Productivity Commission

Review of National Competition Policy Arrangements

Submission by the
Independent Liquor Stores Association Inc.

July 2004

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1. Introducing ILSA

The Independent Liquor Stores Association Inc. (ILSA) was founded on the realisation, by a small group of independent liquor store owners in NSW, that the long established industry associations were no longer effectively representing their interests. The aggressive acquisition strategies of the two major supermarket chains, and the focus on gaming in the on-premise sector, had created a need for an association to represent the small, family owned packaged liquor sector in terms of public profile, political lobbying, negotiation with regulatory authorities and liaison with the media.

The growth of ILSA's membership has confirmed that the decision to form a new association was indeed justified. In the eighteen months since ILSA became active, the membership has increased from six (6) to almost two hundred (200) Ordinary Members. Associate Members from the beer, wine and wide-range wholesaling supply sectors have also joined as their future success also depends on a viable independent sector.

ILSA is now recognised as a key industry association. Although ILSA has concentrated on representing NSW licensees, the issues demand a national, as well as state approach. Submissions have been made responding to the National Competition Policy Review and also to the ACCC. ILSA is a member of the Fair Trading Coalition addressing the area of Trade Practices, and we have communicated with the Federal Government at the highest level and will continue to do so. The impending removal of the "needs test" from the NSW Liquor Act has been the issue of primary importance to ILSA since inception. It is therefore most appropriate that we make input into the Productivity Commission's Review of NCP arrangements and we appreciate the opportunity and the extension of time to allow this to happen.

2. Background

2.1 "Needs test" removed – replaced with Social Impact Assessment

Regulation of the supply of liquor in NSW depends on the "needs test". The "needs test" is the term used to define that part of the liquor legislation that allows objections to a new licence application on the basis that the need of the community in the neighbourhood is already being satisfied by existing licensed outlets. Following five years of indecision and procrastination by the NSW Department of Gaming and Racing (the bureaucratic arm of the NSW Government with responsiblilty for liquor licensing), five years of fear and uncertainty for the holders of liquor licences, five years of speculation, conjecture and media coverage, intense lobbying at all levels by industry associations, concerns expressed by health, police, roads and traffic, indigenous persons, education, religious, social service and other groups, a Bill to remove the "needs test" was passed on 22 June 2004. During the same period there has been a massive increase in the market-share of the two major supermarket chains through mergers and "creeping acquisitions"

In the end, the single deciding factor for the NSW Government was the imposition of financial penalties by the Federal Treasurer, penalties recommended by the National Competition Council (NCC). The Government's priority was to avoid the penalties, rather than to revisit the failed legislation review process in order to achieve the best outcome for the wider community. The liquor laws were changed and the Government's liquor policy reversed.

The Bill was passed by the narrowest of margins having endured a long (five months) and rocky passage through the parliament. There were only two groups that overtly supported the Bill, the Liquor Stores Association of NSW, whose two chain store members Liquorland/Coles and Woolworths constitute a clear majority of the packaged liquor outlets this association represents, and the Australian Hotels Association, convinced that the Social Impact Assessment (SIA) Process that replaces the "needs test" will be at least as effective as the "needs test" in preventing a proliferation of new on-premise licences (pubs).

The Government acted on an understanding from the National Competition Council that the new legislation, which relies on the SIA Process, will comply with NCP principles and NCP penalties will be rolled back. It may be argued, however, that the SIA Process simply replaces one restriction on competition (the "needs test") with another restriction. The SIA Process has been designed to be sufficiently arduous as to deter new entrants to the industry. ILSA's view is that the major difference, in practice, will relate to applications for off-premise (packaged liquor licences), where the SIA Process will be even more prone to manipulation by the two major supermarket chains than the arrangements that existed under the "needs test".

Although the Prime Minister intervened on behalf of pharmacy and brokered a compromise between the NCC and NSW, in order to prevent this retail sector being invaded by the two major supermarket chains, he chose not to do so for the independent liquor sector.

