

DEPARTMENT OF TREASURY AND FINANCE COMMENTS ON DRAFT PROPOSALS FOR A NATIONAL REFORM AGENDA

ENERGY

Governments should complete all outstanding NCP electricity and gas reforms. In addition to its current work program, the Ministerial Council on Energy should give priority to:

- resolving whether generator market power in particular regions is still excessive and if there is a need for further disaggregation of government owned generation businesses;*
- assessing whether processes for screening the competition implications of any reintegration in the electricity industry need strengthening;*
- contributing to the development by CoAG of a more effective process for achieving a national approach to greenhouse gas abatement (see below);*
- improving the efficiency of retail price and access regulation, with particular emphasis on achieving nationally consistent principles and ensuring there are appropriate incentives for investment; and*
- establishing a process for independent monitoring of the implementation and outcomes of the energy reform program and a stocktake of progress in 2009.*

Western Australia's outstanding obligations

The Department of Treasury and Finance (DTF) supports the Productivity Commission's recommendation that all outstanding NCP electricity and gas reforms be completed. Western Australia's obligations for electricity reform vary to those jurisdictions that are part of the national electricity market. Specifically, Western Australia's *Competition Principles Agreement* commitments relate to structural reform and legislation review obligations.

The Western Australian Government is currently well advanced in implementing a range of electricity reforms that flowed from a report submitted to it by its Electricity Reform Task Force in 2002.

Two key elements of these reforms are the establishment of a wholesale electricity market and an independently regulated network access code. Most of the market rules and access code are now in operation; although the wholesale market is not due to commence until mid 2006.

The key outstanding issue for Western Australia's electricity reforms relates to the disaggregation of the State owned service provider. The Electricity Corporations Bill, required to disaggregate Western Power, was introduced to the Legislative Assembly in October 2003. The Bill progressed to the Legislative Council but was subsequently withdrawn with publicised opposition making it evident that the Bill would not be passed. The disaggregation of Western Power, which is an important component in the development of a more competitive electricity market, will be a matter for consideration of Government following the upcoming State election (expected in February 2005).

A further issue on electricity reform is the introduction of full retail contestability. The Electricity Reform Task Force recommended that full retail contestability should not be introduced until a range of prerequisite reforms had been successfully implemented. One of these reforms was the disaggregation of Western Power.

Although consideration and implementation of full retail contestability is not an immediate priority, the Government continues to increase contestability in the market. From 1 January 2005, the contestability threshold is to be reduced from users consuming at least 300 MWh per annum to those consuming at least 50 MWh per annum. The National Competition Council (NCC) accepts that other key reforms need to be implemented before there are further reductions in the contestability threshold.

In relation to gas, Western Australia has already implemented key reform obligations, including full retail contestability and the provision of third party access. Outstanding matters relate to legislation reviews/amendments. These are awaiting completion of Australian Government amendments before Western Australian amendments can be progressed.

Regulations to implement the Gas Industry Ombudsman and Supplier of Last Resort remain to be completed, however, the legal and market infrastructure for full retail contestability is now in place and can be accessed by new entrants wishing to enter the gas market.

Priority areas for the Ministerial Council on Energy (MCE)

Generator market power

Generator market power is an issue that received recent attention through CoAG's Energy Market Review (Parer Review). It was identified as a significant issue in regard to the functioning of the national electricity market, in particular the structure of generation assets in New South Wales. The report also made specific mention of the structural reforms planned for Western Australia. The Parer Review stated:¹

...it considers that many of the benefits that should be derived from the [Government's package of electricity] reforms are unlikely to be achieved unless further changes are made.

The Panel is concerned about... the proposal to maintain the dominance of Western Power in the SWIS... it would be an error to create an active energy market but then establish a dominant generator. Its market power would lead to higher electricity prices unless fettered in some way, which is likely to distort the efficient operation and development of the proposed wholesale market.

To achieve a competitive outcome, Western Power's generation assets need to be disaggregated into as many separate competing units as is practical, rather than seek to address structural weaknesses through complex regulatory arrangements.

DTF supports the principle that appropriate structural reforms are the only real way to address market power issues. Developing regulatory solutions are likely to involve costly administration, attempts by the artificially constrained entity to circumvent the regulatory solutions, and less efficient outcomes.

Reintegration in the electricity industry

The DTF agrees that a priority area for the MCE should be assessing whether processes for screening the competition implications of any reintegration in the electricity industry need strengthening (given the potential for the gains from recent structural and market reforms to be otherwise diminished).

While reintegration can be a legitimate response to manage risk in a competitive market, it has the potential to increase market power, reduce the efficiency of the market and adversely impact on consumers.

¹ Parer Review, *Towards a truly national and efficient energy market*, 20 December 2002, pp 116-119.

This issue was also previously discussed in the Parer Review. It recommended that the ACCC's merger guidelines include specific criteria addressing the potential for generators to exercise market power. The Discussion Draft notes that since the Parer Review, moves towards vertical reintegration in the electricity industry have raised concerns about the adequacy of current institutional arrangements for determining appropriate levels of integration.

The form of reintegration can vary. It may include horizontal mergers between generators as discussed in the Parer review, but also vertical mergers between generators and retailers, and vertical mergers between networks and competitive elements of the supply chain (i.e. generation or retail).

The potential impact of such mergers will depend on the particular characteristics of the firms involved, and the overall market structure. An assessment of the proposed merger will also involve varying considerations depending on its nature. For example, the issues surrounding a horizontal merger between generators would be expected to be different from that involving integration between a network and retailer. The current economy-wide regulatory safeguards may not adequately address relevant issues specific to the electricity industry.

