INDUSTRY COMMISSION

Exports of Government Services

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TERMS OF REFERENCE

The Industry Commission is requested to undertake a study into the export of government services, covering Commonwealth, State and Territory governments. The study would assess existing activity by government departments, agencies and business enterprises and the potential to develop government services as a commercially viable export industry.

In undertaking the study, the Commission should specifically report on:

- the emerging trends in global markets for the export of government services, particularly in the Asia-Pacific region;
- the international marketing environment including impediments to trade, and the effectiveness of government efforts to improve market access;
- the structure and competitiveness of the Commonwealth Government in terms of its own ability to develop government services as an export industry and in terms of its coordination of export activities with State and Territory governments;
- the scope for government to more actively engage in export activities, having regard to the nature of their systems which must be based within the policy framework of professionalism and accountability, and while continuing their core domestic activities;
- the scope for government to work in partnership with the private sector in pursuing export activities; and
- any measures which could be undertaken to facilitate the export of government services, implementation strategies for any suggested measures and the effects on government, industry, consumers and the economy in general of any suggested measures.

The Commission's report is to be submitted by end 1997 or earlier if possible. The report is to be published.

PETER COSTELLO
3 July 1997

OVERVIEW

Governments provide a range of services to the Australian community to meet various economic and social objectives. These include ensuring the availability of services that would not be supplied on a commercial basis and promoting equitable access to key services such as health and education.

However, the nature and scope of government service provision is changing. In recent years, governments have shifted responsibility for delivering some services to the private sector. At the same time, increasing numbers of government providers have sought to complement their domestic activities with exporting.

Australian governments produce many services which are in demand overseas. Service exports by government agencies are currently worth around $2 billion a year, or some 2 per cent of total Australian exports.

The value and range of exports is diverse. Some government business enterprises (GBEs), notably Telstra, are major exporters. The provision of education to foreign students is also an important export earner. At the other end of the spectrum, the exports of many budget sector agencies are counted in thousands rather than millions of dollars. These exports span the full range of public sector activity and include public administration, social security and resource management.

Government exports of services, 1995-96 ($ million)

Sector	*Value*
Transport and communications	870
Education	850
Defence	100
Health services provided to overseas visitors	20
Other public sector agencies	270
Total	**2 110**

More detailed data for much of this activity are lacking. Nevertheless, some general observations can be made:

- Most government service exports involve the provision of technical advice and training or the application of technologies and systems.

- They mainly go to the Asia-Pacific region.
- Many are made through Australia's bilateral aid program, or through multilateral development agencies. Indeed, the export activity of many budget sector agencies is heavily reliant on aid funding.

Many government service exports involve more than one agency, and often the private sector. There are a number of well established private project managers operating in the market. There are also two public sector managers — the Overseas Projects Corporation of Victoria (OPCV) and SAGRIC International in South Australia.

The financial profitability of government service exports is highly variable. GBEs and many of the education institutions face strong commercial pressures to ensure that their exports are profitable. In contrast, it is doubtful if exports by many budget sector agencies fully cover costs, let alone make a profit. In some cases, this may be appropriate given the wider benefits that can accompany these exports (see below). However, in others, it reflects poor commercial judgement or accounting systems that do not properly identify the costs entailed in exporting.

The policy framework

Agencies involved in the export of services pointed to a range of benefits for Australia. Apart from revenue generation, the discipline of competing in export markets, and the experience gained, can help to improve the quality of services provided to Australian residents. Government service exports can often lead to flow-on opportunities for Australian suppliers of equipment, software and the like. And, in areas such as defence and public administration, they can also help to promote foreign policy objectives.

But there are also potential costs. Government agencies are not subject to the full range of market disciplines facing private firms and many public sector managers have little commercial experience. This increases the risk of unsuccessful export ventures, the costs of which are borne by taxpayers. Participants in this study pointed to a number of unsuccessful attempts to enter export markets. There is also the risk that exporting could be at the expense of services provided to Australian residents.

Moreover, there may be other ways to achieve some of the benefits that arise from government service export activity. For example, the revenue generation and flow-on opportunities for other suppliers would also arise were agencies to make their expertise available to the private sector to export on their behalf. This already happens to a considerable extent. Similarly, exporting is only one of a number of options open to agencies to improve the quality and effectiveness of their domestic service delivery.

Given these considerations, agencies need to be clear about their reasons for becoming involved in exporting, and to establish that exporting is the best way of achieving those objectives. This is particularly the case given that the main role for government service providers must continue to be to meet the needs of Australian residents.

Nevertheless, the Commission considers that there can be good reasons for some agencies to export their services directly. Shifting responsibility for managing all exports of government services to the private sector could result in the loss of some profitable export opportunities. For example, close government involvement in an export project can be a valuable marketing tool, not least in the Asia-Pacific region. Further, the more direct its involvement in exporting, the easier it is likely to be for an agency to translate the lessons learned to its core domestic activities.

