



Department of Treasury and Finance  
Government of Western Australia

# Western Australian Government Submission to the Productivity Commission

## Review of National Competition Policy Arrangements

September 2004



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## Executive Summary

### **The effectiveness of competition payments as leverage for reform**

The NCC (2004) has indicated that using competition payments to deliver reform outcomes has proven highly effective. However, Western Australia argues that the payments threat could have been more effective if there was greater use of recoverable suspensions rather than resorting to irrecoverable deductions in the first instance.

In those areas where deductions have been incurred by Western Australia they have provided little incentive for fruitful negotiations between the NCC and the Government because the competition payments have been lost in that year irrespective of reform progress later in that year.

### **Existing competition payments should continue beyond 2005-06**

The 1995 Agreements do not contain a sunset clause. The Implementation Agreement specified that NCP payments would total \$600 million annually from 2001-02 (in 1994-95 prices). It did not state that payments would terminate or change after 2005-06.

Any proposal to renegotiate payments is at odds with the expectation the States and Territories had when they negotiated the payments at the February 1994 COAG meeting. At that time, the expectation was that payments would continue indefinitely. Termination or the addition of new conditions to the payments would represent a reneging by the Commonwealth on the NCP Agreements.

Given the existing competition payments represent the dividend to jurisdictions for implementing NCP reforms, and that the benefits of any reforms made are ongoing, the competition payments should continue to be made to States and Territories beyond 2005-06 in perpetuity. In addition, without ongoing competition payments, gatekeeping mechanisms established for new legislation will be unlikely to function as well as they otherwise would.

### **Commonwealth needs an incentive to reform**

The Productivity Commission should examine how the Commonwealth Government could be provided with a greater incentive (than public interest) to progress NCP reforms. The Commonwealth Government is not subject to NCP competition payments. This creates an inconsistency of treatment between the Commonwealth and all other jurisdictions that fail to comply with their NCP

commitments. Whilst Western Australia and other jurisdictions have been financially penalised for failing to deliver on their NCP obligations, the Commonwealth escapes with the NCC's token criticisms contained within its annual assessments.

### **NCP raises productivity growth**

Over the period since NCP has been in place Australia's productivity growth has been stronger and more sustained than ever. Between 1990 and 2001 Australia's productivity ranking (measured on a GDP per person basis) rose from 15th to 7th among OECD countries (Productivity Commission 2002).

Effective competition policy facilitates the development of a competitive, flexible economy that allows more rapid and less costly adjustment to changes in the domestic and international economic environment. In most cases, developing competitive markets for goods and services allows Australia to increase its level of productivity growth leading to higher real incomes and greater employment opportunities.

### **NCP also contributes to the achievement of wider benefits**

In addition to raising Australia's productivity and economic growth, NCP reforms, have either already, or will in the future, contribute to the achievement of environmental policy goals.

Environmental objectives will be facilitated by NCP electricity reforms in Western Australia. Western Australian water reforms under NCP have also achieved environmental objectives.

### **NCP's effects on rural and regional Australia**

The perception in regional areas has been that metropolitan areas had reaped the benefits of NCP whilst regional areas suffered the costs. However, the Productivity Commission's 1999 Report found that rural and regional Australia had benefited from competition policy. While there are costs associated with implementing NCP, it will bring net benefits to the nation, and to rural and regional Australia as a whole, over the medium term.

The results of the Productivity Commission's 1999 analysis seem to have been ignored, or not been believed, by many rural lobby groups making submissions to this current inquiry. Indeed the negative and sometimes even hostile perceptions of NCP in rural areas appear to have continued unabated since the same criticisms levelled at NCP in 1999 have resurfaced again in 2004.

This highlights that the benefits of NCP to the community, particularly the rural community, need to be better explained and that transitional arrangements be assessed when making decisions about policy change under NCP.

### **NCP reform needs to be better understood**

Despite the evidence of economy-wide benefits, there has been strong criticism of NCP from various sections of the Australian community. In some cases the criticism has not been justified. For example, many of the criticisms have been about compulsory competitive tendering, privatisation of government assets, or the closure of bank branches in regional areas – none of which is NCP.

Given there exists some misplaced criticism of NCP; an organisation should be given the explicit responsibility of correcting any misinformation about NCP in the community. In addition, the organisation could inform the community why and how NCP reform leads to superior outcomes and performance than the alternatives. The NCC could have this role or it could conceivably go elsewhere.

### **Public interest should remain the foundation of the NCP framework**

The Government recognises that NCP reforms, while benefiting the State overall, can have substantial impacts/costs on those directly affected by change.

The public interest test is challenging to apply. This is because the criteria that need to be considered are not always easily quantifiable and sometimes move in opposite directions in response to reform proposals, making the final assessment of public interest subjective and value-laden. The final assessment will depend on how the criteria that improve as a result of reform are weighted against those that are worsened. This is why the NCP framework recognises that public interest assessments ultimately require political decisions.

Notwithstanding these challenges it is imperative that public interest continues to be the underlying foundation of the NCP framework. To justify NCP reforms on a narrower measure of public interest, say the efficient allocation of resources, would lead to inferior public interest outcomes.

### **Taking account of distributional impacts and adjustment costs**

To be successful in implementing reform it is imperative that governments understand the distributional and adjustment implications of reform. Criticism has been prominent in regional areas and while much of this criticism has been inaccurate, and there are instances of significant regional benefits, some people within certain regional communities may have less to gain from NCP.

For these reasons it is imperative that the implementation of NCP reforms are sensitive to the effects on local communities. Transitional arrangements and/or adjustment assistance should be considered where regional impacts are acute. Such sensitivity will go some way to ensuring that reforms in the interests of the whole community still take place despite any negative local/regional impacts.

### **Unfinished business - structural reform in the electricity industry**

For Western Australia there is much to be gained from completing the NCP agenda. While there still remains some progress to be made on legislation review, by far the most important area of NCP to progress is structural reform because this will have by far the greatest potential impact on the economy.

Until Western Australia fully reforms the electricity industry Western Australian businesses and households will continue to pay more for their electricity than businesses and households in the majority of other states.

### **Unfinished business - structural reform in telecommunications**

Reforms of Commonwealth Government legislation have made significant contributions to increased competition in the telecommunications industry and delivered price and choice benefits to consumers. However it appears that further significant gains to consumers do not seem possible unless the Commonwealth seriously considers what other actions need to be taken to promote additional competition benefits.

The Productivity Commission should give high priority to examining what further action needs to be taken in the telecommunications industry to facilitate greater competition. There would appear to be significant public interest justification in separating Telstra's natural monopoly elements from its competitive elements consistent with clause 4 of the *Competition Principles Agreement*.

### **Impediments to achieving unfinished NCP reforms**

A significant impediment to completing the current NCP agenda is the power and influence of business lobby groups. These lobby groups tend to be more influential and successful with governments than consumers or consumer groups.