A national approach to greenhouse gas abatement

Similar to the previous issues discussed above, this is another area commented on in the Parer Review. It noted that the Federal, State and Territory governments have implemented a broad range of measures that seek to reduce greenhouse gas emissions, but that these measures are poorly targeted, uncoordinated and compete with each other.

The Western Australian Government supports a national approach to greenhouse gas abatement that results in least cost abatement measures.

The Discussion Draft notes that the development and implementation of the National Framework for Energy Efficiency (NFEF) may have a role to play in a national greenhouse program. The NFEF is being developed under the auspice of the Ministerial Council on Energy and encompasses a range of integrated measures, including wider application of energy standards, improving the capacity to identify issues among consumers. Stage one is intended to deliver a broad range of energy efficiency measures covering the performance standards of residential and commercial buildings, household and commercial appliances and improvements in the energy efficiency operations of large businesses.

The MCE will consider possible further measures under the second stage of the NFEF in the context of the Productivity Commission inquiry into energy efficiency, due for completion in mid 2005.

Moreover, in the absence of Commonwealth leadership, States and Territories are currently considering design options for a future national emissions trading scheme through the Inter-jurisdictional Emissions Trading Working Group. Any future emissions trading scheme should be national in application and robust national and international trading markets need to be developed for such schemes to be most effective.

Improving the efficiency of retail price and access regulation

In particular, the Discussion Draft raises the issue of retail price caps and the shielding of users from price signals. It notes that where prices are unduly suppressed, the long-term sustainability of supply could be compromised.

The DTF supports the theory that economically efficient outcomes are more likely when market participants are required to respond to appropriate price signals. Retail price caps have the potential to distort consumption, production and investment decisions, often because the cap implies the provision of cross subsidies. Security of supply, protection of the environment and greenhouse gas abatement can all be enhanced by appropriate price signals.

It is noted that governments often impose retail price caps and otherwise regulate retail prices for social and equity reasons (for example, similar consumers facing the same price regardless of location and hence cost to supply). However, there are far more effective and transparent ways to ensure the needy have adequate access to electricity. The provision of transparent community service obligations may be appropriate in such circumstances.

The DTF also notes that an issue for consideration in removing retail price caps is the level of competition in the market. Where the market is not contestable (e.g. full retail contestability has not been introduced), or where there is not effective competition, removal of price caps may simply encourage price increases through monopoly pricing, as opposed to price increases that are justified on a cost to serve basis. The issue of full retail contestability in Western Australia is discussed above.

Independent monitoring of implementation

The DTF agrees that independent monitoring of the implementation and outcomes of the energy reform program, and a stocktake of progress would be valuable

WATER

All governments should complete outstanding NCP water requirements and give high priority to resolving the current uncertainty about the future of the National Water Initiative by recommitting to its reforms.

In addition, the CoAG water reform process should give close attention to:

- *developing ways to achieve more effective management of environmental externalities;*
- *exploring new opportunities for cost-effective water recycling; and*
- *ensuring that monitoring arrangements post-NCP provide a discipline on all governments to progress agreed water reforms.*

National Competition Policy and National Water Initiative reforms

The ongoing implementation of reforms under the 1994 CoAG Water Reform Agreement, and the introduction of effective water trading markets, more comprehensive management plans and perpetual water rights, would provide a sound basis for the improved operation of the Western Australian water industry.

These will become increasingly important as irrigators become more accepting of water as a tradeable resource and of the benefits that can accrue from water being utilised in its highest value application.

However, the Western Australia Government did not sign the National Water Initiative (NWI) because the timelines are considered too restrictive and the focus of many of the reforms is to address problems unique to the eastern states, including over-allocated and stressed river systems.

It is understood that the Government may reconsider signing the NWI if an amendment can be made to enable Western Australia to implement appropriate reforms in accordance with its own timeframes, and not be held to adopting measures that are not applicable to Western Australia's circumstances.

For example, the NWI requires the completion of comprehensive management plans for all river systems and water bodies. However, many river systems and water bodies are relatively unaffected in Western Australia. There would be little benefit in incurring the cost of comprehensive water management plans for these systems.

In addition, the provision of sufficient Commonwealth funding to implement the initiatives would remove a disincentive to Western Australia signing the NWI.

Effective management of environmental externalities

The finding in the Commission's Discussion Draft that the scarcity value of water should be reflected in its price, through water trading arrangements, is strongly supported.

However, it is important to distinguish between resource management costs and recovering the costs of environmental externalities. Resource management costs are those generally incurred by the Government in managing the water bodies and surrounding catchments. Charging for environmental externalities is using price as a disincentive for a service provider to inappropriately use and interact with water bodies, surrounding catchments, and the environment more generally.

At Western Australia's 2002 Water Symposium, attendees supported the introduction of a cost sharing arrangement for the costs of managing the water resource. In response, the Department of the Environment investigated the introduction of a resource management charge. However, the Government decided to continue to fund resource management costs from taxpayer funds.

The management of environmental externalities has in the past been carried out through regulation (for example banning activities that are detrimental to the environment, such as treating wastewater near a river sanctuary). However, pricing can also be used to provide a disincentive to incur negative environmental externalities. The problem is that is generally more difficult to put a price on the environment, and to identify those responsible for some activities.

