,783
Total cash used		**2,736,137**	1,835,776
Net cash from operating activities	15	**91,624**	74,050
INVESTING ACTIVITIES			
Cash received			
Proceeds from sale of property, plant & equipment		**2,700**	-
Total cash received		**2,700**	-
Cash used			
Purchase of property, plant and equipment		**95,824**	72,057
Total cash used		**95,824**	72,057
Net cash used by investing activities		**(93,124)**	(72,057)
Net (decrease)/increase in cash held		**(1,500)**	1,993
add cash at 1 July		**2,000**	7
Cash at 30 June		**500**	2,000

The above Statement should be read in conjunction with the accompanying notes

NATIONAL COMPETITION COUNCIL
SCHEDULE OF COMMITMENTS

as at 30 June 1998

	Agency	
	1998	1997
	$	$
BY TYPE		
OTHER COMMITMENTS		
Operating leases	**591,796**	157,701
Total other commitments	**591,796**	**157,701**
COMMITMENTS RECEIVABLE	**-**	-
Net commitments	**591,796**	**157,701**
BY MATURITY		
One year or less	**136,338**	118,819
From one to two years	**136,638**	38,882
From two to five years	**318,820**	-
Net commitments	**591,796**	**157,701**

The above Statement should be read in conjunction with the accompanying notes

NATIONAL COMPETITION COUNCIL
SCHEDULE OF CONTINGENCIES

as at 30 June 1998

	Agency	
	1998	1997
	$	$
	NIL	NIL

The Council is not exposed to any contingent liabilities.

The above Statement should be read in conjunction with the accompanying notes

NATIONAL COMPETITION COUNCIL
Notes to and forming part of the Financial Statements
for the year ended 30 June 1998

Note 1 Aim and Objectives of the National Competition Council

The National Competition Council (the 'Council') was established on 6 November 1995 by the *Competition Policy Reform Act 1995* following agreement by the Commonwealth, State and Territory governments.

The Council is an independent advisory body for all governments involved in implementing the competition reforms. The Council's aim is to help raise the living standards of the Australian community by ensuring that conditions for competition prevail throughout the economy which promote growth, innovation and productivity.

The Council's program objectives are:

- to promote micro-economic reform within the community, including by undertaking research and providing advice to governments on competition policy matters;
- to recommend on applications for declaration of access to services provided by nationally significant infrastructure and the certification of access regimes under Part IIA of the Trade Practices Act;
- to assess progress with agreed competition policy reforms, and to recommend to the Commonwealth prior to July 1997, July 1999 and July 2001 whether the conditions for National Competition Policy payments to the States and Territories have been met; and
- to recommend on whether State and Territory government businesses should be declared for prices surveillance by the Australian Competition and Consumer Commission, and to report on the costs and benefits of legislation reliant on section 51 of the Trade Practices Act.

Note 2 Summary of Significant Accounting Policies

2.1 Basis of Accounting

The production of the financial statements is required by section 49 of the Financial Management and Accountability Act 1997 and represent a general purpose financial report. The statements have been prepared in accordance with Schedule 2 to the Financial Management and Accountability (FMA) Orders made by the Minister for Finance and Administration. Schedule 2 requires that the financial statements are prepared:

- in compliance with Australian Accounting Standards and Accounting Guidance Releases and the Consensus Views of the Urgent Issues Group; and
- having regard to Statements of Accounting Concepts.

The financial statements have been prepared on an accrual basis and in accordance with the historical cost convention. They have not been adjusted to take account of either changes in the general purchasing power of the dollar or changes in the prices of specific assets.

The continued existence of the Council in its present form is dependent on Government policy and on continuing appropriations by Parliament for the Council's administration.

2.2 'Agency' and 'Administered' Items

A distinction is required to be made within the financial statements between 'agency' items and 'administered' items.

'Administered' items represent those assets, liabilities, expenses and revenues which are controlled by the Government and managed in a fiduciary capacity by the Council.