2.2 NCC recommends penalties because NSW made no report

The predisposition by the NCC to discontinue the "needs test" was welcomed by the senior bureaucrats in the NSW Department of Gaming and Racing back in 1999. Senior bureaucrats from the Department saw this as an opportunity to deregulate the retail supply of liquor and remove what they viewed as an undeserved "privilege" enjoyed by existing licensees. The Department's support for deregulation was made clear in the Discussion Paper of June 2002, opposing the policy of the political arm of Government, as articulated by the Minister and later by the Premier, that regulation and the "needs test" should remain. Despite detailed, professional (and costly) submissions from industry that made a persuasive case for retention of the "needs test" in the public interest, the NSW Discussion Paper recommended discontinuation of the "needs test" on the basis that its primary function was to protect the market-share of existing licensees.

The NCP legislation review as it related to the NSW Liquor Act 1982 was flawed because the review did not take place under a properly constituted process as required by NCP Agreements. The review was not conducted transparently by an independent panel with provision for public participation. The original panel that did include industry representation was abandoned and replaced with a panel comprised solely of Government appointees from Cabinet, Treasury and the Department of Gaming and Racing. The deliberations of this review panel took place in secret. After the Discussion Paper was issued, there was no public (or industry) participation or consultation. The so-called "discussion paper" was never discussed. There was no response to submissions by industry and others as to whether the review panel had been persuaded by the views put forward and subsequent requests to the Government to be informed of developments in relation to the outcome of the review were denied. If there was a report emerging from the review, it has never been released and more importantly was not submitted to the NCC. Under these circumstances, it is reasonable to assume that the findings of the review were politically unpalatable to the Government.

In the absence of any proper report that met the standards for NCP reviews outlined in NCP agreements, the NCC relied on the Discussion Paper of 2002 and this led to its decision to recommend financial penalties on NSW for non-compliance in relation to liquor retailing legislation.

3. Terms of Reference and Issues Paper

3.1 Treasurer Costello refers to the Productivity Commission

The Terms of Reference, referred to the Productivity Commission by Treasurer Peter Costello on 23 April 2004, state under "Background 1." as follows:

There has been substantial progress in the implementation of NCP over the past eight years, including in the related areas of electricity, gas, road transport and water. This has delivered significant benefits to Australia.

and then under "3."

It is therefore timely to undertake an independent review of these arrangements to consider the extent of the benefits the reform program has delivered to date..

ILSA accepts that the NCP arrangements have delivered benefits in these areas, however the NCP Legislation Review of liquor legislation in the state of New South Wales has been less than successful. The review program failed the people of NSW (the wider community) and independent liquor retailers, the holders of existing licences, mainly family owned businesses. The only winners will be the major supermarket chains.

Notwithstanding that Treasurer Costello's Terms of reference are framed in optimism, it is incumbent on the Commission in conducting its independent enquiry, to consider not just the positive impacts, but also the negative impacts.

This submission will try to avoid arguing the merits or otherwise of deregulation of liquor and attempt to follow the terms of reference and the issues paper and explain to the Commission how the NCP Agreement, Arrangements and Legislation Review Program have denied the liquor industry and the wider community an opportunity to present their case for continued regulation of liquor in NSW in the public interest.

3.2 Impact of NCP and related reforms to date (Issues Paper pages 5,6)

The paper speaks positively regarding Australia's economic performance. The Commission needs to put the liquor sector into perspective. Increased productivity and consumption of liquor supplied to the domestic market at lower prices, whilst they may serve to contribute to Australia's higher economic performance by economic measures, would not be considered a socially desirable outcome, by Governments and others, and would certainly not be perceived as being in the "public interest".

The emphasis of NCP on improved economic outcomes does not fit with the liquor industry. There is a widely held view that liquor should be exempted

because of this conflict between the social and health impacts, the primary concern of all governments in relation to liquor, and the economic based goals that drive NCP. The National Competition Council has not recognized this fundamental difference between liquor and other products. This is not to say that competition is anything less than fierce in what has always been one of the most highly contested retail sectors.