Nevertheless, the issue of water pricing and the appropriateness of recovering the cost of externalities through water charges is again being investigated by the Economic Regulation Authority's (ERA) urban water pricing inquiry. The terms of reference for the inquiry directed the ERA to have regard for the cost of externalities and the DTF's submission strongly supported their inclusion in the pricing regime.

The DTF remains a strong advocate of a cost recovery regime for resource management costs.

Included amongst the positive reforms of the NWI is the move to a more efficient trading market. The benefits include the efficient pricing of water that covers the costs of its management. The DTF supports the establishment of an efficient trading market for water in Western Australia, either through the NWI or by other independent means.

Water recycling

With a drying of the climate and an increasing population, the traditional surface and groundwater sources in Western Australia may soon be insufficient and other options, including water recycling, could become standard sources.

The State Water Strategy has committed Western Australia to a recycling target of 20% use of treated wastewater by 2012. The Water Corporation's Wastewater Reclamation Plant, which will produce 6GL of treated wastewater, will comprise a significant portion of this target, but there are a number of other options being considered. These include:

- use on parks and gardens;
- for irrigated agriculture;
- in industrial processes; and
- recharging aquifers.

The State Water Strategy and the Water Corporation are currently assessing each of these options using a triple bottom line analysis to determine their viability. It is also furthering research into the area of wastewater recycling through what it has termed the Shenton Sustainability Project.

The Shenton Sustainability Project is a water, wastewater reuse, recycling and research precinct. The project is designed to utilise the otherwise wasted wastewater for conversion into useful by-products.

The Project consists of three main components centred around the existing Subiaco wastewater treatment plant:

- a world class research facility and technology complex to develop new technologies and viable new products using treated wastewater and solid waste;
- demonstration activities of how these products are produced; and
- a "Sustainable Urban Lifestyles Interpretive Centre" and city farm/community garden to involve the community in understanding how the Water Corporation can treat wastewater, and develop community ownership of broader sustainability objectives.

The DTF would support further investigation of water recycling initiatives across the country. In doing so, the issue of cost recovery for recycled water is one that requires resolution, given the generally high costs involved with further treatment of the recycled water to potable standards.

Post-NCP monitoring arrangements

The National Water Commission (NWC) (to be established by the National Water Commission Bill 2004) is tasked with assessing the progress of the NWI States and Territories against their outstanding NCP reforms. It is also able to assess the progress of non-NWI jurisdictions (Western Australia and Tasmania), but only at the direction of the Prime Minister.

This provides a certain amount of conflict for Western Australia as a non-signatory of the NWI. It is unclear what jurisdiction the NWC would have over Western Australia, and it is expected that this will be the subject of on-going discussions between the Commonwealth and Western Australia.

The NWC Bill also does not provide for the NWC to make recommendations to the Commonwealth on competition payments as part of its assessments. This contrasts to the NCC, and also requires resolution.

FREIGHT TRANSPORT

Governments should complete all outstanding freight transport matters under the NCP legislation review program.

CoAG should sponsor the development of a longer-term strategy for achieving a national freight system that is neutral across transport modes.

As an immediate priority, CoAG should sponsor the development of a national reform agenda for the rail sector that integrates current work in this area and establishes clear timelines for the implementation of reform.

Western Australia has implemented the majority of freight transport reforms required under the original NCP program. The program achieved national consistency in freight vehicle operations (such as oversize/overmass regulations and exemptions, and rules governing pilots and escorts) and in the transport and handling of dangerous goods. When the Australian Capital Territory and the Australian Government implement the heavy vehicle registration reforms, which enforce timely renewals of registration, national consistency will also be achieved in this area.

Western Australia's two outstanding reforms include the national one driver-one licence requirement, and the driver licensing (uniform classes, procedures, renewals, cancellations, medical guidelines, exemptions and demerit points) reforms.

A longer-term strategy for achieving a mode-neutral national freight system, with immediate attention to the rail sector, would be welcomed by the DTF.

PASSENGER TRANSPORT

CoAG should commission an independent national review of the passenger transport sector to assess the impacts of recent reforms and determine what is now required to deliver further performance improvements in both urban and regional areas.

A national review of the passenger transport sector to provide guidelines for best-practice service delivery in urban and regional areas would be welcome. The review should be structured to recognise the low-population, long-distance characteristics of the regional passenger transport markets of Western Australia, Queensland and (to a lesser extent) the Northern Territory. Particular attention should be paid to the issue of choice between government and private sector service provision, and pricing and licensing decisions.

In the taxi market, Western Australia released 48 new taxi plates by tender for lease in the first half of 2004, equivalent to around 4 per cent of the total number of plates in Perth, and an additional 28 plates in the second half of 2004. The Government has committed to the annual release of 40 new plates in each year from 2005 to 2008, which equates to around a 3.5 per cent annual growth in the taxi fleet. New plates are being leased by tender at a price significantly below the current market lease price. Tender criteria relate to the quality of driver and service. Western Australia's release program is sufficient for it to have been assessed as meeting its CPA obligations in 2004.

COMMUNICATIONS

Unless the reviews currently in progress provide a good case to the contrary, the Australian Government should amend its broadcasting policy to remove the restrictions on the number of commercial free-to-air TV stations, multi-channelling, and datacasting.

Any future liberalisation of cross-media ownership rules should have regard to these and other pre-conditions set out in the Productivity Commission's review of broadcasting regulation.

The Australian Government should widen the scheduled 2007 review of the telecommunications-specific, anti-competitive conduct regime to include consideration of the appropriateness of the structural configuration of Telstra. Consistent with NCP requirements, if the Government proceeds with the full privatisation of Telstra prior to that date, this review should also be brought forward and its findings considered before the sale arrangements are put in place.

