



National Competition Policy

A Submission from CANEGROWERS

Introduction

National Competition Policy is a commitment by Australian and State and Territory Governments to reduce anti-competitive behaviour in the economy, specifically in the area of government, professional and occupational services and government business enterprises. The objective is to bring the discipline of competition to bear on activities which have previously been controlled by government.

Under National Competition Policy, proposals for legislation that are *prima facie* anti-competitive should be able to be shown to be in the public interest. The “guiding principle” for legislation review under the Competition Principles Agreement (CPA) is stated in Clause 5 of the agreement as follows;

(5)(1) The guiding principle is that legislation (including Act, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:

- (a) the benefits of the restriction to the community as a whole outweigh the cost; and*
- (b) the objectives of the legislation can only be achieved by restricting competition.*

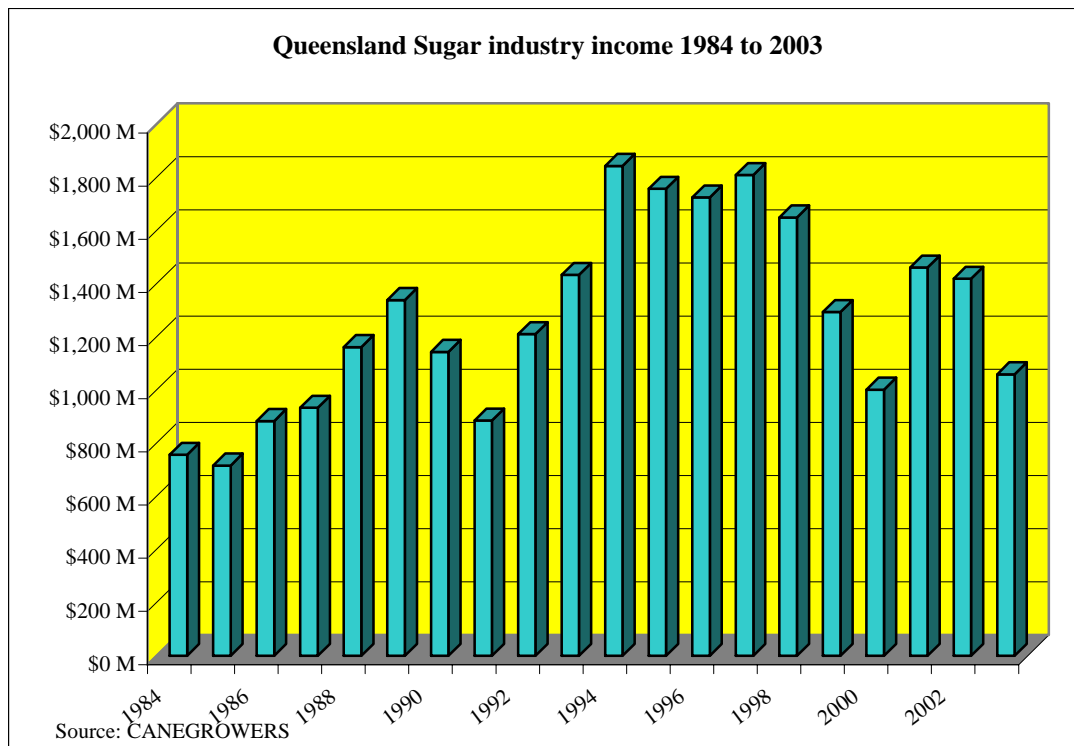
In terms of legislation, the sugar industry is subject to the Sugar Industry Act 1999 as amended. In 1995/96 the Sugar Industry Review Working Party (SIRWP) conducted a review of the current sugar industry legislation according to National Competition Policy principles. The legislation that resulted was the Sugar Industry Act 1999. It has been further amended to reduce industry regulation still further; the effect of this is that the industry is now virtually deregulated except for the marketing sector (Sugar Industry Reform Bill 2004).

This submission will deal with National Competition Policy relating to sugar industry legislation as well as issues pertaining to National Competition Policy which impinge on the activities of cane growers.

Economic significance of the sugar industry

The gross value of production of the raw sugar industry in Queensland is currently about \$1,100 M. In recent years the industry has suffered a series of poor crops and diminished returns due to intense international competition, particularly from Brazil, and a strengthening Australian dollar. The value of the crop for the last ten years is shown in Figure 1.

Figure 1



The gross value of production of the sugar industry is only a part of the value of the industry in the Queensland economy. Estimates have been carried out of the value of the industry in terms of its multiplier effect, the extra economic activity that is generated by the industry. Queensland Government Department of Primary Industries estimates that the industry adds 20,439 fte jobs to the state's economy and in addition a further 3,534 Queensland fte jobs dedicated to supplying inputs to the sugarcane growing sector. In total, the Queensland sugar industry (sugar cane growing and raw sugar manufacturing) is estimated to have contributed up to \$1,254 M in value-adding to Queensland's economy in 1996.