There is a need, however, for safeguards to ensure that only those exports of benefit to the community proceed. Specifically governments must ensure that:

- Exporting enhances, or at least does not reduce, the level and standard of services provided to Australian residents.
- Processes are in place to ensure that risk is managed, commercial practices are followed and public sector intellectual property is protected and rewarded.
- Competitive neutrality principles apply so that government agencies compete with the private sector on an equal footing.
- There are effective accountability and public reporting requirements.

The mechanisms required to give effect to these principles will depend on the type of agency involved in exporting.

For corporatised agencies, legislative requirements and board direction should provide a strong commercial focus and accountability for performance. Corporatised agencies are also subject to the competitive neutrality principles in the National Competition Policy.

For non-corporatised agencies, approaches vary around Australia. Commonwealth agencies and their Ministers take full responsibility for exporting, subject only to general guidelines on aspects like risk management. In some states, agencies retain responsibility for exporting, but must comply with specific export guidelines. Other states seek to centralise export risk and expertise through the activities of public project managers.

All of these approaches give broad effect to the general principles outlined above. However, in the Commission's view, there is a case for strengthening the arrangements for non-corporatised agencies in some jurisdictions.

Export guidelines

Commonwealth, state and territory governments should each publish guidelines for exporting by their non-corporatised agencies. These guidelines should make clear a government's general attitude to exporting and the rules that should apply to any such activity.

Apart from clarifying agencies' scope to engage in exporting, such guidelines should help to ensure that the outcomes are transparent and that agencies are held responsible for those outcomes. They should also help to ensure that agencies comply with competitive neutrality requirements. Specifically, the guidelines should address the relationship between export and domestic activities, pricing, private sector involvement, risk management, capital investments, intellectual property, and reporting requirements.

The New South Wales, Queensland and Western Australian Governments already have such guidelines in place. And, in South Australia, a review panel assesses export projects against broadly similar criteria.

Coordination and facilitation

By providing a consistent framework, export guidelines help to 'coordinate' export activity across agencies.

A number of states also have arrangements to provide generic information to agencies on such matters as bid preparation and marketing. Access to such information can reduce the risks for agencies new to exporting. It also avoids the need for each agency to invest resources to 'reinvent the export wheel'. The Commission sees considerable merit in this approach.

Victoria and South Australia (and recently the Northern Territory) have extended the coordination role to include the management of export projects. For a number of years, OPCV in Victoria and SAGRIC in South Australia have handled many of their state's exports of government services.

OPCV and SAGRIC appear to have operated effectively in a highly competitive market. More generally, they have played a valuable role in developing government service exports in Australia.

Nonetheless, the case for other jurisdictions to replicate the OPCV or SAGRIC models is not compelling. The marketing of government services is now much better developed than when these organisations were established. Over the years, private project managers and some agencies have acquired considerable marketing experience in this field. Thus, it is not clear that new public sector managers would add much value in an already competitive market. Centralising responsibility can also mean that, for individual agencies, the direct link between exporting and their domestic activities is weakened.

National coordination

In some sectors there can be benefits from national coordination of export activity. In particular, it can help to mobilise the best public sector resources from around the country and prevent confusion overseas about what Australia as a whole has to offer.

Agencies in certain sectors, notably education and health, have already taken steps to coordinate some export activity at the national level. More generally, both the private and public project managers operating in this area have commercial incentives to adopt a national perspective if it can enhance their bids.

Accordingly, while national coordination has been helpful in certain sectors, the Commission sees no need for any formal national coordination mechanism. Indeed, such a mechanism would only have an appreciable impact if it were compulsory for agencies to work through it. But compulsion would result in loss of flexibility at the agency level and could preclude beneficial competition between jurisdictions.

Competitive neutrality

Competitive neutrality considerations arise whenever governments are involved in commercial activities. It is not in Australia’s interests for government agencies to take business from private firms by virtue of artificial advantages associated with public ownership.

There have been longstanding competitive neutrality claims in this area. Private sector interests contend, for example, that:

- some government agencies do not pay all of the costs incurred by private competitors, such as tax (or tax equivalents), and are not required to earn a commercial rate of return on assets; and
- some are cross-subsidising their exports (by, for example, recouping most of their overheads from funding for non-commercial domestic services).

Evidence to substantiate such claims is lacking.

However, it would be surprising if they were totally without foundation, at least as far as budget sector agencies are concerned. For example, as noted earlier, some of these agencies are not in a position to cost their exports properly because of deficiencies in their accounting systems.

That said, over the last couple of years, there has been much greater emphasis on commercial practice and competitive neutrality within the government services sector. For example, as state-owned enterprises, the OPCV and SAGRIC are subject to strong commercial disciplines. Governments are also improving their accounting systems, notably through the introduction of accrual accounting.