The Productivity Commission should also give some thought to processes for encouraging and nurturing a well organised and well-resourced consumer advocacy group in Australia. The specific focus of such a group should be on encouraging competition in markets for the benefit of consumers since it is recognised that consumer protection is undertaken by government agencies. A strong consumer advocate could provide an effective counterweight to vested interest groups, exposing the flaws in their so-called 'public interest' arguments that defend the status quo.

### **New approach for legislation review**

The approach agreed to by COAG (1995) for legislation review has not functioned effectively. Sovereign governments have been prevented from implementing NCP within their jurisdictions as they have seen fit. Rather than suffer financial penalty, some governments have felt they have had no choice but to comply with



the Commonwealth's demands. This has not only weakened democratic processes but also led to confusion over which tier of government is accountable for the decisions made on NCP. An approach that maintains jurisdictional sovereignty while still producing NCP outcomes in the public interest is what is required.

The Productivity Commission could examine whether alternative NCP assessment processes, particularly for legislation review, have the potential to deliver better public interest outcomes. The results of the Productivity Commission's work could then inform COAG's own review of NCP arrangements that is due by September 2005.

### **Materiality test for legislation reviews**

With the benefit of hindsight there has perhaps been too much emphasis placed on legislation reviews that were not material, and that this issue could be resolved by the inclusion of a materiality test in deciding if legislation review is warranted.

The Productivity Commission could examine whether a materiality test, particularly for legislation review, has the potential to deliver public interest outcomes in a less costly manner. The results of the Productivity Commission's work could then inform COAG's own review of NCP arrangements that is due by September 2005.

### **National review process should be fine-tuned**

NCP provides the scope for national reviews to be undertaken where a review has a national dimension or effect on competition under clause 5(7) of the *Competition Principles Agreement*. However, very few reviews have been undertaken on a national basis and where they have been undertaken the reform outcomes have been mixed at best.

Using the lessons learnt from the national reviews undertaken already, the Productivity Commission should examine how the national review process can be fine-tuned to consistently deliver best practice regulation. The results of the Productivity Commission's work could then inform COAG's own review of NCP arrangements that is due by September 2005.

### **Greater transparency in review processes is needed**

While many review reports of existing legislation have been published, there is no NCP obligation to publish them, or even make them available to the NCC. In Western Australia it is up to the responsible Minister to decide whether a review report is made public. However, in all instances in which the NCC has requested review reports, the relevant Western Australian Minister has complied.

Transparent processes are crucial when assessing the public interest. Without transparency it is extremely difficult to gain the community's confidence that

public interest considerations have been examined in an impartial manner and that it is the community's interest that is the overriding concern rather than any particular sectional interest group when deciding whether a reform should or should not be progressed.

### **A new reform agenda**

Western Australia supports the views of the Victorian Government that any future reform agenda must be strongly based on a substantial and credible case for the need for reform. NCP was based on a strong foundation (i.e. the Hilmer Report), any new national reform agenda must be equally strongly based. Jurisdictions should make no commitment for further reform until a substantial and credible case for the need for reform is made.

If a strong case can be made for a new reform agenda, there must be robust boundaries around jurisdictions' agreed obligations. Any new reform obligations should be accompanied by new payments from the Commonwealth to ensure the gains from the new reform agenda are appropriately shared.

## Background

The National Competition Policy (NCP) reform agenda was developed in the early 1990s following a range of micro-economic reforms introduced in the 1970s and 1980s by both State and Federal governments.

However, by the 1990s this piecemeal approach to competition policy was severely inhibiting the scope for further improvement in Australia's economic performance and the welfare of the community. Business and the community more generally were frustrated with the lack of progress made by governments in reforming uncompetitive infrastructure and anti-competitive regulations.

In 1992, the Prime Minister announced the establishment of a major independent inquiry – now known as the Hilmer Report – into competition policy in Australia. The terms of reference were drawn up in consultation with the States and Territories and special emphasis was given to areas of economic activity outside the *Trade Practices Act 1974* (TPA).

According to the Hilmer Report (1993) the imperative for developing a national competition policy rested on three main factors:

1. increasing acknowledgement that Australia was for all practical purposes a single integrated market;
2. many goods and services provided by public utilities, professions and some areas of agriculture remained sheltered from international and domestic competition despite the existence of the TPA; and
3. the domestic pro-competitive reforms implemented previously had all been progressed on an inefficient and costly sector-by-sector basis, without the benefit of a broader policy framework or process.

In response to the Hilmer Report, the Commonwealth and all State and Territory governments agreed, in April 1995, on the need for a more coordinated and consistent approach to competition policy reform.

### **The National Competition Policy Package**

The NCP framework consists of three intergovernmental agreements:

- the *Conduct Code Agreement* which establishes the basis for extending the coverage of the TPA to all businesses and professions in Australia;

- the *Competition Principles Agreement* (CPA) which sets out principles for prices oversight, structural reform of public monopolies, review of anti-competitive legislation, third party access to services provided by essential infrastructure, competitive neutrality, and the application of these principles to local government; and
- the *Agreement to Implement the National Competition Policy and Related Reforms* (the Implementation Agreement) which sets out the conditions for provision of financial transfers from the Commonwealth to the States and Territories in return for implementing competition reforms.

The *Competition Policy Reform Act 1995* established two new institutions to oversee the implementation of the NCP package:

- the National Competition Council (NCC) was established as an independent advisory body for all Australian governments on NCP issues. The NCC's core responsibility is to assess governments' progress in implementing NCP, including making recommendations to the Federal Treasurer on competition payments.
- the Australian Competition and Consumer Commission (ACCC) was created through the merger of the former Trade Practices Commission and the Prices Surveillance Authority. The ACCC is involved principally with the enforcement of the TPA.

Governments agreed to the NCP based on the presumption that competition will create the incentives for better economic performance in Australia. As the Hilmer Report said:

*"Competition provides the spur for businesses to improve their performance, develop new products and respond to changing circumstances. Competition offers the promise of lower prices and improved choice for consumers and greater efficiency, higher economic growth and increased employment opportunities for the economy as a whole."* (Hilmer 1993, p. 1)

However, NCP is not about the pursuit of competition for its own sake: competition is a means rather than an end in itself. This was clearly outlined in the Hilmer Report:

*"Competition policy is not about the pursuit of competition per se. Rather it seeks to facilitate effective competition to promote efficiency and economic growth while accommodating situations where competition does not achieve efficiency or conflicts with other social objectives. These accommodations are reflected in the content and breadth of application of pro-competitive policies, as well as the sanctioning of anti-competitive arrangements on public benefit grounds."* (Hilmer 1993, p. xvi)

As a consequence, NCP provides for the retention of anti-competitive arrangements where they can be justified in the public interest (or not contrary to the public interest). For example, the review of anti-competitive legislation, the structural reform of public monopolies and the application of competitive neutrality to government businesses are subject to the public interest provisions of the CPA (i.e. clause 1(3)). With respect to a 'declaration' of infrastructure services for third party access, access must not be contrary to the public interest. Finally authorisation of anti-competitive practices prohibited by the TPA can be sought from the ACCC based on net public benefit grounds.