'Agency' items represent those assets, liabilities, expenses and revenues which are controlled by the Council.

The purpose of this distinction is to enable an assessment to be made of the efficiency of the Council in providing goods and services ('Agency' items), while at the same time enabling accountability by the Council for all resources administered by it.

Note 2 Summary of Significant Accounting Policies (continued)

The Council did not manage 'administered' items on behalf of the Government in relation to the reporting period.

2.3 Taxation

The Council is exempt from all forms of taxation except fringe benefits tax.

2.4 Insurance

In accordance with Commonwealth Government policy, assets are not insured and losses are expensed as they are incurred.

2.5 Comparative figures

Where necessary, comparative figures have been adjusted to conform with changes in presentation in these financial statements.

2.6 Program Statements

The Council represents a component of a sub-program within the Department of the Treasury portfolio. As a result there is no requirement for a program statement to be included in the financial statements.

2.7 Appropriations

Appropriations for agency operations other than running costs are recognised as revenue when the Council obtains control over the funds. Control is obtained at the time of expending the funds.

Appropriations for agency running costs operations are recognised in accordance with their nature under the Running Costs Arrangements. Under these arrangements, the Council receives a base amount of funding by way of appropriation for running costs each year. The base amount may be supplemented in any year by a carryover from the previous year of unspent appropriations up to allowable limits, as well as by

borrowings at a discount against future appropriations of the base amount. The repayment of a borrowing is effected by an appropriate reduction in the appropriation actually received in the year of repayment.

The Council recognises, in relation to agency running costs operations:

- as revenue an amount equal to the appropriation spent during the financial year;
- as a receivable an amount equal to the unspent appropriation carried over to the next year; and
- as a liability an amount equal to the running cost borrowings. The interest cost of the borrowing is expensed over the life of the borrowing.

Change in accounting policy: comparative figures

The above mentioned policy in relation to the accounting treatment of appropriations for agency running costs differs to the policy adopted in the reporting period 1995/96.

In reporting periods prior to 1996/97 running cost appropriations were recognised as revenue only to the extent that appropriation funds were spent.

The financial effect of this change in policy resulted in an adjustment to opening accumulated results of $207,000 for the 1996/97 comparative figures relating to the recognition of appropriation carry-over from 1995-96.

2.8 Employee Entitlements

The liability for employee entitlements includes all employee benefits including; salaries and wages, annual leave, and long service leave.

No provision has been made for sick leave as all leave is non-vesting and the value of sick leave estimated to be taken in the future is expected to be less than the entitlement that will accrue to Council staff in those future periods.

The non-current portion for the liability for long service leave reflects the present value of the estimated future cash flows to be made in respect of all employees.

Note 2 Summary of Significant Accounting Policies (continued)

In determining the value of the liability, the Council has taken into account attrition rates and pay increases through promotion and inflation.

The determination of current and non-current liability portions of the long service leave provision is based on a staff survey. The value of long service leave entitlements estimated to be taken within the next twelve months are classified as current.

Annual leave entitlements are classified as current liabilities.

2.9 Superannuation

Staff of the Council contribute to the Commonwealth Superannuation Scheme and the Public Sector Superannuation Scheme. Superannuation contributions made by the Council on behalf of staff in relation to these schemes have been expensed in these financial statements.

A liability is not shown for any unfunded superannuation liability that exists in relation to Council staff as the employer contributions fully extinguish the accruing liability assumed by the Commonwealth.

2.10 Resources Received Free of Charge

Resources received free of charge are recognised in the statement of Agency Revenues and Expenses as revenue where the amounts can be reliably measured. Use of those resources is recognised as expenses, or where there is a long term benefit, as an asset.

Resources received free of charge which cannot be reliably measured are disclosed in the notes.

2.11 Cash

For the purposes of the Statement of Cash Flows, cash includes notes, coins and cheques on hand.

2.12 Inventory

Inventories held for sale are valued at the lower of cost and net realisable value.