To reinforce these developments, governments should ensure that their export guidelines spell out pricing principles which meet efficiency and competitive neutrality requirements. In this regard, the guidelines should provide agencies with the same sort of pricing flexibility open to their private sector competitors. Thus, for example, rate of return requirements should apply to agencies' export activity as a whole, rather than to individual projects. Guidelines should also recognise that where spin-off benefits for agencies from export activity are demonstrably significant, full cost recovery may be unnecessary on efficiency grounds, even in the longer term.

Future prospects

In broad terms, the outlook for Australia's government service exporters is promising. The market will continue to grow as developing countries seek to improve their services and strengthen their public institutions. Many Australian agencies have the basic skills and experience to cater for this demand.

Of course, Australia will not be handed business on a platter. Agencies must have the right skills and operating practices to take advantage of export opportunities. While often obvious in hindsight, there are many traps for agencies that enter exporting unprepared. Agencies new to exporting can therefore learn much from the experiences of those who have gone before (see box).

And, while there will be significant opportunities available through the various aid programs, agencies will do well to look beyond those programs if they wish to expand their export activity. At the same time, the need for agencies to give priority to providing services to Australian residents will tend to limit the resources available for exporting.

Doing it right: what agencies in the export market had to say

Preparing the agency

Agencies should:

- be clear about the objectives of, and commitments entailed in, entering the export market;
- have a quality service which can be tailored to the needs of the target market;
- seek advice on the key factors influencing export competitiveness for their services; and
- be cost competitive.

Understanding the market

Agencies should:

- become familiar with the market and the competitive environment, including the nature of any regulatory and other barriers to entry; and
- visit the target market to gain an understanding of its particular requirements.

Operating successfully in the market

Agencies should:

- be prepared to invest resources in effective marketing;
- become familiar with the requirements of operating through aid agencies;
- consider employing a local agent to assist during all stages of the project cycle (from identification to implementation), and to facilitate access to key decision makers in government and aid agencies; and
- evaluate projects after completion to identify any inefficiencies in the process and possible future opportunities.

RECOMMENDATIONS

Chapter 3: Government agencies as exporters

Recommendation 3.1

Government agencies should only export their services where this enhances, or at least does not reduce, the level and standard of services provided to Australian residents.

In applying this principle, governments should provide their agencies with some scope to balance longer-term gains for domestic customers against any short-term costs.

Chapter 4: Export guidelines

Recommendation 4.1

Those jurisdictions which do not have explicit export guidelines for non-corporatised agencies should introduce them.

Export guidelines should include a statement of government policy on exporting by agencies. They should also address the relationship between export and domestic activities, pricing, private sector involvement, risk management, capital investments, the use of intellectual property, and accountability and public reporting.

Recommendation 4.2

Export guidelines should emphasise the need for rigorous risk assessment and management, and effective accountability mechanisms.

With such requirements in place, government agencies should have some capacity to undertake export projects which involve more than minimal risk.

Recommendation 4.3

Governments should not place a blanket ban on capital investments by non-corporatised agencies in offshore activities. Rather, export guidelines should make provision for case-by-case assessment of any such proposals. Responsibility for approving capital investments should reside with Treasurers.

Recommendation 4.4

Governments should include specific provisions in export guidelines covering the use of their intellectual property.

Recommendation 4.5

Budget sector agencies should report separately on the performance of any significant commercial export activity. Apart from information on revenues, costs, profits and rates of return, such reports should indicate the basis for cost allocation between commercial export and other activities.

Chapter 5: Collaboration and competition with private firms

Recommendation 5.1

If governments wish to provide general support to the private sector to develop export markets, they should do so independently of commercial export ventures by their agencies and fund the activity separately.

Recommendation 5.2

To provide for a return on their intellectual property, government agencies should generally charge for staff participating in private projects, rather than grant those staff leave without pay.

Recommendation 5.3

Export guidelines for non-corporatised agencies should spell out pricing principles that meet efficiency and competitive neutrality requirements. In particular, they should:

- spell out all components to be included in an agency's cost base, including all taxes (or equivalent payments), charges and other costs normally faced by a private supplier, and the policy for allocating costs to the commercial activity; and
- provide agencies with similar pricing flexibility open to private sector competitors, subject to their meeting an appropriate longer-term rate of return target.

Other matters

The Commission also draws attention to its comments on:

- future prospects for exports of government services (section 2.3);
- OPCV's access to Victorian public sector resources (section 5.2)
- coordination of export activities in individual jurisdictions (section 6.2); and
- Australia-wide export coordination (section 6.3).