### **COAG Review of the National Competition Policy Agreements**

When Australia's governments adopted NCP in 1995 they acknowledged the importance of assessing whether the principles and procedures underpinning the NCP continued to be relevant after a period of operation. In 2000 a Senior Officials' Working Group reviewed the NCP on behalf of the Council of Australian Governments (COAG).

This review drew on the findings of the Productivity Commission's 1999 inquiry into the impact of competition policy reforms on rural and regional Australia and the 2000 report of the Senate Select Committee on the socio-economic consequences of the National Competition Policy.

On 3 November 2000, COAG endorsed the importance of NCP in sustaining the competitiveness and flexibility of the Australian economy and contributing to higher standards of living (COAG 2000). COAG recommitted to NCP for a further five years and scheduled another review of the NCP agreements and the role of the NCC before September 2005.

COAG also accepted the Working Group's proposed fine-tuning of the NCP process and the role of the NCC. According to the NCC (2001):

*"Their objective was to establish a practical framework for the effective implementation of the NCP, while demonstrating their ongoing commitment to upholding the policy and safeguarding the benefits that the policy delivers to Australia. COAG also sought to address community concerns about the implementation of the NCP that had been identified in the Productivity Commission and Senate Select Committee reviews."* (page 8)

These community concerns included:

- a lack of community understanding of the NCP generally (and of the constitution and implementation of the public interest test particularly);
- difficulties with the way in which particular reviews had been conducted, and the infrequent use of national review process for matters relevant across jurisdictions;

- perceived deficiencies in government's oversight of the NCP and the NCC (usually expressed as concerns that the NCC was too independent of elected governments); and
- adverse impacts on regions and deficiencies in structural adjustment and transitional arrangements.

## The Assessment Process and NCP Payments

### **Payments are dividends for implementing reform**

As outlined by the NCC (2003) it has undertaken five assessments of State and Territory government progress in implementing the NCP, in June 1997, 1999, 2001, 2002 and 2003. The NCC's assessments make recommendations to the Commonwealth Treasurer on whether States and Territories have met their commitments to implement the NCP reforms and, consequently, whether they should receive NCP payments.

The NCC views the payments as dividends for implementing reform. To receive full competition payments, States and Territories must achieve satisfactory progress against the agreed reform agenda. According to the NCC (2001):

*“Governments are entitled to choose to not implement elements of the NCP, but is so doing may not receive full competition payments. This is a logical approach because a decision not to introduce reforms that benefit the community potentially reduces economic growth and the financial dividend available for distribution.”*

COAG (2000) directed the NCC on the nature of any financial penalty or suspension for identified non-compliance with the NCP. Thus, in its recommendations to the Federal Treasurer on competition payments penalties, the NCC must consider:

- the extent of the relevant State or Territory's overall commitment to the implementation of the NCP;
- the effect of one State or Territory's reform efforts on other jurisdictions; and
- the impact of a State or Territory's failure to undertake a particular reform.

This effectively means that minor breaches of reform obligations are unlikely to have negative payment implications if a jurisdiction's overall progress has been satisfactory. However, adverse recommendations are likely where a priority NCP area has not been reformed which affects other jurisdictions.

### **The effectiveness of competition payments as leverage for reform**

The NCC (2004) has indicated that using competition payments to deliver reform outcomes has proven highly effective. However, Western Australia argues that the payments threat could have been more effective if there was greater use of recoverable suspensions rather than resorting to irrecoverable deductions in the first instance.

In those areas where deductions have been incurred by Western Australia they have provided little incentive for fruitful negotiations between the NCC and the Government because the competition payments have been lost in that year irrespective of reform progress in that year.

This lack of incentive is evidenced by the 2003 NCP assessment process. In 2003-04 Western Australia incurred the following specific penalties:

- a permanent deduction of 10% for non-compliance in respect of retail trading hours legislation (estimated at \$7.52 million);
- a permanent deduction of 5% for non-compliance in respect of the regulation of liquor sales (estimated at \$3.76 million);
- a permanent deduction of 5% for non-compliance in respect of the marketing of potatoes (estimated at \$3.76 million);
- a specific suspension of 5% for non-compliance in respect of egg marketing (estimated at \$3.76 million); and
- a specific suspension of 10% for lack of transparency in water pricing (estimated at \$7.52 million).

In the cases of retail trading hours, liquor licensing and potato marketing, where Western Australia received permanent deductions, no change in the Government's position has been forthcoming in response to the irrecoverable financial penalties. However, where recoverable suspensions were incurred for egg marketing and water pricing the Government has announced policy changes.

On 4 June 2004 the Agriculture Minister Kim Chance announced that State Cabinet had approved provisions to terminate the *Marketing of Eggs Act 1995* on or before 31 December 2005, the timeframe imposed by the NCC<sup>1</sup>.

On the 16 June 2004 the State Treasurer announced an independent inquiry into Western Australian water prices. The Treasurer indicated he had formally asked

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<sup>1</sup> See Press Release by the Minister for Agriculture, "Assistance scheme planned for deregulation of egg marketing", 4 June 2004.



the State's Economic Regulation Authority to investigate whether water prices - imposed by Western Australia's monopoly service providers - were justified and complied with NCP<sup>2</sup>.

### **Existing competition payments should continue beyond 2005-06**

The 2003-04 Commonwealth Budget did not include NCP estimates in the forward year 2006-07. A footnote to the payments stated that "provision has been made for National Competition Policy Payments in 2006-07, however the final amounts will not be disclosed until after the conclusion of negotiations." The 2004-05 Commonwealth Budget made no provision for payments in 2006-07.

The 1995 Agreements do not contain a sunset clause. The Implementation Agreement specified that NCP payments would total \$600 million annually from 2001-02 (in 1994-95 prices). It did not state that payments would terminate or change after 2005-06.

Any proposal to renegotiate payments is at odds with the expectation the States and Territories had when they negotiated the payments at the February 1994 COAG meeting. At that time, the expectation was that payments would continue indefinitely. Termination or the addition of new conditions to the payments would represent a reneging by the Commonwealth on the NCP Agreements.

When all Australian jurisdictions signed the Implementation Agreement in 1995, the States and Territories did not attach any significance to the fact that the Commonwealth's published table of estimated payments did not extend beyond 2005-06, as it appeared to be simply a convenient place to end the table.

Importantly, the rationale for the payments has not changed since COAG agreed to the NCP package in 1995. Under the Implementation Agreement, the Commonwealth makes payments to State and Territories as a financial incentive to implement the NCP and related reform program. Competition payments recognise that the States and Territories have responsibility for the majority of NCP reform effort, yet much of the financial dividend from the economic growth arising from competition reforms accrues to the Commonwealth through the taxation system. The competition payments also recognise that the States and Territories have lost revenue from the loss of monopoly rents from government trading enterprises.