The wider community has become more responsible in its approach to the use of alcohol products and in fact per-capita consumption in Australia and other Western countries continues to fall incrementally year after year. In Australia this is due in no small way to regulations (such as the "needs test") that have worked to control outlet density and control the overall licence number to that which is actually needed by the community.

Pages 5 and 6 list various (mainly positive) outcomes and poses questions. In the area of packaged liquor retailing, there have been no benefits and ILSA believes the impacts will be negative in future years in terms of:

> Competition
> Reduced competition as small business exits.
> Lower productivity as suppliers are squeezed.
> Higher prices as the duopoly becomes entrenched.
> Limited choice of outlets.
> Limited product range.
> Public Interest
> Erosion of standards of responsible service in the supermarket check-out environment.
> Increase in the abuse and misuse of alcohol as outlet numbers increase, personal responsibility diminishes, inspections become more difficult.

3.3 The Commission's approach (Issues Paper page 4)

ILSA has concerns regarding the following comment:

> *This community-wide framework (the Australian community as a whole) implicitly recognises that policy change can involve both winners and losers, benefits and costs. While the costs imposed on some groups need to be taken into account, they do not provide a justification for forgoing reforms where the costs are significantly outweighed by benefits to the wider community.*

It would be unfair if the above rationale encouraged the Commission to regard the impact on the independent, packaged liquor sector, clearly "losers" under NCP arrangements, as justified on the basis that removal of perceived restrictions and "barriers to entry" provide a net benefit to the wider community.

The real loser will in fact be the wider community, of which our members are only a part.

3.4 "Losers" include other states and other retail sectors

The NSW liquor deregulation experience has been virtually replicated in principle and in practice in all of the other states and territories (except Queensland). Also, for the purposes of the Commission's enquiry, the "losing group" should also include other retail sectors that are (were) regulated because of the special services they provide to the community, including pharmacy, dentistry and optometry. ILSA hopes that the Productivity Commission will give our submission a high level of priority due to the size of this group and the negative impacts caused by the determination of the Council to pursue the theories of NCP by strict application of NCP arrangements.

4. Unfinished business (Issues Paper pages 7,8,9)

4.1 Efficiency of Reviews

Question: Have aspects of NCP processes (for example, the requirement for separate State and Territory legislation reviews of common issues) been inefficient and/or contributed to the time taken to complete the agenda?

In hindsight, it would have been preferable, in terms of consistency and efficiency, for the Legislation Review process to somehow draw together, state and territory representatives (of industry for example) so that reviews of specific sectors could be conducted on a National basis. In the area of liquor licensing, the early removal of the "needs test" in Victoria was used as leverage by the NCC to encourage and persuade other states and territories that this was the "right answer", the lowest common denominator. In hindsight, a reading of the report from the Victorian Review raises questions as to whether the fundamentals and possible consequences of NCP were fully understood at this time. The Victorian experience has seen increased outlet numbers, decimation of the independent sector and no advantage to consumers.

4.2 Incentive Payments

Question: Is the current NCP framework (its legal underpinnings, processes, institutions and incentive payments) the most effective way of progressing and extending competition reform and "locking in" worthwhile changes that have already been made?

The short answer must be a resounding NO if the review of liquor legislation in NSW is taken as a case in point.

Briefly, the reasons are as follows:

1. From the very earliest stage of the liquor legislation review program, it was obvious that the NCC had formed the view that the "needs test" should be discontinued.

2. This view was embraced by the NSW Department of Gaming and Racing and despite that this view was not Government policy, the die was cast.

3. A "properly constituted review process" never took place and the Report of the findings of the NSW Liquor Review were never released, nor submitted to the NCC.

4. Finally penalties for non-compliance in the area of liquor (and pharmacy etc.) were recommended by the NCC and imposed by the Federal

Government, despite the conviction of the Carr Government that the "needs test" should be retained in the "public interest", and protestations to the Federal Government

5. The law was changed and the "needs test" removed to avoid the penalties.

6. As a result, the wider community (including industry) was denied any effective input into the NCP legislation review program.