2.13 Capitalisation Threshold – Property, Plant and Equipment

All items of computers, plant and equipment with historical cost equal to or in excess of $500 are capitalised in the year of acquisition. The items below this threshold are expensed in the year of acquisition.

All items of leasehold improvements controlled by the Council and with historical costs equal to or in excess of $5,000 are capitalised in the year of acquisition.

The capitalisation threshold is applied to the aggregate cost of each functional asset.

2.14 Measurement of Property, Plant and Equipment

All property, plant and equipment assets in excess of the capitalisation threshold are recorded at cost, except in circumstances in which acquisitions are made at no cost from other Commonwealth controlled entities. In such circumstances property, plant and equipment are recorded at the amounts at which they were recognised in the transferor's books immediately prior to transfer.

2.15 Depreciation and Amortisation of Property, Plant and Equipment

Depreciable property, plant and equipment are depreciated over their estimated useful lives. The useful life of an asset reflects the life of the asset to the Council.

Depreciation is calculated using the straight–line method which reflects the pattern of usage of the Council's depreciable property, plant and equipment.

Leasehold improvements are amortised over the estimated useful life of each improvement, or the unexpired period of the lease, whichever is shorter.

2.16 Revaluations of Property, Plant and Equipment

All items of leasehold improvements and with historical costs equal to or in excess of $5,000 and all items of computer, plant and equipment will be progressively revalued

Note 2 Summary of Significant Accounting Policies (continued)

in accordance with the 'deprival' method of valuation by 1 July 1999 and thereafter be revalued progressively on that basis every three years.

The Council is implementing the revaluations as follows:

- Leasehold improvements will be revalued progressively every three years. The leasehold was initially acquired in November 1995 and will be revalued in 1998/99.
- Computers, plant and equipment will be revalued in 1998/99, given the Council commenced in November 1995, and thereafter over successive three year periods.

Assets in each class acquired after the commencement of the progressive revaluation cycle will be reported at cost for the duration of the progressive revaluation then in progress.

The financial effect of the move to progressive revaluations is that the carrying amounts of assets will reflect current values and that depreciation charges will reflect the current cost of the service potential consumed in each period.

2.17 Leases

A distinction is made between finance leases which effectively transfer from the lessor to the lessee substantially all the risks and benefits incidental to ownership of the leased plant and equipment asset and operating leases under which the lessor effectively retains substantially all such risks and benefits.

Where a non-current asset is acquired by means of a finance lease, the asset is capitalised at the present value of minimum lease payments at the inception of the lease and a liability recognised for the same amount. Lease payments are allocated between the principal component and the interest expense.

Operating lease payments are charged to the statement of Agency Revenues and Expenses.

2.18 Lease Incentives

The value of rent which would otherwise have been incurred during a rent free period, provided by building owners, is initially recognised as a liability. This liability is reduced once the rent free period ceases by allocating payments between rental expense and reduction of the liability.

	1997-98 $	1996-97 $

Note 3 Expenses: Employees

Basic Remuneration (for services provided)	**1,593,403**	1,020,510
Other employee expenses	**-**	17,760
Total	**1,593,403**	**1,038,270**

Note 4 Expenses: Suppliers

Supply of goods and services	**1,215,142**	883,145
Operating lease rentals	**102,819**	86,310
Total	**1,317,961**	**969,455**

Note 5 Expenses: Depreciation and Amortisiation

Depreciation of property, plant and equipment	**99,926**	87,332
Amortisation of leased assets	**-**	-
Total expense	**99,926**	**87,332**

The aggregate amounts of depreciation or amortisation expensed during the reporting period for each class of depreciable asset are as follows:

Leasehold improvements	**18,403**	10,067
Leasehold improvements – received free of charge	**43,902**	43,902
Computers, plant and equipment	**31,412**	27,154
Computers, plant and equipment – received free of charge	**6,209**	6,209
Total	**99,926**	**87,332**

No depreciation or amortisation was allocated to the carrying amounts of other assets.