The Industry Commission (1995), later the Productivity Commission, estimated in March 1995 that the Hilmer reforms assessed could add 5.5 per cent, or \$23 billion, to Australia's gross domestic product per year. The Hilmer reforms

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<sup>2</sup> See Press Release by the Treasurer, "State to investigate water prices", 16 June 2004.

assessed suggested gains to Commonwealth revenue of \$5.9 billion and to the States and Territories of \$3 billion in real terms.

The benefits from NCP reforms are ongoing; they contribute to a permanent and sustained increase in productivity and economic growth and result in continued revenue benefits.

Given the existing competition payments represent the dividend to jurisdictions for implementing NCP reforms, and that the benefits of any reforms made are ongoing, the competition payments should continue to be made to States and Territories beyond 2005-06 in perpetuity. In addition, without ongoing competition payments, gate-keeping mechanisms established for new legislation will be unlikely to function as well as they otherwise would.

### **Commonwealth needs an incentive to reform**

The Productivity Commission should examine how the Commonwealth Government could be provided with a greater incentive (than public interest) to progress NCP reforms. The Commonwealth Government is not subject to NCP competition payments. This creates an inconsistency of treatment between the Commonwealth and all other jurisdictions that fail to comply with their NCP commitments. Whilst Western Australia and other jurisdictions have been financially penalised for failing to deliver on their NCP obligations, the Commonwealth escapes with the NCC's token criticisms contained within its annual assessments.

Given its inability to be sanctioned it is not surprising that the Commonwealth's performance has been judged 'well below average' by the NCC in its 2003 assessment report.

A good example of the Commonwealth's poor performance is in relation to export marketing for wheat. The Commonwealth continues to retain the wheat export single desk (i.e. the Australian Wheat Board) despite an NCP review showing that allowing competition is more likely to be of net benefit to the community.

The Commonwealth's inaction is having the effect of causing some other jurisdictions to be very cautious about removing monopoly powers from their statutory grain marketing organisations, as they fear their grain marketers without statutory powers could not compete with the Australian Wheat Board 'armed' with its statutory powers.

Other major failures by the Commonwealth include the retention of restrictions in broadcasting legislation, the lack of competition in postal services by failing to establish an access regime, and the incomplete review and reform of health-related legislation (pathology collection centre licensing and services covered by private health insurance) and legislation on industry assistance.

As the NCC (2003a) said:

*“its (i.e. the Commonwealth’s) progress in the review and reform of legislation has set a poor example for the States and Territories.”* (page lvi)

# Evaluating the Benefits and Costs of NCP

## **NCP raises productivity growth**

Over the period since NCP has been in place Australia's productivity growth has been stronger and more sustained than ever. Between 1990 and 2001 Australia's productivity ranking (measured on a GDP per person basis) rose from 15th to 7th among OECD countries (Productivity Commission 2002).

While measuring the impact of NCP separately from other demographic, government and market driven factors can be problematic, recent research by the OECD (2003) indicate that structural reform, and NCP in particular, has been a significant contributor to Australia's improved productivity and economic growth. Other OECD evidence indicates that excessive product market regulation can have a negative impact on productivity and also countries that have taken significant steps to introduce competition, like Australia, have experienced the strongest employment gains (OECD 2002a, 2002b).

Effective competition policy facilitates the development of a competitive, flexible economy that allows more rapid and less costly adjustment to changes in the domestic and international economic environment. In most cases, developing competitive markets for goods and services allows Australia to increase its level of productivity growth leading to higher real incomes and greater employment opportunities.

## **NCP also contributes to the achievement of wider benefits**

In addition to raising Australia's productivity and economic growth, NCP reforms, have either already, or will in the future, contribute to the achievement of environmental policy goals.

Environmental objectives will be facilitated by NCP electricity reforms in Western Australia. Electricity reform will encourage energy efficiency and demand management resulting in greenhouse gas reductions. The market operator is also obliged to consider the most cost effective options to expand system capacity, including demand side management options. Renewable generators will find it easier to enter the electricity market as stand alone entities following third party access to electricity infrastructure and the establishment of electricity wholesale markets that are better able to handle an intermittent supply. In addition, the

increased use of natural gas, both as a primary energy source and for electricity generation, has been assisted by third party access to gas infrastructure.

Western Australian water reforms under NCP have also achieved environmental objectives. Setting water prices on per unit volume charge has provided incentives for more efficient water use.

Establishing water entitlements separate from land title and setting up water trading has allowed water to be used where it is most valued. Water has also moved to more productive areas better suited to irrigation reducing environmental costs. In addition, Western Australia has developed water management arrangements for surface and groundwater that allocate water to the environment addressing environmental matters on an integrated catchment management basis.

### **NCP's effects on rural and regional Australia**

On 14 October 1999 the Federal Government released the Report of the Productivity Commission inquiry into the *Impact of Competition Policy Reforms on Rural and Regional Australia*.

The Report indicated that most of the hardships affecting rural Australia are the result of long-term factors, such as falling rural commodity prices, technological change (reducing the demand for labour) and changing consumer preferences. These factors are mainly responsible for the population drift away from inland country areas. The Report noted that NCP was wrongly blamed and had become a 'scapegoat' for some of the effects of these broader influences.

The perception in regional areas has been that metropolitan areas had reaped the benefits of NCP whilst regional areas suffered the costs. However, the Report found that rural and regional Australia had benefited from competition policy. While there are costs associated with implementing NCP, it will bring net benefits to the nation, and to rural and regional Australia as a whole, over the medium term.

However, it also found NCP reforms produced greater cost reductions for large rather than small businesses, and for business users rather than residential customers, but that benefits would spread to smaller users over time. The Report also noted that improved competitiveness of businesses supplying rural firms and consumers is likely to indirectly benefit country communities through reduced costs and prices and increased output and employment.

Some specific examples identified in the Report included:

- real gas prices fell by 22 per cent on average and the extension of the gas network has created opportunities for new and existing businesses in rural Australia;

- rail reforms produced significant benefits, particularly for users in country Australia, with national freight rates falling 16 per cent in real terms. Freight rates on the Melbourne to Perth rail route fell by over 40 per cent;
- port authority charges declined 23 per cent, a considerable benefit to country Australia given the significance of mining and agricultural exports;
- regional Australia has also benefited from improvements in communications. Competition in telecommunications saw STD prices fall by 25 per cent. The real price of posting a letter fell by 9 per cent, while the number of retail postal facilities in rural and remote Australia increased; and
- more flexible retail trading hours have been of net benefit to consumers and appear to have increased employment, including in country Western Australia.

The 1999 Report found that virtually all regions would gain as the benefits from NCP reform flow to the economy. In particular, the Productivity Commission's modelling found that the regions most likely to gain the greatest benefits tended to be in Queensland and Western Australia. For Western Australia, gross regional product was estimated to be 3.3 per cent higher and, employment 0.8 per cent higher, following the NCP reforms.

The results of the Productivity Commission's 1999 analysis seem to have been ignored, or not been believed, by many rural lobby groups making submissions to this current inquiry. Indeed the negative and sometimes even hostile perceptions of NCP in rural areas appear to have continued unabated since the same criticisms levelled at NCP in 1999 have resurfaced again in 2004.