The industry is the dominant economic factor of production in many Queensland rural communities. For example, detailed studies of the Johnston and Cardwell Shires by Cummings Economics indicates that sugar growing and milling represents about a quarter of the earnings of the base industries in those shires in 2000-01. Similar results have been obtained in AEC Group studies of shires such as Herbert, Burdekin, Mackay, Marani, Bundaberg and Childers. Therefore, policies that impact adversely

on the industry have significant effects in areas such as this. The application of National Competition Policy has had adverse effects and therefore significantly affected these communities.

National Competition Policy in the Sugar Industry

In 1988, the sugar industry could be said to have been significantly regulated. The Queensland Government's *Regulation Of Sugar Cane Prices Act* put in place central control of expansion, land area and significant aspects of miller/grower contracts. Production above a preset level was subject to acquisition with only a nominal payment as penalty. Bulk sugar terminals up and down the Queensland coast, which the industry had paid for, were owned by local Harbour Boards, who leased them at peppercorn rentals to the Sugar Board. Marketing of all sugar was in the hands of the Sugar Board, which contracted with commercial refiners to toll refine sugar, which supplied all sugar on the domestic market and was responsible for all exports. Industry representative and research bodies were statutory and all growers were required to be members. The Federal government had in place a fixed domestic price of sugar and an embargo on imports.

Since that time, these regulations have been almost completely dismantled. In 1988, the embargo on imports of sugar was removed and replaced by a tariff, initially set at \$115 per tonne. This was progressively reduced until 1995 when the Sugar Industry Review Working Party examined it using National Competition Policy principles. As a result of this review, it was recommended that the tariff be removed and this took place in 1997. This removal has cost the industry approximately \$37 M per year since then.

Control of expansion and land area moved from being centrally controlled to a locally determined process with the passage of the Queensland government's *Sugar Industry Act 1991*. All sugar production was to be acquired, with no penalty for "overproduction". As a result of the SIRWP, further modifications to the process of granting cane production area were made in the 1999 Act. All constraints have subsequently been removed with the 2004 amendments. The effects of this on cane growers are as yet unclear.

Ownership and management of the bulk sugar terminals has been transferred to an industry owned company, Sugar Terminals Limited. A limited market in shares of this company now operates.

Under the 1999 Act and the 2004 amendments, all sugar produced in Queensland is vested in Queensland Sugar Limited, the body that has replaced Queensland Sugar Board. This is an industry-owned company, limited by guarantee, which retains the statutory acquisition of sugar. The industry peak bodies, CANEGROWERS and Australian Sugar Milling Council (ASMC), have committed to reviewing the industry marketing arrangements with the view of developing proposals for non-legislative arrangements prior to 2006, when the next review of industry legislation under National Competition Policy is required.

Representative and research bodies CANEGROWERS, BSES and local productivity boards are now voluntary bodies and have been set up and have, in general, been set up as companies limited by guarantee.

The SIRWP review examined issues relating to the vesting of all sugar in Queensland Sugar and the Single Desk for sale of sugar both on the domestic and export market. Clear benefits were shown for a single desk in the export market due to Australia's position in relation to regional markets. In relation to the domestic market, it was concluded that the maintenance of this Single Desk could be shown to pass the public benefit test as it prevented potential "leakage" of sugar from the domestic to the export market. However, in order to prevent losses to consumers in Australia through the single desk on the domestic market, it was concluded that Queensland Sugar would sell sugar on this market at the price at which the market would settle if there was strong competition, export parity price. Queensland Sugar is required to sell on the domestic market at export parity price through a directive issued by the Queensland Minister for Primary Industries under the Sugar Industry Act 1999. This Ministerial Directive, which is in place directly because of the application of National Competition Policy, costs the industry between \$4M and \$8M per year.

Effects of National Competition Policy on sugar communities

CANEGROWERS recognizes that National Competition Policy cannot be blamed for a number of the changes in service level that have occurred in regional areas in the last ten years. The closure of banks, the rationalization of privately provided service etc. are not the result of National Competition Policy. However, regional communities along the Queensland coast have suffered severely from the loss of sugar income. This is often seen as being influenced by the application of National Competition Policy. The removal of the tariff and application of the Ministerial Directive can be demonstrated to cost the industry a total of approximately \$45 M per year. Although this is not a large proportion of the industry's overall turnover of \$1,100 M, the difficult circumstances that the industry has experienced over the last few years have meant that every dollar counts. Certainly the application of this policy has had a significant effect at the margin, which may have contributed to business failures.

Impact of NCP water reforms on cane industry

In 1994, CoAG introduced a set of water reforms aimed at reforming and improving the water sector in Australia as part of National Competition Policy (NCP). These NCP reforms were meant to have substantial benefits for agricultural water users but unfortunately this has not been the case. The impact of water reforms have been substantial to cane growers and has added significantly to the cost of growing cane.