The Broadcasting Services Act 1992 and related Acts contain a range of restrictions on competition that reduce the scope for a diversity of views and opinions in the broadcasting services market, strengthen the market power of incumbent broadcasters in their dealings with advertisers, limit the uptake of digital technology, and reduce consumer access to major sporting events.

There would appear to be considerable community benefit in removing the restrictions on the number of commercial free-to-air television licences, allowing free-to-air broadcasters to provide more than one channel over their existing spectrum, and removing the restrictions on datacasting. Such reforms would deliver more content and more choice to consumers and would facilitate the uptake of new technologies so that they can be used to their full potential.

An independent review of Telstra's structural configuration is supported. Telstra's existing structure does not appear to facilitate competitive outcomes consistent with the public interest.

LEGISLATION REVIEWS

The Australian Government should conduct the previously scheduled review of anti-dumping at the earliest possible date. It should also review cabotage legislation either through the Legislation Review Program process or as part of a broader review of coastal shipping.

Continuing restrictions on competition in export wheat marketing and the provision of pharmacy and insurance services should be re-examined sooner rather than later. Unless addressed in other review fora, these areas should be afforded priority under a modified legislation review program (see below).

The Commonwealth Government's below average performance in reviewing and reforming legislation was noted in the Western Australian Government's earlier submission. 'Second round' reviews of wheat marketing, compulsory third party and workers' compensation insurance are supported. However, the pharmacy sector has already been subjected to extensive review.

The following reviews are also supported:

- a review of the Commonwealth's anti-dumping arrangements contained in the *Customs Tariff Act 1901 (Part XVB)* and *Customs Tariff (Anti-dumping) Act 1975*, where these arrangements restrict competition and penalise consumers and user industries; and
- a review of coastal shipping, including cabotage. By limiting access to more cost-effective foreign flagged vessels, cabotage may reduce the competitiveness of Western Australian producers who rely on coastal shipping. This may especially affect Western Australia's mineral exporters who are large users of this mode of transport.

In relation to the restrictions on competition in the *Wheat Marketing Act 1989* in June 2002 the National Competition Council (NCC) assessed that the Commonwealth Government had not met its *Competition Principles Agreement* clause 4 and 5 obligations, because the review did not show that retaining the wheat export single desk is in the public interest. Rather, the review found that allowing competition is more likely to be of net benefit to the community.

As indicated in the Western Australian Government's submission to this review, the Commonwealth's inaction is having the effect of causing some States to be very cautious about removing monopoly powers from their statutory grain marketing organisations.

The recent report by ACIL Tasman, on behalf of the NCC, found that Australia is a price taker on world markets and no evidence that grain prices had fallen as a result of deregulation of grain marketing boards. This finding provides further support for the removal of the wheat export monopoly.

A further review of the wheat marketing arrangements could also be informed by new evidence on the effects of grain marketing reforms recently implemented in Western Australia.

A re-examination of the insurance services issue would be beneficial, given the current lack of clarity over whether public monopoly or private competitive provision of compulsory third party (CTP) and workers' compensation insurance delivers greater benefits to the community. Currently Western Australia licenses multiple private companies to provide workers' compensation insurance, but legislates for the monopoly supply of CTP insurance, despite the two types of insurance being similar.

The DTF would not support a re-examination of restrictions in the pharmacy sector, as the extensive review process conducted under the current NCP agreement has concluded that removing the identified restrictions would further the public interest (rendering a re-examination unnecessary).

Notwithstanding the Prime Minister's intervention in 2004 regarding the extent of reform required in the pharmacy sector (in particular retaining restrictions on pharmacy numbers), further expenditure on reviewing the pharmacy sector would appear difficult to justify, given the extensive review processes already undertaken.

Re-review of restrictions around the Pharmaceutical Benefits Scheme, prior to the signing of the fourth Australian Community Pharmacy Agreement, should however proceed as recommended by the initial NCP review process, within the term of the current NCP arrangements.

APPLICATION OF THE TPA TO GOVERNMENT BUSINESSES

Those provisions of the TPA extending coverage to government businesses should be examined in the light of recent court decisions, to ascertain whether legislative changes are warranted to ensure that particular activities do not inadvertently escape coverage.

There would appear to be some merit in examining whether the coverage of the Trade Practices Act (TPA) should be more clearly defined. Some government procurement policies (e.g. buy local) aim to support regional and local businesses winning government work, primarily by imposing a cost penalty on non-regional or non-local suppliers and weighting the qualitative evaluation in favour of higher local content. It is unclear whether such businesses are subject to the TPA.

CONSUMER PROTECTION POLICY

The Australian Government in consultation with the States and Territories should establish a national review into consumer protection policy and administration in Australia. The review should focus particularly on: the effectiveness of existing measures in protecting consumers in the more competitive market environment; mechanisms for coordinating policy development and application across jurisdictions and for avoiding regulatory duplication; the scope for self-regulatory and co-regulatory approaches; and ways to resolve any tensions between the administrative and advocacy roles of consumer affairs bodies.

The Productivity Commission's Discussion Draft recognises that consumer protection regulation is not without costs, highlighting that:

- if it is poorly designed, it can stifle efficient market competition, investment and innovation and thereby be detrimental to the longer-term interests of consumers;
- product standards that reduce the range of market offerings may represent an unnecessary and unwarranted constraint on purchasing decisions; and
- regulatory compliance and enforcement costs can often be significant.