This reinforces the points made later in this submission that the benefits of NCP to the community, particularly the rural community, need to be better explained and that transitional arrangements be assessed when making decisions about policy change under NCP.

The following case study provides an example of the benefits to the grains industry and growers from recent reforms to grain marketing in Western Australia.

### **Case study: Benefits from reforms to Grain Marketing Act**

The reforms to grain marketing in Western Australia have led to improved grain marketing options for rural Western Australia.

According to Department of Treasury and Finance (2004), the *Grain Marketing Act 2002* separated the roles of the regulator and the single desk marketer of prescribed grains in Western Australia, establishing the Grain Licensing Authority (GLA) as the independent regulator of bulk barley, lupin and canola exports from Western Australia. The GLA is responsible for considering applications for special export licences for bulk prescribed grains (barley, lupins and canola).

The Grain Pool Pty Ltd, formed from the privatisation of the Grain Pool of Western Australia and its merger with Cooperative Bulk Handling Ltd, holds the main export licence for bulk prescribed grains.

The GLA licenses exports except where it is convinced that a proposed export licence would affect the 'price premium' earned by the Grain Pool in certain uncompetitive export markets where it retains a degree of market power.

The new licensing arrangements have given grain growers more options for marketing their barley, canola and lupins in competitive export markets. Where there are benefits from a single desk in particular markets, a single desk can operate, but where this is not the case other sellers are now also permitted. Recent anecdotal evidence tends to suggest that the release of licences has had a positive effect on the prices farmers receive for their grain from grain marketers.

Growers have also welcomed more choice. According to DTF (2004), to date, since 22 September 2003 when the new licensing system came into effect, the GLA has approved a total of twelve licences:

- nine export licences for the bulk export of 433,000 tonnes of feed barley to the Middle East. These licences represent approximately 29 per cent of Western Australia's feed barley production in 2003-04;
- one export licence for 48,000 tonnes of canola to the sub-continent;
- one export licence for 20,000 tonnes of lupins to East Asia; and
- one export licence for 35,000 tonnes of malting barley to Asia. This approval was provided through appeal to the Minister.

The GLA has declined applications for 318,000 tonnes of feed barley to the Middle East, 45,000 tonnes of canola to the sub-continent, and 40,000 tonnes of canola to Asia, in recognition of the marketing efforts of the Grain Pool. The latter application was the subject of an unsuccessful appeal.

Western Australia's innovative approach to grain marketing is likely to be followed by South Australia where 70 per cent of South Australian grain growers support the introduction of a grain licensing authority in that State.

The steps taken in Western Australia are transitional and have been adopted because the Commonwealth retained its single desk monopoly export powers for the Australian Wheat Board (AWB). The Western Australian Government is not prepared to remove single desk powers when subject to 'unreformed' competition from the much bigger AWB.

### **NCP reform needs to be better understood**

Despite the evidence of economy-wide benefits, there has been strong criticism of NCP from various sections of the Australian community. In some cases the criticism has not been justified. For example, many of the criticisms have been about compulsory competitive tendering, privatisation of government assets, or the closure of bank branches in regional areas – none of which is NCP.

Opponents often cite NCP as the 'reason' for decisions to privatise or reduce funding for an activity. Such actions tend to confuse the community about what NCP is and as a consequence tends to make it difficult for many people to understand. Similar problems arise with the issue of globalisation.

Frequently criticisms from vested interest groups representing only one (vocal) side of an NCP issue are widely publicised in Western Australia, but alternative views representing the interests of the wider community, are not. This is in many ways a reflection of the lack of an effective, well-resourced consumer advocacy body in Western Australia.

Criticism of NCP has also tended to involve the distribution of the gains in real incomes and employment opportunities and the transitional impacts of reforms on different groups, rather than the gains in themselves. A popular backlash against reform arose in the late 1990s because of misplaced concerns that NCP has been anti-worker or anti-regional areas.

NCP has also drawn criticism because the NCP agreements do not contain clearly defined reform outcomes. For example, in relation to legislation review, Governments are only required to reach conclusions in review reports that are within a range of outcomes that could reasonably be reached based on the information available to a properly constituted review process (COAG 2000). COAG stipulated that it is a matter for the relevant government to determine,



within this range of outcomes, what policy is in the public interest. This allows individual jurisdictions some degree of flexibility in implementing reforms.

Given there exists some misplaced criticism of NCP; an organisation should be given the explicit responsibility of correcting any misinformation about NCP in the community. In addition, the organisation could inform the community why and how NCP reform leads to superior outcomes and performance than the alternatives. The NCC could have this role or it could conceivably go elsewhere.

## Efficacy of the Public Interest Test

### **Public interest should remain the foundation of the NCP framework**

The Government recognises that NCP reforms, while benefiting the State overall, can have substantial impacts/costs on those directly affected by change. Because of these impacts the NCP framework requires an assessment of these costs and benefits – commonly known as the ‘public interest test’ – prior to implementing reform.

It is important that the community is confident about the extent of the costs and benefits associated with NCP reforms. In Western Australia this has been achieved through a rigorous and independent public interest test. This has led to community confidence in the test being applied fairly, and also that the resulting policy outcome has been justified.

How the interests of the whole community are assessed and determined is therefore a critical factor in implementing NCP reforms and more importantly the success of those reforms. In this regard the public interest test has been criticised for being too ‘narrow’ in its focus – this criticism is misguided.

The ‘public interest test’ is contained in clause 1(3) of the *Competition Principles Agreement* and includes a wide range of factors relevant to evaluating community benefits and costs. These include the environment, employment, social welfare and consumer interests as well as business competitiveness and economic efficiency. The public interest test was finetuned following the 2000 COAG review.

Social and environmental matters in the public interest test have as much status as financial and economic considerations. However, the weight of each public interest criterion will vary depending on its contribution to the overall costs and benefits of proceeding with the particular reform. The list is also non-exhaustive, meaning that any other relevant matter can also be considered when assessing the merits of a particular NCP reform. In Western Australia the economic, social and environmental factors relevant to making an assessment of the public interest must be explicitly accounted for in each review.

The public interest test is challenging to apply. This is because the criteria that need to be considered are not always easily quantifiable and sometimes move in opposite directions in response to reform proposals, making the final assessment of public interest subjective and value-laden. The final assessment will depend on

how the criteria that improve as a result of reform are weighted against those that are worsened. This is why the NCP framework recognises that public interest assessments ultimately require political decisions.

Application of the public interest test has probably been the cause of most criticism rather than its 'narrow' definition. In many instances the most vocal critics of the public interest test have been those groups who have had the most to lose from the recommended reforms; citing their interests were not given sufficient consideration.

Hence, strong government leadership is required to focus on the interests of the general community, to communicate the benefits of reform in a robust manner, and to explain the public interest reasons justifying the reform.

Notwithstanding these challenges it is imperative that public interest continues to be the underlying foundation of the NCP framework. To justify NCP reforms on a narrower measure of public interest, say the efficient allocation of resources, would lead to inferior public interest outcomes.