What water reforms have taken place

The key aspects of the 1994 CoAG water reforms are pricing, investment and institutional reforms as well as water property rights trading.

Pricing reform – consumption based pricing and full cost recovery (including, where practical, a return on the written down replacement cost of assets); the reduction or elimination of cross-subsidies; and making remaining subsidies transparent.

Investment reform – investment in new rural water supply schemes, or in the extension of existing schemes, to proceed only if an appraisal indicates that it is economically viable and ecologically sustainable.

Institutional reform – the adoption of an integrated water catchment approach; separating the roles of water resource management, standard setting and regulatory enforcement by 1998; and further development of interagency performance comparisons.

Water property rights and trading - implementation of comprehensive systems of water allocations or entitlements which secure allocations of water for the environment. Also, separate water property rights from land title and clearly specific these entitlements in terms of ownership, volume, reliability, transferability and if appropriate quality. Finally, allow trading in water entitlements including interstate trading where feasible.

Impact of water reform

Generally, there has been inadequate assessment of the economic and community costs and benefits of the water reforms. Also, there has not been sufficient effort at the local level to implement the reforms so as to minimise adverse impacts and encourage adoption. Consequently, the impacts of water reform on cane growers in Queensland have been significant. Many of the negative elements of NCP water reform have been implemented leading to much higher water charges but many of the positive elements have not been fully implemented yet including water trading.

Water prices much higher

New water prices were implemented in 2000 for all state run irrigation schemes that would cover the period up until 2005. This resulted in substantially higher prices in most cane growing irrigation schemes with prices rising by as much as around 70 per cent but did not deliver any genuine efficiency gains. The higher water prices have directly threatened the viability of many cane farms throughout Queensland.

The new water prices for water do not reflect efficient costs of delivering water in each scheme. Some schemes, such as the Burdekin, are paying prices that are in excess of COAG pricing policy requirements i.e. the cost of operating and maintaining the scheme. They are being forced to pay a rate of return on sunk assets which is inconsistent with what is happening elsewhere in Australia including in NSW and Victoria. In a number of irrigation schemes irrigators will not have the capacity to pay the increased charges.

Water pricing policies are currently in the process of being reviewed. Subsequently, new water prices are due to be developed in 2005 and it is unclear at this stage what the policies and prices will be. However, there is a real risk that prices will increase substantially if government implements policies such as charging a rate of return in all schemes and charging for environmental externalities.

Local Management not allowed to occur

Water customers have not been given the opportunity to locally manage their own irrigation schemes or have any effective input into management of their scheme. This is inconsistent with NCP and is a clear case of NCP not being applied to the detriment of cane growers. This has meant that water price rises have been higher than they needed to be. Local management has occurred in most irrigation schemes throughout Australia and has led to a substantial reduction in the costs of delivering water in most schemes. It would be expected that cost reductions in the order of 15% could be achievable under local management.

Increased uncertainty over water entitlements

The ten-year guaranteed access right given to growers is not adequate for investment planning given the long-term nature of farm development and has increased planning uncertainty. Also, the review of the entitlements within 10 years will reopen the debate over environmental needs and could mean a claw back of water entitlements without compensation.

The scientific investigations used to determine water requirements for the environment have not been sufficiently detailed to assess environmental water allocations. Consequently, the precautionary principle has been applied and the amount of water allocated to the environment has often been far in excess of actual requirements.

Stifled Water Resource Development

There is no commitment by government to plan and assist with further water resource development in Queensland to underpin regional development and diversification. This, along with over allocating water to the environment in many catchments has led to a stifling of regional economic development in many areas such as Bundaberg, Isis, Atherton Tablelands and Mackay due to stalling and preventing many water infrastructure developments.

Impact of NCP electricity reforms on cane industry

Similar reforms have taken place in the electricity industry to that of water as part of the NCP reforms. Just like for water, this has led to higher electricity charges as a result of pricing reforms that have included commercial rates of return being charged for all capital. These price increases have more than outweighed any price reductions that have occurred from increased competition.

Generally, only cane growers that irrigate use substantial amounts of electricity. Irrigated cane growers generally use electricity in high amounts to run their water pumps, water winches and other irrigators. In many cases, the cost of electricity is actually higher than the cost of water charges.

Consequently, irrigated cane growers have been hit hard twice by NCP from vastly higher water and electricity charges. This has had an enormous impact on the profitability of their farm. And in addition to the reduction in the sugar price, has made cane growing unprofitable for many growers.

Unfortunately, NCP hasn't lead to the competition from suppliers that we would have hoped for in rural areas and thus prices have not come down as they should have under NCP. With more competition, we would hope that prices will start to fall and growers will see some benefit from NCP.