4.3 Modifications and Improvements

Question: What modifications to the present framework would improve its operation?

This is of course the key question for the Productivity Commission and this is the main focus of our submission. The NCC has tremendous power – it is independent of the executive arm of governments. This power should be curtailed in the area of private enterprise and in particular sectors in which large numbers of small businesses operate. This could be achieved by changing some of the fundamental principles and processes of NCP and the following suggestions are intended to encourage a wider view of possible alternatives..

4.3.1 Penalties too great

Unfortunately perhaps, money is power. The "big stick" approach, the threat of financial penalties for non-compliance that are so large, as to allow the NCC to force its view of the world on democratically elected governments, amount to a gross misuse of power and offend against our constitutional democracy. As Premier Carr stated, the penalties represented "a gun at our head".

4.3.2 Changing laws to avoid penalties should not be permitted

Conversely, the current arrangement, that allows a government that has failed to conduct a proper review process, to avoid penalties by simply changing policies or laws, to take the easy way out, does a disservice to the wider community, the voting public. This should not be permitted as an alternative remedy for governments in future.

4.3.3 NCC responsible for "proper" reviews

ILSA believes that, had a "properly constituted review process" been conducted, the conclusion would have been that the "needs test" should be retained. The ILSA view was shared by the NSW Government, however the NCC forced its own agenda (via the Federal Government), refusing to accede to NSW's request for time to consider the outcomes of it's Alcohol Summit or to revisit the legislation review process and make a proper case for retention of the "needs test" in the "public interest".

All State and Territory Governments should be made to conduct NCP legislation reviews in accordance with "properly constituted review process". It should be the responsibility of the NCC to ensure that this takes place, and the NCC should be held accountable if it does not.

4.3.4 Fines - not Penalties

Failure by governments to complete proper reviews should continue to result in fines, however the quantum of these fines, should be set at a reasonable level, a level that encourages compliance with the requirement to conduct legislative reviews in a proper and timely manner. The fines should be defined specifically in terms of their quantum, the time frame for their imposition and the specific legislation to which they relate. Fines should not be contingent on negotiations or discussions between the government parties to the NCP Agreement and should be transparent and not hidden in the "fine print".

4.3.5 NCC must become "hands on"

The Council's current approach to legislation review performance, which is to "consider whether review conclusions are within a range of outcomes that could reasonably be reached based on a 'properly constituted review process'", is ineffectual and vague and too far removed from the facts of the particular legislation subject to review. Under the current NCP arrangement, the NCC is the judge and jury with the power to impose the sentence (the Federal Government is the executioner in this scenario), however the NCC does not conduct the review of legislation or take part in the legislative review process. Further, it does not prepare, or comment on, submissions to legislative reviews, leaving these tasks to review panels with access to relevant expertise. ILSA suggests that if the NCC is to continue making recommendations that influence changes to the law, then the NCC must take some responsibility for those decisions. The NCC must become fully cognisant of every aspect of each legislation review, including in particular all public submissions to the review.

4.3.6 "Presumption" in favour of legislation, not competition

There is is a fundamental issue that must be questioned above all else. The NCP is predominately based on a presumption in favour of competition (and against regulation). This presumption is not appropriate for those special retail sectors such as liquor (and pharmacy, dentistry, optometry etc.) that are regulated for good reason. In these industry sectors there should be a presumption in favour of regulation; a presumption that the laws put in place by elected governments, having regard to the will of the people and the circumstances particular to the individual States and Territories and refined over many years, are good laws. Taking it one step further, no individual, no corporation, no judiciary, no bureaucracy, certainly no "council" should regard the law with anything other than respect. To hold a "presumption" in favour of competition, justified by theories, propped up by experiences in other places - against existing legislation and regulation (in other words the law of the land), is to treat the law with contempt. In this country people are still innocent until proven guilty. The same principle

should apply to our laws – they should be regarded as right, unless proven wrong.