The following case study provides an example of the complex range of social and economic factors that must be weighed by Government in coming to a public interest decision on the deregulation of retail trading hours.

#### **Case study: Deregulation of retail trading hours**

In June 2003 the Western Australian Government decided to extend weeknight trading (Monday to Friday) to 9pm for all general retail stores in the metropolitan area. The extension of weeknight trading will come into effect four weeks after the next general State election, due in early 2005.

The Retail Shops and Fair Trading Legislation Amendment Bill was introduced into the Legislative Assembly to effect these changes on 15 October 2003. The Western Australian Government heard and took account of the views of all contributors to the debate on retail trading hours; this was clearly outlined by the Minister for Consumer and Employment Protection (2003) in the Second Reading Speech of the Bill:

*"The amendments recognise the evolving consumer expectations and changing patterns of employment, together with the social framework of modern society. The changes also recognise there is little consensus in the community about the issue of retail trading hours or about the role, if any, that Government should have in determining retail trading hours.*

*Arising from its review of trading hours, the option of easing restrictions on weeknight trading after the next election has been preferred as an appropriate response to the competing needs of the consumer and both big and small business. The*

*extension of general trading hours until 9.00pm on weeknights will provide consumers in metropolitan Perth with access to 12 hours more shopping hours per week. This is an increase of 19 per cent over those currently available.*

*The Government considered the option of introducing Sunday trading but decided that this was not in the overall public interest for reasons which include concerns about the impact of Sunday trading on the leisure and family time of workers in the retail sector. This applies to not only employees of large retail stores but also owner-managers of small retail stores.*

*There is also concern about the potential for coercive employment practices that force people to work when they wish to keep Sunday free for purposes of religious observance, participation in sport or other family or recreation pursuits.*

*Small retail business is a key part of the Western Australian economy. The competitive advantage of having extended trading hours assists small retail shops to continue competing with larger chains. The benefits to the economy include supporting local suppliers and flow-on benefits to the economy. The wholesale deregulation of trading hours, including the introduction of Sunday trading, would force owner-operators to spend more time working with a negative impact on familylife.*

*In addition, it is important to recognise there is a significant degree of Sunday trading already available, so consumers already have the opportunity to shop on Sunday if they wish. Consumers have access on Sundays to the tourism precincts as well as community and suburban markets."*

The Western Australian Government is of the view that the restriction on Sunday trading provides a net public benefit to the community.

## Managing Change

### **Taking account of distributional impacts and adjustment costs**

To be successful in implementing reform it is imperative that governments understand the distributional and adjustment implications of reform. Criticism has been prominent in regional areas and while much of this criticism has been inaccurate, and there are instances of significant regional benefits, some people within certain regional communities may have less to gain from NCP.

For these reasons it is imperative that the implementation of NCP reforms are sensitive to the effects on local communities. Transitional arrangements and/or adjustment assistance should be considered where regional impacts are acute. Such sensitivity will go some way to ensuring that reforms in the interests of the whole community still take place despite any negative local/regional impacts. COAG (2000) was cognisant of this relationship when it fine-tuned the arrangements for NCP in November 2000.

While the benefits of reform to the community are usually large they are also generally diffuse and sometimes take time to be fully effective. On the other hand, the costs of reform tend to be more localised and quicker to impact specific communities. In response to this reality governments undertook to consider identifying the likely impacts of reform measures on specific industry sectors and communities, including the expected costs of adjusting to change, when examining the public interest matters under clause 1(3) of the Competition Principles Agreement (COAG 2000).

It is important to note that that consideration of the impact on industry sectors and communities was always implicit in the NCP public interest test. COAG's decision just made such considerations explicit, addressing any perceptions that NCP processes ignore the impacts of change.

Consistent with COAG's direction the Western Australian Government revamped its legislation review guidelines in November 2001. The new guidelines made it mandatory for all reviews to explicitly address the impact of change on those sectors of the community that may be worse off as a consequence of reform and examine transitional arrangements as a means of smoothing the adjustment burden.

Western Australia has had some recent experience in assisting people to adapt to change in response to NCP reforms. Two pertinent case studies are in relation to the deregulation of egg marketing and the release of additional taxi plates.

### **Case study: Deregulation of egg marketing**

Where the social welfare system is not sufficient specific adjustment assistance may be warranted. Adjustment assistance can be justified where significant long-term costs are borne by an identifiable section of the community who would suffer significant hardship in the absence of such assistance. For example, where reform impacts are severe and are concentrated on regions where there is little opportunity for alternative employment.

On the 4 June 2004 the Agriculture Minister announced an \$8.75 million assistance scheme for egg producers to coincide with the transition to a deregulated egg market.

A Transition Advisory Committee had been working on the proposed changes since September 2003. In 2003, the Western Australian Government announced its intention to deregulate the egg industry by July 2007, but unfortunately this timeframe was not acceptable to the NCC and had to be brought forward to avoid competition payments penalties.

Under the reforms the monopoly marketing powers of the Western Australian Egg Marketing Board will be removed allowing egg producers to sell their eggs directly to wholesale markets and allowing independent processors to enter the industry to acquire eggs from Western Australian producers and sell them. In addition, the quota system that limits the production of eggs in Western Australia will be eliminated which is likely to result in the price of eggs being reduced.

The State Government recognised that moves to deregulate the market and cancel licences with hen quotas would have a significant impact on 107 licence holders with base hen quotas under the *Marketing of Eggs Act 1945*. The \$8.75 million adjustment assistance package recognises the impact of the repeal of the Act on the licences and quotas administered by the Board and proposes assistance to be paid to producers in proportion to base hen quotas.

### **Case study: Release of additional taxi plates**

Adjustment assistance need not necessarily be financial. Governments can also assist those adapting to change by the provision of advice on financial and business management, training and development and providing speedy access to government social services. It can also include the phased implementation of reforms or a grace period before a reform is implemented to allow affected parties to plan for the new environment and provide a degree of certainty.

Phasing of reforms has proven successful in reducing opposition to taxi industry reform. Perth taxi customers and taxi drivers are benefiting from the State Government's commitment to the staged release of additional taxi plates into the Perth market over the next five years.

The scheme has three objectives:

- to give drivers the opportunity to be owner-operators;
- to meet increased public demand for taxi services; and
- to reduce cost structures, therefore reducing pressure on fares.

On 15 December 2003 the Taxi Amendment Bill 2003 was assented to, allowing licences to be leased rather than sold by tender. Soon after the Government advertised 48 lease licences (32 conventional, 12 peak-period and four multi-purpose taxi plates) direct to drivers. These were the first new full-time taxi plates released for 14 years.

On 10 June 2004 the Minister for Planning and Infrastructure<sup>3</sup> announced that 10 conventional taxi plates, 10 peak-period taxi plates and eight multi-purpose taxi plates will be made available on a tender basis. A further 28 conventional and peak period taxi plates and 12 multi-purpose taxi plates, will be made available each year from 2005 through to 2008.