It may be beneficial to improve the interface between competition policy and consumer protection. In some instances legislation designed to protect consumers is ineffective, inappropriate or costly, impacting adversely on competitive markets. A national review of the effectiveness of the current consumer protection framework would seem a useful first step in reconnecting the two disciplines.

Government agencies responsible for consumer protection need to be fully informed about the benefits of competitive market outcomes. Competition delivers very important consumer benefits and needs to be taken into account when examining consumer protection frameworks.

A review would provide an opportunity to examine whether existing consumer protection policies are continuing to meet the needs of consumers as well as look at ways to resolve any tensions between the regulatory and advocacy roles of consumer affairs agencies. It would also address the issue of consumer protection agencies being captured by vested interests.

ASSISTANCE-RELATED IMPEDIMENTS TO EFFICIENT COMPETITION

The requirements in the Australia-US Free Trade Agreement for periodic review of the government procurement chapter should be used as a means to examine whether restrictions on competition resulting from government purchasing preferences continue to be in the public interest.

The recently signed State and Territory agreement aimed at preventing bidding wars should have strengthened provisions to ensure compliance and be extended to include all jurisdictions.

Government procurement policies (e.g. buy local) impose a range of requirements on the tendering and evaluation process that have conflicting objectives. Given the Commonwealth has agreed to a review of the government procurement chapter as part of the Australian United States Free Trade Agreement, and has announced a review of current procedures for Commonwealth agencies, it would be an opportune time for all jurisdictions to consider the benefits and costs of retaining preferences for local suppliers.

State and Territory governments have, in the past conducted costly 'bidding wars' based on financial incentives (e.g. tax breaks, interest-free loans, etc) aimed at attracting investment projects, which has detracted from the net national economic benefits of the projects. This has led to the States and Territories (with the exception of Queensland) signing the *Agreement between States and Territories on Investment* in September 2003.

However, there are no sanctions for breaking the agreement or any monitoring mechanism to enforce the agreement, so it remains to be seen how effective the agreement is. The DTF supports the proposed strengthening of provisions to ensure compliance, and the extension to include all jurisdictions.

THE COMPETITIVE NEUTRALITY REGIME

The competitive neutrality regime should be retained beyond the life of the current NCP.

The DTF supports the broad principles underlying the competitive neutrality regime and that the regime should continue into the future. However, perhaps the guiding principles could be refined to encourage all governments to adopt best practice, particularly in relation to complaints handling mechanisms.

THE LEGISLATION REVIEW PROCESS

Governments should complete the existing legislation review program.

A more targeted program of legislation review should then be put in place following the completion of the current NCP. The modified mechanism should:

- *be limited in its scope to areas where reform of anti-competitive legislation is likely to be of significant net benefit to the community;*
- *include provision to bring forward second-round reviews where circumstances have changed significantly, or where the external monitoring agency has assessed a previous review outcome to have been 'problematic';*
- *give greater emphasis to independent reviews; provide for adequate public consultation; and require governments to make review reports public;*
- *give explicit recognition to distributional, regional adjustment and other transitional issues in the public interest test;*
- *involve national reviews where legislation in individual jurisdictions has a significant impact on the scope to develop national markets; and*
- *give more emphasis to monitoring whether review outcomes are within the range of those 'that could reasonably have been reached'.*

For Western Australia there is still much to be gained from completing the existing legislation review and reform program. While some of the remaining reforms may be difficult to implement, the community will benefit from Western Australia completing the existing legislation review program.

The proposed modifications to the legislation review process, in particular, those initiatives aimed at targeting significant anti-competitive legislation, enhancing the independence and transparency of the review process, and strengthening the external monitoring regime, are strongly supported.

In addition, encapsulating the essence of the November 2000 CoAG directive on transitional issues in the guiding principles underpinning the reform program would be beneficial. A common criticism of NCP is that too little attention has been given to adjustment costs and, in particular, the cumulative impacts of individual reforms on communities. Making explicit the consideration of the need for transitional arrangements to support those who may be adversely affected by changes, which are in the overall public interest, may lessen this criticism.

The Discussion Draft notes that the NCP reversed the traditional onus of proof in policy reform, whereby it has generally been up to the proponents of change to demonstrate that change will be worthwhile. In the case of competition policy reforms, governments endorsed the approach proposed by Hilmer and reversed the onus of proof on the grounds that theory and evidence strongly suggest that removing restrictions on competition will typically be in the public interest.

While not making an explicit proposal to revert to the traditional burden of proof the Discussion Draft says:

“In public policy, it is often hard to ‘prove’ anything. Consequently, it is desirable to put the onus of proof on those favouring the more ‘problematic’ a priori outcome. For regulatory restrictions on competition in product or factor markets, where there is minimal social and environmental policy content, the onus of proof in NCP seems appropriate. However, where regulation has important social policy or environmental objectives the traditional onus of proof may be preferable.” (p. 124)

Having two different approaches each dependent on the significance of social or environmental objectives may lead to confusion for agencies carrying out reviews as to which approach is the most appropriate for their particular review. It is also unclear how using the traditional onus of proof in legislation reviews where a wide range of factors are impacted upon (by removing a restriction on competition), will necessarily lead to better outcomes. This could perhaps be more clearly explained in the Final Report.

GATE-KEEPING ARRANGEMENTS FOR NEW AND AMENDED REGULATION

To guard against the unwinding of previous reforms and to help ensure that new regulatory initiatives are in the public interest, all Australian governments should ensure that they have in place effective and independent arrangements for monitoring new and amended legislation.