1 WHAT IS THE STUDY ABOUT?

Australian governments are increasingly looking to export their services. Apart from earning revenue, exporting can lead to the provision of better quality services to Australians. It can also help to make better use of the skills available in the public sector. And it may have wider benefits — for example, increasing Australia's involvement in the Asia-Pacific region.

But there are potential costs. Government agencies are not subject to the full range of market disciplines that apply to private firms, increasing the risk of unsuccessful export ventures. There is also the risk that exporting could be at the expense of services provided to Australian residents.

1.1 The reference

Against this background, the Treasurer asked the Commission to undertake a study:

- to provide information on export activity by government bodies; and
- to examine the potential to develop government services as a commercially viable export industry.

The study covers exports of services (as distinct from goods) by government business enterprises (GBEs) and budget-funded agencies and departments at both the Commonwealth and state and territory level.

In undertaking the study, the Commission was directed to report on a number of matters including:

- emerging market trends, particularly in the Asia-Pacific region;
- impediments to trade in these services, and the effectiveness of government initiatives to improve market access;
- the competitiveness of the government sector in export markets;
- the scope for government to more actively engage in exporting and to work with the private sector when doing so; and
- measures to facilitate the export of government services.

The full terms of reference are on page viii.

1.2 The Commission's approach

Definition of a government service

The first purpose of the study is to provide better information on current government service exports and future growth prospects. This raises a number of definitional issues:

- At the margin, there is some blurring between services and goods. For example, the provision of water, power and telecommunications services often involves the supply of equipment as well as technical advice and know-how. In this report, the Commission has focused on the 'non-hardware' components of such exports.
- Some services are traded directly, while others are embodied in other traded goods and services. Thus, for example, power and telecommunications services provided by government are important inputs to many of Australia's exports. In this study, however, the Commission has only considered directly traded service exports made by government agencies.
- Many government service exports involve Australian agencies providing services in other countries. But in areas like education and health, foreigners come to Australia to receive services. This study covers both types of export.
- The role of government agencies is changing all the time. Increasingly, governments are shifting the delivery of some services (as opposed to ensuring their provision) to the private sector. Consequently, the concept of a 'government' service is in a state of flux. The point of reference for this study has been exports by service delivery agencies that are *currently* in public ownership.

The second purpose of the study is to examine the prospects for 'commercially viable' exports of government services. In this context, 'commercially viable' would generally mean exports capable of generating a profit. However, as discussed later, non-monetary benefits may be as, or in some cases more, important than the potential financial gains from exporting. For example, the discipline of competing in export markets and the experience gained can help improve the quality of services provided to Australian residents. Hence, in the study, the Commission has looked more broadly at policies to encourage export activity of benefit to the community as a whole.

An emphasis on generic issues

The Commission has not looked closely at policy issues specific to particular sectors such as telecommunications, education and health. This is not to downplay the significance of such issues. Indeed, as the Commission's previous reports on exports of education and health indicate (IC 1991a, b), sector-specific factors may have a major effect. But these factors are also likely to vary substantially between services, making them difficult to assess comprehensively in a study of this sort. Hence, this study concentrates on generic policy issues relevant to a broad sweep of government service exports.

Some of these generic issues go to the heart of the role of government in providing services. For example, should services provided to Australian residents and others be viewed as equivalent, or should exports always be subordinate to local provision? The terms of reference also raise 'competitive neutrality' issues in relation to competition between government service agencies and private firms. The study seeks to shed light on these issues.

Finally, in focusing on generic policy issues, the Commission recognises that there are significant differences between corporatised GBEs and other agencies. The report draws out these differences as far as future policies towards exporting are concerned, although its focus is very much on non-corporatised agencies.

1.3 Information sources

In preparing its report, the Commission drew on information from a range of sources. Early on, it released an issues paper and sought written submissions on the matters raised. The Commission received 36 submissions, representing the views of more than 60 individuals and organisations.

The Commission valued the assistance it received from discussions with a cross section of Commonwealth, state and territory agencies, as well as from some of the private firms which both compete with those agencies and work with them in export markets. In the (more limited) second round discussions, some participants had the opportunity to comment on the Commission's proposed findings and recommendations. Appendix A lists those participants with whom the Commission held discussions and those who made written submissions.

1.4 Structure of the report

The next chapter provides industry and market information on government service exports. It first looks at the current situation, providing information on exports by Australian government agencies at both an aggregate and sectoral level, the significance of the aid market to those exports, and collaboration between the public and private sectors in export ventures. It then considers future prospects, including the impact of barriers to trade in government services.