The plate release program should also meet the obligations of the State under NCP ensuring competition payments are retained.

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<sup>3</sup> See Press Release by Minister for Planning and Infrastructure, "Additional taxi plates will improve customer service and industry certainty", 10 June 2004.

## Unfinished Business

### **Structural reform in the electricity industry**

For Western Australia there is much to be gained from completing the NCP agenda. While there still remains some progress to be made on legislation review, by far the most important area of NCP to progress is structural reform because this will have by far the greatest potential impact on the economy. Research has shown that electricity reform in Western Australia could see an 8.5% fall in electricity prices, \$300 million per annum increase in Gross State Product and 2900 additional jobs created by 2010 (Electricity Reform Task Force 2002).

In recent years Western Australia has continued to progress energy reforms in accordance with its commitments and obligations under NCP. The current reforms build on those reforms that preceded NCP, such as the separation of the State Energy Commission of Western Australia into Western Power and AlintaGas.

Under the current industry structure the Government-owned corporatised business entity, Western Power, is the primary provider of electricity services in Western Australia. Electricity is distributed via two major interconnected transmission and distributions systems – the South West Interconnected System (SWIS) and the North West Interconnected System (NWIS) – and 28 isolated regional systems. Within Western Power four specific business units (generation, networks, retail and regional) provide services to the community. The remainder of the electricity industry is characterised by a number of private companies throughout the State that generate electricity primarily to supply their own mining, mineral processing or other operations and in some instances townships.

Despite not being able to participate in the national electricity market, Western Australia continues to support the need to reform the electricity industry and to introduce competition. Impediments to competition are being removed in the wholesale and retail sectors of the industry, access to the transmission and distribution systems is provided for in legislation, the number of contestable customers is being increased and private sector involvement in the industry is being promoted.

To promote greater competition and sustainable lower electricity prices, the Government established the Electricity Reform Task Force (ERTF) in August 2001 to develop a framework for further reform of the State's electricity supply industry. The ERTF's final report, submitted in October 2002, recommended the



creation of a new electricity market that balances the need for greater competition, lower prices and consumer protection. Specifically, the report recommended:

- the creation of a wholesale market;
- a strong and independent regulatory system;
- the disaggregation of Western Power into four new entities; and
- the retention of the uniform tariff as a safety net and existing rebates.

The ERTF's review and proposed structural and regulatory reforms accorded with Western Australia's obligations under clause 4 of the *Competition Principles Agreement*. Particularly in regard to:

- separating regulation for the electricity industry from Western Power's enabling legislation;
- separating the monopoly elements from potentially competitive elements of the industry (i.e. vertical disaggregation);
- ensuring competitive neutrality is achieved and ensuring transparent funding arrangements for the delivery of community service obligations.

The Government endorsed the recommendations of the ERTF in November 2002 and began drafting legislation to implement its recommendations.

The *Electricity Industry Act 2004* was assented to on 23 April 2004. The Act creates a wholesale electricity market, provides for the development of an electricity access code, and establishes an independent licensing regime and consumer protection measures. The Act provides greater opportunity for the development of competition in the generation and retail sectors of the electricity industry.

Unfortunately the second plank of the Government's electricity reform, the Electricity Corporation Bill 2003, failed to progress through Parliament because the opposition parties that control the upper house refused to support it. The Bill would have led to Western Power's activities in the SWIS being vertically disaggregated into three independent entities – State Generation, State Networks and State Retail – and the establishment of a fourth entity, the Regional Power Corporation having responsibility for the NWIS and Western Power's non interconnected systems.

Until Western Australia fully reforms the electricity industry Western Australian businesses and households will continue to pay more for their electricity than

businesses and households in the majority of other states<sup>4</sup>. However, the Government remains firmly committed to the disaggregation of Western Power and intends to reintroduce the disaggregation legislation after the next election. In the interim, the Government is considering the most effective measures to mitigate Western Power's vertical and horizontal market power.

### Structural reform in telecommunications

Past reforms of Commonwealth Government legislation have made significant contributions to increased competition in the telecommunications industry and delivered some price and choice benefits to consumers.

The introduction of the *Telecommunications Act 1997* allowed full competition in carriage services and the amendments to parts XIB and XIC of the TPA, the Telecommunications Act and the *Telecommunications (Carrier Licence Charges) Act 1997* in 2002 improved the efficiency of the regime regulating access to telecommunications network facilities.

However it appears that further significant gains to consumers do not seem possible unless the Commonwealth seriously considers what other actions need to be taken to promote additional competition.

According to the ACCC (2003) while Telstra no longer has a monopoly position in the telecommunications industry it is still one of the most integrated communications companies in the world. It continues to be the major wholesale and retail supplier of telecommunications in Australia, including:

- local, national, long-distance, international and mobile voice;
- dial-up and broadband internet;
- data;
- printed and online directories; and
- pay TV (through its 50% ownership interest in Foxtel).

The ACCC (2003) said:

*“the extent of Telstra’s dominance of the sector is demonstrated by the fact it receives almost 60 per cent of total industry revenue, which is almost four times the revenue its closest rival, Optus, receives. It is reported to receive over 90 per cent of industry profits.”* (page XV)

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<sup>4</sup> See Press Release by Minister for Energy, “WA electricity prices a handbrake on economy”, 25 February 2004.

It would appear that Telstra's existing structure does not facilitate competitive outcomes consistent with the public interest. The NCC (2003a) said:

*"The Council remains of the view that achieving a competitive telecommunications industry capable of delivering substantial benefits to consumers may require the Government to further consider the structure of Telstra, including the option of the structural separation of the fixed network."* (page 11.13)

The Productivity Commission should give high priority to examining what further action needs to be taken in the telecommunications industry to facilitate greater competition. There would appear to be significant public interest justification in separating Telstra's natural monopoly elements from its competitive elements consistent with clause 4 of the *Competition Principles Agreement*.

### **Impediments to achieving unfinished NCP reforms**

A significant impediment to completing the current NCP agenda is the power and influence of business lobby groups. These lobby groups tend to be more influential and successful with governments than consumers or consumer groups.

These special interest groups generally have more to lose from NCP reforms than individual consumers within the community stand to gain from reform. As a consequence such interests have much stronger incentives to gain political support. For consumers, an NCP issue in isolation is unlikely to be significant enough to influence their voting patterns. In other words, the votes of vested interests will 'swing' on NCP issues, the votes of consumers will not.

Another impediment to achieving NCP reform is the media continually focusing on, and giving more significance to, the interests of the identifiable and vocal losers from NCP reforms, rather than the 'anonymous' wider community who are generally the winners from NCP reforms. This media bias tends to result in even some of the winners from the general community supporting anti-competitive regulation that is not in the public interest.

The influence of vested interests is often not recognised by the community and those groups are often skilled in presenting arguments which can gain wider public support. Vested interests in some cases maintain that legislation that prevents the entry of new competitors is for protecting the community from a social harm that will arise if new competitors are allowed to enter the market, without disclosing their interest in avoiding competition.