Consideration should also be given to widening the range of regulations encompassed by gate-keeping arrangements and strengthening national monitoring of the gate-keeping arrangements in place in each jurisdiction and the outcomes delivered.

An effective and independent gate-keeping process is a necessary condition for guarding against the introduction of legislation that is not in the public interest. As the Discussion Draft correctly points out:

“...backsliding would send an unfortunate signal about the commitment of governments to resisting pressure from sectional interest groups.” (p. 157)

It is essential that gate-keeping processes be improved since governments across Australia are already under pressure from vested interest groups to reintroduce restrictions on competition. This is particularly the case in Western Australia in relation to statutory marketing of agricultural products.

Irrespective of whether NCP payments continue, the *Competition Principles Agreement* clause 5(5) commitment is ongoing. It is the primary safeguard against:

- ‘backsliding’ on reforms already introduced; and
- the introduction of new legislation with restrictions on competition that are not in the public interest.

Perhaps jurisdictions that do not have sufficiently robust gate-keeping mechanism in place should work towards establishing independent bodies with relevant expertise to advise agencies on when and how to conduct regulatory impact assessments. Such bodies should be empowered to examine regulatory impact assessments and advise on the adequacy and/or quality of the analysis in a transparent manner.

OVERSIGHT OF REGULATED INFRASTRUCTURE PROVIDERS

Governments and regulatory agencies should continue to explore opportunities to improve the efficacy of price setting and access arrangements for regulated infrastructure providers. Particular emphasis should be given to improving incentives for providers to undertake investment to maintain existing facilities and expand networks, including through the implementation of clear and nationally consistent principles to guide regulators. Specific approaches outlined in recent Productivity Commission reports into the National Access Regime and the Gas Access Code provide a basis for improvements in this area.

Section 9.5 of the Discussion Draft discusses the oversight of monopoly service providers, noting that concerns have been raised regarding current regulatory practices. It is not surprising that regulated service providers would raise concerns with regulatory practices given their vested interests. Nonetheless, it is worth considering whether the regulatory requirements are achieving their intended aims, and more generally whether the objectives are appropriate. These considerations have been taking place, and the Productivity Commission itself has been involved in two important reviews recently covering the national access regime (contained in the Trade Practices Act) and the national gas access regime.

One of the key issues that the Productivity Commission has raised in these previous reviews and also in its draft report on NCP arrangements is the impact regulatory arrangements may be having on infrastructure investment. It developed in its reviews of the national access regime and national gas access regime an overall objects clause for each regime which would guide the regulatory process. Importantly, the proposals noted that efficient investment in infrastructure is an integral part of the regulatory process and regulators' decisions.

The Western Australian Government has given support to the Commonwealth's proposed amendments to the national access regime on this issue. The Productivity Commission recommendations on the national gas access regime are currently being considered through the MCE process. The DTF inputs to this process through the Western Australian Office of Energy. It is noted that the Productivity Commission's recommendation on the objects clause for the national gas access regime is consistent with that for the national access regime. The DTF supports this recommendation.

More specifically than the objects clause, the Productivity Commission has proposed a number of mechanisms to reduce uncertainty and increase prospective returns for infrastructure investors. These proposals include binding 'no coverage' rulings for 15 years where the proposed infrastructure (e.g. pipeline) does not meet the coverage criteria, and light handed regulation through price monitoring.

The DTF considers, and it is widely accepted, that the guiding principle in the application of regulation should be that the benefits of regulation outweigh the costs involved. The mechanisms proposed by the Productivity Commission are consistent with this principle – regulation (and a particular form of regulation) is only applied where the benefits outweigh the costs.

The measures proposed are therefore generally supported. However, it is noted that such matters are now being considered in detail by jurisdictions through the MCE process. The DTF will continue to input to these processes.

Another area of regulation that has recently been discussed is the methodology for setting allowed tariffs for a monopoly service provider. Traditionally regulators have usually applied a cost of service approach. However, measures that focus on productivity improvements and benchmarking techniques have been raised as alternate methodologies.

The DTF notes that the potential application of these alternate methodologies is currently being explored. However, where a service provider has substantial monopoly power (i.e. the infrastructure meets the coverage criteria and is subject to a tariff setting regime) it is difficult to envisage the setting of prices being totally decoupled from a cost assessment, especially over the longer term.

HEALTH CARE

CoAG should initiate an independent public review of Australia's health care system as a whole. This should be the first step in the development of an integrated reform program to address structural problems of long standing that are preventing the health care system from performing to its potential. The review should include consideration of the determinants of future demand for and supply of health services; health financing issues (including Federal/State responsibilities and their implications); coordination of care (including with aged care); the interaction between private and public services; and information management. It could also incorporate the proposed CoAG review of medical workforce issues.

The Final Report of the Health Reform Committee (HRC), 'A Healthy Future for Western Australians', was released in March 2004, with 85 of the Committee's 86 recommendations being subsequently endorsed by the Western Australian Government.

The HRC Report provides a “blueprint” for State health system reform and improvement over the next 13 years. Recommendations for reform are wide-ranging and cover the entire continuum of care from primary care through to aged care. Specific reforms relate to clinical practices, hospital role delineation, infrastructure, workforce, efficiency, governance, performance management and resource allocation. Implementation of the reforms is currently being progressed by a Health Reform Implementation Taskforce.

Recommendation 71 of the Report states:

“The Department of Health should work to improve joint Australian/State Government planning and service provision, integrated models of care and pooled funding. The newly established Bilateral Working Group should be used as a vehicle to achieve this.”