4.3.7 Governments should consult NCC

Having said that, it should be compulsory for Governments to seek the advice of the NCC in relation to legislation that is perceived by the NCC as restricting competition and this liaison and interchange of views should become an essential part of the legislation review process in future.

4.3.8 Disputes resolved by COAG

Following such consultation, should the NCC be dissatisfied with a Government's refusal to change legislation to remove a restriction, perhaps the matter in dispute should be referred to a meeting of the Council of Australian Governments (COAG). Appropriate consideration may then be given to the desirability of consistency across all states and territories. It may be considered appropriate that the final decision be determined in formal session by a vote of all COAG members, with the state or territory government, whose legislation is under consideration, abstaining from the vote.

5. Specific questions for the Commission

Responding to questions from ILSA, the NCC in a letter dated 6 February 2004 clarified as follows:

> *The Council does not conduct the review of legislation. Further, it does not prepare, or comment on, submissions to legislative reviews, leaving these tasks to review panels with access to relevant expertise.*
>
> And,
>
> ***The Council was not provided with copies of responses by interested parties to the New South Wales review's discussion paper and would not see it as appropriate to comment on these responses.***
>
> And finally,
>
> ***The Council does not base its assessments on government's 'submissions' which clearly would not meet the standards for NCP reviews outlined in the NCP agreements.***

Comments in the 2002 NCP assessment report relating to the NSW progress in relation to liquor are of great concern as they appear to conflict with the above policy position. The 2002 NCP assessment states in part:

> *While New South Wales has not completed its review and implemented appropriate reform by the COAG deadline of 30 June 2002, the date for completion of the liquor licensing review is imminent.* ***Moreover, the discussion paper prepared for the review clearly recognises that there is a significant question about the contribution of the current needs test to delivering the harm minimisation objectives in the legislation. The discussion paper concludes for example that most benefits of the current needs test arrangements flow to existing operators of liquor businesses, because restriction on the number of licensed premises in a given local area helps to protect the market share held by existing licensees. Other evidence provided to the Council supports this acknowledgement by the discussion paper. One party for example told the Council that in a rural town of more than 3000 inhabitants, the needs test has entrenched a single licensed outlet charging such high prices that many consumers travel to neighbouring towns to purchase packaged liquor.***

Clearly, by its own admission, the Council did in fact base its assessment of NSW liquor legislation review progress, on a sub-standard Government submission (the Discussion Paper),

and secondly,

the Council did receive, and comment on, at least one response by an interested party.

The above raises serious concerns as to the entire legislation review process and goes to the impartiality of the Council. The Council has been unwavering in its pursuit of a predetermined outcome for the regulation of the supply of liquor. ILSA believes it is incumbent on the Productivity Commission to seek answers. Good questions are as follows:

Why did the Council include in its published 2002 assessment, just one isolated piece of evidence referring to one single licensed outlet in a community of 3000 people, against the staggering weight of evidence provided by industry associations representing upwards of 4000 licensees in NSW?

How was it that the Council came by this evidence, given that it was compulsory for all submissions to be directed to the NSW Department of Gaming and Racing's Review Panel?

ILSA suggests that the Council abandoned its principles because both the Discussion Paper and the response it chose to detail in the assessment, supported the Council's unwavering disposition to get rid of the "needs test". The Council was not disposed to consider evidence and argument that defended retention of the "needs test".

6. Summary of Recommendations

- Discontinuation of imposition of large penalties.
- Changes to legislation simply to avoid penalties should not be a convenient remedy available to the States and Territories.
- It should be made the responsibility of the Council to ensure that "properly constituted review processes" are conducted.
- The Council should have the power to impose fines for non-compliance with above.
- The Council should be fully involved in the review process including thorough analysis of all public submissions.
- In the area of private enterprise and in particular retail sectors that are regulated, the Council should hold a presumption in favour of regulation, not in favour of competition.
- The review process should ensure effective consultation between States and Territories and the Council.
- Final resolution of irreconcilable differences between the States and Territories should be resolved by a formal resolution of the Council of Australian Governments.