The second part of the report looks at the policy framework necessary to support the efficient and effective export of government services:

- Chapter 3 examines the role of government as an exporter and the broad caveats that should attach to export activity.
- Chapter 4 discusses the rules required to promote efficient export activity. In doing so, it distinguishes between general policy guidelines for exports by non-corporatised agencies, and agency-specific arrangements for corporatised bodies.
- Chapter 5 explores issues relating to interaction between the public and private sectors in this area. These include requirements to encourage efficient and effective collaboration in export ventures and competitive neutrality issues when the two sectors compete for export business.
- Chapter 6 examines the need for, and the nature of, mechanisms to 'coordinate' export activity across agencies and jurisdictions.

The final chapter looks at what agencies have found they can do to make the most of the export opportunities available to them. It reports the experiences of agencies, and documents successful strategies as well as the potential traps for those new to exporting.

2 TRADE IN GOVERNMENT SERVICES

Information on exporting activity by Australia's government agencies is far from comprehensive. Exports of services by these agencies are not separately identified in much of the trade data published by the Australian Bureau of Statistics (ABS). While previous reports looking at government service exports have provided estimates for some states, these are not presented on a consistent basis. Moreover, there is no published aggregate data for government exports in a number of jurisdictions, including the Commonwealth.

However, by pooling published information with unpublished ABS data and information in submissions, the Commission has been able to provide a reasonable picture of overall service exports by Australian government agencies.

What emerges is a diverse range of often small scale exporting activity, interspersed with a few substantial export activities. In value terms, the education and transport and communication sectors account for the major share of total exports.

2.1 Current export activity

The value of exports

The Commission estimates that Australia's government service exports are worth a little over $2 billion a year. This represents around 9 per cent of total Australian service exports and 2 per cent of all exports (see table 2.1).

Notwithstanding the qualifications to the data set out in box 2.1, these figures indicate that government service exports make a significant contribution to Australia's overall export performance. By way of comparison, at about $2.2 billion, exports of motor vehicles and components are of a similar magnitude.

Table 2.1: Government exports of services, 1995-96 ($ million)

Sector	*Value*
Transport and communications [a]	870
Education[b]	850
Defence[c]	100
Health services provided to overseas visitors [d]	20
Other public sector agencies [e]	270
Total	**2 110**

a Includes both telecommunications and postal services.
b Includes fee income ($800 million) paid to public sector schools, higher education institutions and ELICOS colleges by overseas students in Australia on student visas, and education services ($50 million) delivered in other countries by Australian education agencies.
c Includes training and Defence Cooperation Program activities such as engineering, surveying, maritime and communication projects.
d The ABS estimates that the value of private and public health services provided to foreign patients in Australia is about $60 million a year. After making allowances for revenues to private hospitals and doctors, the Commission estimates that about $20 million of this income accrued to government health providers.
e Includes exports by budget sector agencies and GBEs outside the transport and communications sector as well as AusAID running costs.
Source: ABS special request and Commission estimates.

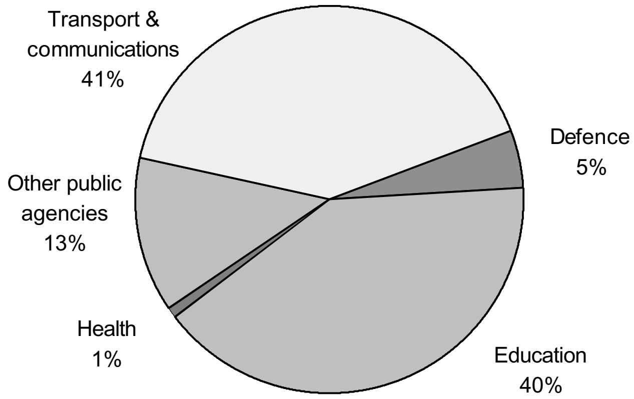
Types of exports

Transport and communication services and education together account for more than 80 per cent of Australia's government service exports. While many budget sector agencies are involved in exporting, most of their export activity is relatively insignificant in value terms. Thus, the 'other public sector agencies' group, comprising mainly budget sector agencies other than health and education providers and the Department of Defence, accounts for only around 13 per cent of total exports (see figure 2.1).

Transport and communications

Telstra is the major exporter of government services in the transport and communications sector. Other exporters include Australia Post, Queensland Rail Consulting Services and the Australian National Line.

Figure 2.1: Exports of government services by sect or (percentage)



Source: ABS special request.

Box 2.1: ABS data on exports of government services

ABS data used to prepare table 2.1 are subject to a number of qualifications.

Some of the export data at the Commonwealth level are sourced from either Department of Finance and Administration ledgers or other official advice by Commonwealth departments. If a department records export revenue in ‘other receipts codes’, the ABS cannot distinguish these exports from other receipts. However, the Bureau advised the Commission that any resulting understatement in the data is likely to be insignificant.