The HRC Report identified a range of issues and limitations with regards to Commonwealth/State arrangements at this time:

- difficulties in coordination of care between different treatment levels;
- duplication of services and gaps in service delivery;
- potential for cost shifting;
- multiple funding and accountability for some service provider organisations;
- lack of long term comprehensive planning; and
- inefficiencies in the planning, educating, training, registering and employing of the health workforce.

To elaborate on the last point, the training and accreditation of health professionals is currently significantly influenced by the professional bodies. There should be an evidence-based evaluation of whether or not this influence unduly limits the available numbers. Although it is imperative that the professions are consulted in relation to the content, quality and standard of training, the decision on numbers and factors related to this decision, should be managed by independent agencies, conceivably on a national basis.

Having recognised the fragmentation and inherent inefficiencies apparent within the current Commonwealth-State arrangements for health service delivery, the DTF welcomes and supports the Productivity Commission’s recommendation for an independent review of Australia’s health care system, managed under the auspices of CoAG.

It is recommended that any such review recognises some specific issues that are relevant to Western Australia, including:

- a shortage of certain specialists, GPs and nurses;

- relatively low bulk billing rates;
- large indigenous population and lack of access to GP services by indigenous persons;
- lack of remote and regional access to health services;
- lack of after-hours access to health services;
- greater promotion of medical research and development;
- capacity shortages in the aged care sector; and
- improving the benefits of the 30% health insurance rebate in an environment of low use of private health insurance in public hospitals, as compared to other jurisdictions.

It is also recommended that any nationally coordinated review account for the State health system reform program that is already underway. The HRC reform program is considered to be crucial for promoting the long-term financial sustainability of the State system. Future improvements to Commonwealth-State arrangements should seek to build upon the efficiency and effectiveness of outcomes currently being pursued.

NATURAL RESOURCE MANAGEMENT

CoAG should immediately take a greater role in addressing fragmentation and uncertainty in relation to greenhouse gas abatement policies. It should also initiate a review to identify other areas of natural resource management – beyond its current and foreshadowed responsibilities – where the pay-offs from nationally coordinated reform are likely to be high.

The issue of greenhouse gas abatement was discussed above under issues relevant to the energy industry. The DTF agrees with the recommendation that a review be undertaken to identify other areas where a nationally coordinated approach would be highly beneficial.

It is also noted that a range of submissions suggested that a broad institutional and policy framework akin to NCP would be appropriate for what are national issues, and similarly that such a framework would provide a suitable mechanism to progress the reforms.

Clearly the proposed review, as well as considering the areas of natural resource management that should be given priority, could also consider the specific framework through CoAG to implement the reforms.

THE GENERAL FRAMEWORK FOR FUTURE NATIONALLY COORDINATED REFORM

The institutional framework(s) used to progress future nationally coordinated reforms should be underpinned by:

- *clearly enunciated objectives and reform principles;*
- *effective preparatory work detailing the benefits of reform in particular sectors and the specific changes required within jurisdictions to reap those benefits;*
- *some flexibility for jurisdictions to determine how to implement reforms, but with sufficient specification of desired outcomes to allow for effective monitoring of reform progress;*
- *transparent and independent assessment processes, incorporating a comprehensive public interest test and providing scope for consultation with, and input from, interested parties;*
- *a timetable for the implementation of the review and reform program including, as appropriate, interim targets and provision to refine targets as new information emerges, or if circumstances change;*
- *independent monitoring and public reporting on progress made in implementing the program; and*
- *robust mechanisms to lock-in the gains of past reforms and prevent backsliding.*

These principles provide a very useful starting point from which CoAG can begin discussions on the most appropriate set of institutional arrangements to give effect to the agreed future reform agenda. Reform should focus on those areas likely to bring substantial benefits to the Australian community.

The institutional arrangements for any new reform agenda should be characterised by the 'three pillars' as outlined by the NCC in its submission on the Discussion Draft:

- an agreed agenda based on a set of principles that provides a degree of flexibility in application, but at the same time sufficient detail to ensure the desired outcome is delivered;
- an independent agency to monitor progress and assess the extent to which jurisdictions have met their commitments; and
- financial incentives for jurisdictions to implement reforms in recognition of the 'fiscal dividend' of such reform and the divergences in this dividend across different levels of government.

It may be useful for the Productivity Commission's Final Report to more fully describe some alternative approaches, identifying their particular advantages and disadvantages in a transparent manner. This work could prove valuable when CoAG reviews the NCP arrangements by September 2005.

At this stage, it would appear that the multi-faceted approach referred to in the Discussion Draft could be a fruitful approach. A series of CoAG sponsored sector-specific nationally coordinated reform programs sitting alongside a formal successor to the NCP involved with the competition framework and regulatory architecture issues would appear to have some merit. However, it would be imperative to ensure that independent monitoring and public reporting on progress is consistent across sector-specific reform programs.

It is also essential that the Commonwealth and other State and Territory Governments work in a cooperative manner in forming the agenda for further reforms to enhance Australia's productivity. Without a significant degree of cooperation between the jurisdictions it is unlikely that reforms will be implemented in a manner necessary to reap the potential returns available from a nationally coordinated reform framework.