	1997-98	1996-97
	$	$

Note 6 Expenses: Net Losses from Sale of Assets

Non-financial assets:		
Plant and equipment	**2,181**	-
Total	**2,181**	**-**

Note 7 Expenses: Write down of Assets

Non-financial Assets:		
Inventories – held for sale	**6,179**	-
Total	**6,179**	**-**

Note 8 Provisions and Payables: Employees

Salaries and wages	**82,442**	11,629
Leave	**281,868**	233,757
Superannuation	**2,177**	1,790
	366,487	247,176
Other	**-**	17,760
Aggregate employee entitlement liability	**366,487**	**264,936**

Note 9 Provisions and Payables: Suppliers

Trade creditors	**53,420**	64,290

Note 10 Provisions and Payables: Other

Lease incentives	**14,286**	50,751

	1997-98	1996-97
	$	$

Note 11 – Equity: Accumulated Results

Opening balance	**126,352**	259,008
Add: Operating result	**(34,518)**	(339,656)
Change in accounting policy	**-**	207,000
Closing balance	**91,834**	**126,352**

Note 12 Financial Assets: Receivables

Appropriations	**151,000**	30,122
Goods and services	**6,694**	918
Total	**157,694**	**31,040**

No component of the above receivables was overdue at the end of the reporting period. In addition no component of the receivables was considered doubtful.

Note 13 Non-Financial Assets: Property, Plant and Equipment

LAND AND BUILDINGS		
Leasehold improvements - at cost	**122,922**	60,398
Less: accumulated amortisation	**30,714**	12,311
	92,208	48,087
Leasehold improvements - received free of charge	**219,511**	219,511
Less: accumulated amortisation	**116,310**	72,408
	103,201	147,103
Total land and buildings	**195,409**	**195,190**

Note 13 Non-Financial Assets: Property, Plant and Equipment (continued)

PLANT AND EQUIPMENT		
Plant and equipment - at cost	**202,420**	175,987
Less: accumulated depreciation	**67,832**	38,406
	134,588	**137,581**
Plant and equipment - received free of charge	**25,137**	25,137
Less: accumulated depreciation	**16,449**	10,240
	8,688	14,897
Total infrastructure, plant and equipment	**143,276**	152,478

Note 14 Non-Financial Assets: Analysis of Property, Plant and Equipment

	Land and buildings $	Plant and equipment $	Total $
AGGREGATE			
Gross value as at 1 July 1997	279,909	201,124	481,033
Additions	62,524	33,300	95,824
Disposal	-	6,867	6,867
Gross value as at 30 June 1998	**342,433**	**227,557**	**569,990**
Accumulated depreciation/amortisiation as at 1 July 1997	84,719	48,646	133,365
Depreciation/amortisation charge for assets held as at 1 July 1997	53,969	35,321	89,290
Depreciation/amortisation charge for additions	8,336	2,300	10,636
Adjustment for disposal	-	1,986	1,986
Accumulated depreciation/ amortisation as at 30 June 1998	**147,024**	**84,281**	**231,305**
Net book value as at 30 June 1998	**195,409**	**143,276**	**338,685**
Net book value as at 1 July 1997	**195,190**	**152,478**	**347,668**

AT COST			
Gross value as at 1 July 1997	60,398	175,987	236,385
Additions	62,524	33,300	95,824
Disposals		6,867	6,867
Gross value as at 30 June 1998	**122,922**	**202,420**	**325,342**
Accumulated depreciation/amortisation as at 1 July 1997	12,311	38,406	50,717
Depreciation/amortisation charge for assets held as at 1 July 1997	10,067	29,112	39,179
Depreciation/amortisation charge for additions	8,336	2,300	10,636
Adjustment for disposals	-	1,986	1,986
Accumulated depreciation/amortisation as at 30 June 1998	**30,714**	**67,832**	**98,546**
Net book value as at 30 June 1998	**92,208**	**134,588**	**226,796**
Net book value as at 1 July 1997	**48,087**	**137,581**	**185,668**
RECEIVED FREE OF CHARGE			
Gross value as at 1 July 1997	219,511	25,137	244,648
Gross value as at 30 June 1998	**219,511**	**25,137**	**244,648**
Accumulated depreciation/amortisation as at 1 July 1997	72,408	10,240	82,648
Depreciation/amortisation charge for assets held as at 1 July 1997	43,902	6,209	50,111
Accumulated depreciation/amortisation as at 30 June 1998	**116,310**	**16,449**	**132,759**
Net book value as at 30 June 1998	**103,201**	**8,688**	**111,889**
Net book value as at 1 July 1997	**147,103**	**14,897**	**162,000**