A second, and more important, qualification concerns export projects that involve both the public and private sectors. In such cases, the ABS has attributed the full value of the export contract to the ‘prime contractor’. This has particular implications for the data for the other public sector and transport and communication groups. It means, for example, that where a private firm subcontracts work on an export project to a government agency, the ABS export data would still attribute the full value of the contract to the private firm. Conversely, if a government agency is the prime contractor and a private company the subcontractor, the full value of the contract would be recorded as a government export. As discussed later in the report, other than OPCV and SAGRIC, the government is not usually the prime contractor in these types of joint ventures. This suggests that the export data in table 2.1 are likely to understate actual exports.

A final qualification to the data is that, although the ABS business register includes about 7000 public agencies, the services export data include only 80 of these agencies. Evidence presented to this study indicates that there are more than 80 government service agencies involved in exporting. Again, however, the ABS suggested that the omissions are unlikely to be significant in overall value terms.

Telstra is well established in the Asia-Pacific region, supplying a range of communication services and related products to governments and corporations. These include international frame relay and lease lines, global internet access, international toll-free and facsimile services, conference services and digital mobile phone services.

Destinations for Telstra's exports include Cambodia, India, Indonesia, Laos, Sri Lanka and Vietnam. In Vietnam, Telstra has invested $US 170 million to expand and upgrade its international network. And in Indonesia, it is involved in a joint venture to expand Java's fixed telephone network (Telstra 1997).

Australia Post has exported technical advice through consultancy missions to postal enterprises in Indonesia, Kenya, Poland, Solomon Islands and Thailand. For example, it advised the Communications Authority of Thailand on the installation of automated machinery and operational planning for a new mail centre. It is currently marketing the Riposte postal system in the Asia-Pacific region.

In the transport sector, Australian National Line is a significant exporter, while Queensland Rail Consulting Services (in partnership with other Australian consultants) has completed railway projects in over 30 countries, including China, India, Indonesia, Malaysia, Thailand and Vietnam.

Education

Over 90 per cent of education export revenue comes from fees paid by overseas students studying in Australia. Within the public sector, most overseas students are enrolled in higher education or vocational education institutions. Within the higher education sector, nearly half of overseas students are enrolled in business administration and economics. Box 2.2 provides further information on overseas students in Australia.

About 85 per cent of Australia's overseas students come from the Asia-Pacific region. The Republic of Korea is the largest single source of foreign students. Other significant sources include Indonesia, Malaysia, Japan, Singapore and Hong Kong (see table 2.2).

Box 2.2: Overseas students in Australia, facts and figures

Revenue

- In 1996, overseas students paid $1.3 billion in fees to public and private education providers. In addition, they spent over $1.7 billion on other goods and services.
- About 60 per cent of education export revenue is generated by public sector institutions. This equates to about $800 million in fee income.

Student numbers

- In 1996, about 143 000 overseas students were enrolled in Australia. They studied mainly in New South Wales (37 per cent), Victoria (25 per cent), Queensland (17 per cent) and Western Australia (13 per cent).

Sectoral breakdown

There are four distinct market segments: higher education, vocational education, schools and ELICOS.

- The higher education sector has traditionally been the major export earner. In 1996, it accounted for 47 per cent of fee income.
- The biggest growth in exports in recent years has been in the vocational education and ELICOS sectors. Vocational education now accounts for about 23 per cent and ELICOS 21 per cent of fee income.
- The school sector is a relatively minor exporter of education, accounting for about 9 per cent of fee income.

Source: DEETYA (1997).

Education exports also include correspondence courses, the electronic transmission of lectures and courses overseas, and the provision of consultancy services in other countries. For example:

- Curtin University has used video conference links to provide services to students in Singapore.
- The South Australian Government exports an offshore matriculation course to students in Malaysia.
- OPCV exports a range of school, technical and vocational, tertiary and distance education services. In 1996, for instance, it was involved in an Asian Development Bank project to upgrade Cambodia's school system.
- Various TAFEs export consultancy services on a fee-for-service basis. For example, TAFE Queensland is involved in consultancies in China, Indonesia, Malaysia and Papua New Guinea.

Table 2.2: Overseas students [a] studying in Australia, by country, 1993 and 1996

	1993	*1996*
Republic of Korea	6 800	20 300
Indonesia	8 500	16 700
Malaysia	10 100	13 700
Japan	8 100	13 500
Singapore	6 000	11 600
Hong Kong	11 300	11 200
Taiwan	5 000	9 700
Thailand	3 900	8 100
India	1 000	4 000
China	7 300	3 500
Other	16 800	30 900
Total	**84 700**	**143 100**

a Includes students attending both public and private institutions.
Source: DEETYA (1997).

Defence

A major component of defence exports is training. For example, the Australian Defence Force has been providing advice and training on the detection and clearance of mines to the Royal Cambodian Armed Forces.

Other Department of Defence exports include engineering, surveying, maritime and communication projects under the Defence Cooperation Program. The Department also provides some education services to foreign students in its academies and colleges.