In relation to competition payments the Discussion Draft appears to send some mixed messages:

"In the Commission's view, competition payments have clearly played a pivotal role in maintaining reform momentum within the States and Territories. However, it has also become apparent, particularly during the periodic debates about whether withholding of some payments ('penalties') is justified, that the payments issue can become a distraction. In particular, it can mislead the community as to the main rationale for reform – namely to achieve improvements in productivity, household incomes and overall living standards, rather than simply to increase government revenue." (pp. 140-141)

"That said, within a federation, circumstances can arise where the distribution of benefits and costs of reforms across jurisdictions are such that, in the absence of interjurisdictional transfers, worthwhile change may be placed at risk. Hence, to judge whether it is appropriate to offer incentives requires an analysis of the specific reforms involved, including the extent to which reforms undertaken by one jurisdiction are likely to provide benefit for others." (p. 141)

"Drawing on experience to date, it is apparent that providing financial incentives for jurisdictions to proceed with agreed reforms can be very useful in a multi-jurisdictional context, although their rationale and value clearly depend on the nature of the proposed reforms." (p. 144)

"However, it (i.e. the Productivity Commission) observes that while the competition payments regime has clearly helped in progressing the NCP agenda, it would be unfortunate if an undue focus on the precise distribution of the future reform dividend among jurisdictions were to put at risk progress on policy changes that would be in the national interest." (p. 297)

"...some recent instances of governments publicly implying that they have only undertaken reforms to avoid the imposition of financial penalties have been unhelpful in maintaining support for reform within the community." (p. 300)

The Productivity Commission could provide greater clarity in the Final Report of the efficacy of financial incentives for jurisdictions to proceed with agreed reforms. It is not clear from the Discussion Draft where the Productivity Commission actually stands on this issue.

Public interest is a necessary condition for reform, but it is not always a sufficient condition when vested interests apply political pressure to governments. Sometimes additional incentive is required to get governments 'over the line' irrespective of whether reforms undertaken by one jurisdiction are likely to provide benefits for others. If the Productivity Commission does not envisage that a future reform program will include competition payments it should provide CoAG with options for alternative mechanisms to prevent backsliding and to provide an impetus to continue reforms.

ADJUSTMENT SUPPORT

The framework(s) used to progress future nationally coordinated reforms should make explicit reference to the need for up-front assessment of distributional and adjustment issues and the case for adjustment support. They should also include criteria relating to circumstances in which adjustment support is likely to be warranted, and the characteristics it should embody to facilitate rather than frustrate adjustment and avoid duplication with generally applicable income support.

As stated above, given distributional and adjustment concerns will continue to be an issue with any future reform agenda there would appear to be some value in embedding the need to consider distributional and adjustment issues in the guiding principles underpinning the future reform program.

Currently the reform framework provides no guidance on the circumstances in which governments should provide additional support to aid adjustment or address adverse distributional consequences from the reform process. Developing robust criteria for adjustment would also reduce the risk of the inappropriate provision of adjustment support, poorly configured support, and failing to consider such support when it is justifiable.

COMMUNICATION AND CONSULTATION

Governments should take a lead role in explaining to the community why further reform is required and what benefits it will bring. They should also ensure that there is effective consultation and engagement with those parties directly affected by reforms.

Without question, governments do have a role in elevating the community interest above sectional interests, publicly supporting reform processes and explaining the reform and the public interest reasons why it is necessary.

However, as the Discussion Draft says:

“Consumer advocacy groups could also play a greater role in communicating the benefits of reform for the end consumer.” (p. 300)

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.

Effective consultation processes in reform processes are also critical. If done well, they can contribute to the reform process in a number of ways by:

- bringing the expertise, perspectives and ideas for alternative actions of those directly affected;
- helping policymakers to balance opposing interests;
- identifying unintended effects and practical problems with the reform proposal;
- providing a quality check on the policymaker’s assessment of costs and benefits;
- identifying interactions between regulations from various agencies within government; and
- enhancing voluntary compliance, reducing the reliance on enforcement and sanctions.

The Western Australian Government has issued best practice guidelines for consultation, *Consulting Citizens: A Resource Guide* (Department of Premier and Cabinet, 2002).

OTHER KEY REFORM AREAS

Australia’s future reform needs range more widely than the above program, which focuses on areas identified by the Commission as being particular priorities for oversight by CoAG or another national leadership body.

Other important areas for policy attention include:

- *improving the quality and responsiveness of education and training systems at primary, secondary and post-secondary levels;*
- *following through on identified measures to enhance the performance of aged care services;*
- *extending the scope for workplace flexibility within industrial relations frameworks and addressing constraints on labour supply;*
- *removing general inefficiencies and perverse work-incentive effects in the taxation system, including by improving its interface with social support programs;*
- *promoting the efficient development of our cities and regions, allowing for their diverse circumstances; and ensuring that there are cost-effective mechanisms in place to address market failures in technological innovation, including appropriate intellectual property protection.*

Reforms in these areas offer the prospect of significant gains for the community and, in most cases, would be complementary to the above agenda. However, the Commission's judgement is that any additional benefits from using a nationally coordinated approach are unlikely to be sufficient to make this the preferred way forward at this time, especially given the other demands on the resources of a high-level body like CoAG. Nonetheless, the Commission welcomes feedback on these judgements, as well as on other matters in this draft document for public discussion.

The following areas identified as offering the prospect of net community benefits from reform are supported:

- improving the quality and responsiveness of education and training systems and enhancing the performance of aged care services delivery;
- removing inefficiencies in the work-incentive effects from taxation and social support programs;
- promoting the efficient development of cities and regions through appropriate urban planning and regional development policies; and
- cost-effective mechanisms to address market failures in technological progress.