Note 15 Cash Flow Reconciliation

	1997-98 $	1996-97 $
Reconciliation of net cost of services to net cash provided by operating activities:		
Net cost of services	(3,006,730)	(2,092,656)
Extraordinary items	-	-
Loss on sale of property, plant and equipment	2,181	-
Depreciation/ Amortisation	99,926	87,332
Revenue from government	2,972,212	1,753,000
Change in accounting policy	-	207,000
Changes in assets and liabilities		
(Increase) in receivables	(126,654)	(30,658)
(Increase)/decrease in other assets	95,839	49,359
Decrease/(increase) in inventories	634	(7,087)
Increase/(decrease) in provisions and payables	54,216	107,760
Net cash from operating activities	**91,624**	**74,050**

Note 16 Reconciliation of Agency Running Costs

	Expenditure 1997-98 $	Expenditure 1996-97 $
ORDINARY ANNUAL SERVICES OF GOVERNMENT APPROPRIATION ACT NOS 1 & 3		
Division 676 - National Competition Council		
1. Running Costs	2,830,461	1,909,826
less appropriations under FMA Act section 31	(3,152)	(948)
	2,827,309	**1,908,878**
add carryover 30 June	151,000	30,122
less carryover 1 July	30,122	207,000
Revenue from Government – ordinary annual services	**2,948,187**	1,732,000

Note 17 Expenditure from Annual Appropriations

1997/98 Budget Estimates	1997/98 Additional Approp	1997/98 Advance from Minister for Finance	1997/98 Total Approp	1997/98 Actual Expend	**1996/97 Actual Expend**
ORDINARY ANNUAL SERVICES APPROPRIATION ACT				ACT NO.1	ACT NO.3
APPROPRIATION ACT NOS 1 & 3					
Division 676 - National Competition Council					
1. Running Costs					
$	$	$	$	$	$
2,730,000	274,000	-	3,004,000	**2,830,461**	1,909,826

Note 18 Services Provided by the Auditor-General

Audit services are provided free of charge by the Auditor-General. The fair value of audit services provided in relation to the reporting period is $20,000 (1996-97:$21,000).

Other services provided by the Auditor-General in relation to the reporting period is $4,025
(1996-97:$NIL).

Note 19 Executive Remuneration

The number of executive officers who received or were due and receivable to receive fixed remuneration of more than $100,000 or more:

	Number	Number
$100,000 to $110,000	**-**	1
$110,001 to $120,000	**1**	-
$120,001 to $130,000	**1**	-
The aggregate amount of fixed remuneration of executive officers shown above	$246,181	$103,361

Note 20 Act of Grace Payments, Waivers and Amounts Written Off

No Act of Grace payments were made pursuant to sub-section 34A(1) of the *Audit Act 1901* during the reporting period.

No waivers of amounts owing to the Commonwealth were made pursuant to sub-section 70C(2) of the *Audit Act 1901* during the reporting period nor pursuant to any other legislation.

Note 21 Events Occurring After Balance Date

No events of a material nature have occurred since the end of the reporting period (1995-96: Nil) which warrant disclosure within the financial statements.