The Productivity Commission should reaffirm the need to complete the unfinished business of NCP, in particular structural reform and the legislation review program. This will send a clear signal to vested interests that they should perhaps start to focus on competition and innovation rather than rent-seeking behaviour.

The Productivity Commission should also give some thought to processes for encouraging and nurturing a well organised and well-resourced consumer advocacy group in Australia. The specific focus of such a group should be on encouraging competition in markets for the benefit of consumers since it is recognised that consumer protection is undertaken by government agencies. A strong consumer advocate could provide an effective counterweight to vested interest groups, exposing the flaws in their so-called ‘public interest’ arguments that defend the status quo. Obviously, serious consideration would have to be given to how such a consumer group should be funded, to how its independence would be protected, and the extent of its consumer representation - to ensure that it does not become just another narrow vested interest.

### **Case study: Liquor licensing reforms**

On 1 September 2003 the Government announced reforms to the *Liquor Licensing Act 1988* that would allow liquor stores to trade on Sundays. In addition, the reform package also proposed the public ‘needs’ test (i.e. licence applicants must show a public need for a new liquor outlet in relation to services already existing in the locality) be replaced by a public interest test<sup>5</sup>.

The effect of the proposed reforms would have been to increase competition in the liquor industry to the benefit of consumers. The reforms were also consistent with Western Australia’s NCP obligations.

However, the Government’s proposed legislation dealing with liquor licensing reforms met with strong resistance from the Australian Hotels’ Association and opposition from the Liberal Party and Greens.

Since the NCP amendments were unlikely to be supported in the upper house the Premier announced the Government would not be proceeding with the amendment of the Act during the current session of Parliament. Instead, the Government will appoint a committee to review the Act<sup>6</sup>.

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<sup>5</sup> See Press Release by Minister for Racing and Gaming, “Liquor stores to get green light for Sunday trading”, 1 September 2003.

<sup>6</sup> See Press Release by Minister for Racing and Gaming, “Committee to review liquor licensing laws”, 15 June 2004.

## Improvements to the Existing Reform Framework

There are a number of areas where a case can be made for some improvements to the existing NCP reform framework. This section outlines four issues that the Productivity Commission could examine in further detail. The results of the Productivity Commission's work could then inform COAG's own review of NCP arrangements that is due by September 2005.

### **New approach for legislation review**

The approach agreed to by COAG (1995) for legislation review has not functioned effectively. Sovereign governments have been prevented from implementing NCP within their jurisdictions as they have seen fit. Rather than suffer financial penalty, some governments have felt they have had no choice but to comply with the Commonwealth's demands. This has not only weakened democratic processes but also led to confusion over which tier of government is accountable for the decisions made on NCP. An approach that maintains jurisdictional sovereignty while still producing NCP outcomes in the public interest is what is required.

For arguments sake, perhaps an approach similar to the one outlined in the National Gas Code would have delivered improved legislation review outcomes across jurisdictions. Under the National Gas Code jurisdictions agreed on a policy framework and uniform legislation to implement reform. All jurisdictions introduced the uniform legislation and it took account of jurisdiction-specific concerns through transitional arrangements and derogations, which are only allowed if they have been approved by other jurisdictions.

If a similar framework were applied to legislation review it would be up to each individual jurisdiction to convince the other jurisdictions why an NCP reform outcome in that particular jurisdiction should differ from the norm. Such 'peer appraisal' may have been less contentious and led to better reform outcomes than under the existing framework that has led to confrontation between the States (and Territories) and the NCC.

The Productivity Commission could examine whether alternative NCP assessment processes, particularly for legislation review, have the potential to deliver better public interest outcomes.

### **Materiality test for legislation reviews**

With the benefit of hindsight there has perhaps been too much emphasis placed on legislation reviews that were not material, and that this issue could be resolved by the inclusion of a materiality test in deciding if legislation review is warranted.

This would tend to moderate some of the concerns expressed by Western Australian Government agencies with NCP processes, including:

- the time (resources) required for completion of NCP reviews;
- the depth and detail of review activity required for every piece of new and amending legislation; and
- the cost of obtaining the required review expertise within agencies.

A well-designed materiality test should not be controversial as long as gatekeeping processes are sufficiently robust to ensure that significant restrictions on competition not in the public interest are identified before any new legislation is introduced.

It would be important to ensure that the conclusions of any materiality test are based on analysis rather than just assertion; this is particularly the case where the agency conducting the test has little incentive to recommend undertaking a comprehensive legislation review.

The Productivity Commission could examine whether a materiality test, particularly for legislation review, has the potential to deliver public interest outcomes in a less costly manner.

### **National review process should be fine-tuned**

NCP provides the scope for national reviews to be undertaken where a review has a national dimension or effect on competition under clause 5(7) of the *Competition Principles Agreement*. However, very few reviews have been undertaken on a national basis and where they have been undertaken the reform outcomes have been mixed at best.

There are pros and cons with national review processes. On the one hand national reviews should be cheaper to conduct and they can improve regulatory consistency across jurisdictions reducing compliance costs for both business (particularly professionals) and consumers. On the other hand, national reviews can lead to too many compromises in the negotiations between jurisdictions over the final review outcome. This 'lowest common denominator' problem can result in review outcomes that fail to deliver best practice regulation.

In addition the national review model carries the risk of complete regulatory failure, whereas a jurisdiction-by-jurisdiction approach facilitates 'policy learning'

as each jurisdiction adopts the best practice innovations of the others over time (NCC 2004).

Using the lessons learnt from the national reviews undertaken already, the Productivity Commission should examine how the national review process can be fine-tuned to consistently deliver best practice regulation.

**Greater transparency in review processes is needed**

While many review reports of existing legislation have been published, there is no NCP obligation to publish them, or even make them available to the NCC. In Western Australia it is up to the responsible Minister to decide whether a review report is made public. However, in all instances in which the NCC has requested review reports, the relevant Western Australian Minister has complied.

Transparent processes are crucial when assessing the public interest. Without transparency it is extremely difficult to gain the community's confidence that public interest considerations have been examined in an impartial manner and that it is the community's interest that is the overriding concern rather than any particular sectional interest group when deciding whether a reform should or should not be progressed.

## Extending a Formal NCP-type Framework to other Areas

### **A new reform agenda**

Western Australia supports the views of the Victorian Government (2004) that any future reform agenda must be strongly based on a substantial and credible case for the need for reform. NCP was based on a strong foundation (i.e. the Hilmer Report), any new national reform agenda must be equally strongly based. Jurisdictions should make no commitment for further reform until a substantial and credible case for the need for reform is made.

If a strong case can be made for a new reform agenda, there must be robust boundaries around jurisdictions' agreed obligations. Any new reform obligations must be accompanied by new payments from the Commonwealth to ensure the gains from the new reform agenda are appropriately shared and governments do not face disincentives to reform. New incentive arrangements would be totally separate from existing payments which must continue under the current agreements.



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