Defence exports are usually made for strategic rather than for commercial reasons. As such, most are budget funded. However, the Department of Defence does charge some of its overseas students. In 1996-97, it recovered around $5 million, or about 15 per cent of total costs in this area, through user charges.

Health services provided to visitors to Australia

Some visitors travel to Australia on medical visas specifically to obtain medical treatment. In 1995-96, about 4300 people entered Australia on medical visas, primarily from Oceania and South East Asia (Department of Immigration and Multicultural Affairs 1997).

However, most visitors with a medical visa are treated as private patients in private hospitals. Thus, most services provided to visitors in public facilities are to students, tourists and business people who require 'unexpected' medical treatment during their stay.

Other public sector agencies

The range of export activity by other budget sector agencies (and GBEs outside transport and communications) is diverse, although usually small scale. Services exported include consulting and technical advice, information technology systems, and training.

Consultancy advice

In addition to the consultancy exports already noted, Australian agencies export advice in areas as diverse as social policy development, urban planning, infrastructure development, environmental management and health policy planning. For example:

- The Great Barrier Reef Marine Park Authority provides advice on establishing, planning, managing and maintaining coastal and marine areas.
- Aus Health International (AHI) — a New South Wales GBE — advises governments and health agencies on health service capacity building, health planning and development, and hospital and health services management. AHI has exported consultancy services to China, Indonesia, Malaysia, Papua New Guinea, the Philippines and Western Samoa.
- The Australian Geological Survey Organisation is a research organisation within the Commonwealth Department of Primary Industries and Energy. It provides specialist geoscientific advice and expertise for technical and institutional strengthening programs.
- Vic Roads, in collaboration with the OPCV and the private sector, exports a range of consultancy services in the areas of road management, traffic systems, registration and licensing. Markets for these exports include Ireland, Malaysia and Singapore.
- Powerlink Queensland exports consultancy advice on high voltage transmission systems, including plant condition monitoring, testing, maintenance, refurbishment and repair. It has exported to Fiji, Hong Kong, New Zealand, Papua New Guinea and Thailand.

Information technology systems

A number of budget sector agencies export information technology based systems. For example:

- The Department of Social Security (DSS) helps foreign governments and institutions install, reform or review social protection systems. The DSS's exportable services include the design and development of information technology platforms, tender preparation and evaluation, fraud control and management information systems. It exports primarily to the Asia-Pacific region.
- The Health Insurance Commission (HIC) has developed a model to analyse and develop health financing policies. The model operates on a personal computer platform, and can be tailored to meet an individual country's needs. The HIC has exported the system to Romania and Turkey.
- The Victorian Environmental Protection Agency, in partnership with the CSIRO, won a contract in Hong Kong to develop the software for state-of-the-art air quality modelling and monitoring.

Training

Many budget sector agencies export training programs. For example:

- The Insurance and Superannuation Commission has provided training to overseas insurance regulators in China, Fiji, Malaysia, Papua New Guinea, Vietnam and Western Samoa.
- The Australian Customs Service conducts an annual training program for senior customs officers from overseas administrations under the Customs International Executive Management Program. It has also provided 'in-country' training, most recently in Vietnam.
- WorkSafe Western Australia has provided occupational health and safety training in Indonesia, Malaysia, Papua New Guinea, the Philippines and Thailand.
- In 1996, the Victorian Police Force conducted an executive development training program for police officers from 13 countries including Belgium, Malaysia, Singapore, South Africa, the United Arab Emirates and the United States.
- The Queensland Office of Racing exports vocational education and training services to Japan, Korea and Malaysia.

Collaboration between the public and private sectors

A common feature of trade in government services is collaboration between the public and private sectors. This can take a number of forms.

Some projects involve a consortium comprising one or more government agencies as well as the private sector. In many instances, a private project manager, such as ACIL or SMEC, will manage the project. However, for some projects, the public sector project managers — the OPCV and SAGRIC — will be the prime contractor. Individual agencies may also coordinate joint ventures. For example, the Australian Nuclear Science and Technology Organisation seeks private partners for its research and development activities.

In other instances, collaboration will simply involve the provision of inputs on a fee-for-service basis. Anderson Consulting, for example, contracted the Department of Social Security to advise on administrative systems in Thailand.

At yet another level, collaboration can involve private sector provision of advice on the marketing of government services. SMEC, for example, performs this function for some government agencies in Western Australia. Chapter 5 considers collaboration and the attendant policy issues in detail.

The financial profitability of exports

Other than for the OPCV, the Commission received no explicit profitability data for Australian government service exports. In 1996-97, the OPCV reported a rate of return on assets of 6.6 per cent and a return on shareholders' equity (after tax and profit distribution to individual Victorian agencies) of 7 per cent (OPCV 1997).