Note 22 Average Staffing Levels

Average staffing levels for the Council are as follows:

	1997-98	1996-97
	Number	Number
National Competition Council	19.4	14.6

Note 23 Financial Instruments

a) Terms, conditions and accounting policies

Financial Instrument	Notes	Accounting Policies and Methods (including recognition criteria and measurement basis)	Nature of underlying instrument (including significant terms & conditions affecting the amount, timing and certainty of cash flows)
Financial Assets			
Cash		Deposits are recognised at their nominal amounts	Deposits are non interest bearing
Receivables for goods and services	12	These receivables are recognised at the nominal amounts due less any provision for bad and doubtful debts	All receivables are with entities external to the Commonwealth
Financial Liabilities			
Trade Creditors	9	Creditors and accruals are recognised at their nominal amounts, being the amounts at which the liabilities will be settled. Liabilities are recognised to the extent that the goods or services have been received (and irrespective of having been invoiced)	All creditors are entities that are not part of the Commonwealth legal entity. Settlement is usually made net 30 days

Note 23 Financial Instruments (continued)

b) Interest Rate Risk: Agency

Financial Instrument	Notes	Non-Interest Bearing		Total	
		97-98	96-97	**97-98**	96-97
Financial Assets		**$**	$	**$**	$
Cash at Bank		**500**	2,000	**500**	2,000
Receivables for goods and services	12	**6,694**	918	**6,694**	918
Total Financial Assets (Recognised)		**7,194**	2,918	**7,194**	2,918
Total Assets				**526,027**	506,329
Financial Liabilities					
Trade creditors	9	**53,420**	64,290	**53,420**	64,290
Total Financial Liabilities (Recognised)		**53,420**	64,290	**53,420**	64,290
Total Liabilities				**418,565**	379,977

c) Net Fair Values of Financial Assets and Liabilities

	Note	**1997-98 Total carrying amount**	**1997-98 Aggregate net fair value**	1996-97 Total carrying amount	1996-97 Aggregate net fair value
Departmental Financial Assets					
Cash at Bank		**500**	**500**	2,000	2,000
Receivables for Goods and Services	12	**6,694**	**6,694**	918	918
Total Financial Assets		**7,194**	**7,194**	2,918	2,918
Financial Liabilities (Recognised)					
Trade Creditors	9	**53,420**	**53,420**	64,290	64,290
Total Financial Liabilities (Recognised)		**53,420**	**53,420**	64,290	64,290

Financial assets

The net fair value of cash and non-interest-bearing monetary financial assets approximate their carrying amounts.

Financial liabilities

The net fair values for trade creditors are short-term in nature, and are approximated by their carrying amounts.

d) Credit Risk Exposures

The Agency's maximum exposures to credit risk at reporting date in relation to each class of recognised financial assets is the carrying amount of those assets as indicated in the Statement of Assets and Liabilities.

The Agency has no significant exposures to any concentrations of credit risk.

COMPETITION POLICY UNITS

For further information about National Competition Policy, please contact the National Competition Council or the relevant Commonwealth, State or Territory competition policy unit.

National

National Competition Council
Level 12
Casselden Place
2 Lonsdale Street
MELBOURNE VIC 3000
Telephone: (03) 9285 7474
Facsimile: (03) 9285 7477
Email: ncc@c031.aone.net.au
Website: http://www.ncc.gov.au

Commonwealth

Competition Policy Branch
Commonwealth Treasury
Block B, Parkes Place
PARKES ACT 2600
Telephone: (02) 6263 3887
Facsimile: (02) 6263 2937

New South Wales

Inter-governmental and Regulatory
Reform Branch
The Cabinet Office
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Governor Macquarie Tower
1 Farrer Place
SYDNEY NSW 2000
Telephone: (02) 9228 5414
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Victoria

Economic Development Branch
Department of Premier and Cabinet
1 Treasury Place
MELBOURNE VIC 3002
Telephone: (03) 9651 5143
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Queensland

National Competition Policy Unit
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100 George Street
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Western Australia

Competition Policy Unit
Treasury
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PERTH WA 6000
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South Australia

Microeconomic Reform Branch
Department of Premier and Cabinet
State Administration Centre
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Tasmania

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