However, it is clear that profitability varies considerably across agencies.

The bulk of Australia's education exports are most probably profitable. A number of education agencies told the Commission that the revenues earned from foreign students have helped to supplement government funding. Indeed, a Curtin University paper reported that:

> Australia's higher education system has become financially dependent on fee paying international students ... Any loss of such income would result in a dramatic shedding of both academic and non-academic staff and the reduction of numerous services (Mazzarol and Hosie 1997).

Similarly, dividend requirements applying to GBEs place significant commercial pressures on these agencies to ensure that any export activity is profitable.

But in some other cases, exporting is clearly not profitable in a narrow financial sense. As already noted, the Department of Defence exports for strategic rather than commercial reasons with minimal cost recovery. More generally, many budget sector agencies see exporting as providing significant spin-off benefits for core service provision (see chapter 3). In view of these benefits, some only seek to cover costs.

The situation is further clouded by inadequacies in accounting systems within the budget sector. The Commission understands that some budget sector agencies would find it difficult to measure the costs of export activity accurately, let alone determine whether it is profitable.

2.2 The role of aid programs

A significant proportion of Australia's government service exports is made through bilateral or multilateral aid programs.

Bilateral aid

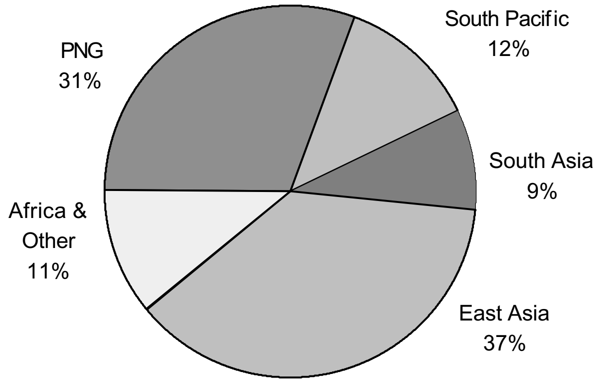
In 1996-97, the Australian Government spent around $1450 million on official development assistance. Of this, $1040 million was for bilateral aid. The remainder was for multilateral aid and other official development assistance (AusAID 1997a).

AusAID administers the bilateral aid program, although the private sector and other government agencies deliver most projects.

Bilateral aid services usually involve the provision of technical advice and training or infrastructure and systems. Bilateral aid projects are only open to bidders from Australia or New Zealand.

Areas currently targeted under the bilateral aid program include health, education, transport and communications, sustainable resource management and trade policy. In Papua New Guinea, for example, Australia is helping to strengthen health service institutions and develop programs to improve teaching skills and school infrastructure. It is also assisting with the drafting of new legislation for the country's prisons. Around 90 per cent of Australia's bilateral aid funding goes to countries in the Asia-Pacific region (see figure 2.2).

Figure 2.2: Destination of Australian aid, 1996-97



Source: AusAID (1997a).

The bilateral aid program provides significant opportunities to government service exporters. Indeed, AusAID projects often provide agencies with an entry point to export markets. Accordingly, the export activities of many agencies, including OPCV and SAGRIC, are heavily dependent on the bilateral aid program.

In 1996-97, contracts held by Australian government agencies were valued at around $320 million, or 29 per cent of the total value of AusAID's outstanding contract commitments. SAGRIC and OPCV were AusAID's largest public contractors. Other major government contractors were ANUTECH, the Hawthorn Institute of Education and Telstra (see table 2.3).

Multilateral aid

Multilateral development agencies administer a system of commercial and concessional loans and grants for developing countries (see box 2.3).

The World Bank is the largest provider of multilateral development assistance, approving loans totalling close to $US 20 billion a year. The bank has been the major export client for a number of Australian agencies including OPCV, the Department of Social Security, the Department of Employment, Education, Training and Youth Affairs and the Health Insurance Commission.

Various other United Nations agencies also provide significant development assistance. However, with notable exceptions like the Great Barrier Reef Marine Park Authority and the Australian Customs Service, it appears that relatively few Australian government agencies have accessed United Nations funding for export projects. Indeed, United Nations procurement from

Australian suppliers of services, both public and private, only totalled around $20 million in 1996 (see box 2.3).

At the regional level, Australia is a member of the Asian Development Bank (ADB) and the European Bank for Reconstruction and Development (EBRD). The ADB has been a significant client for Australian government services. OPCV, the Health Insurance Commission, Queensland Rail Consulting Services, the Insurance and Superannuation Commission and the Queensland Department of Education are among the large number of agencies that have won ADB projects.

Table 2.3: Public sector agencies with AusAID contracts, 1996-97 [a] ($ million)

Agency	*Value*
SAGRIC	104
OPCV	64
ANUTECH	51
Hawthorn Institute of Education	14
Telstra	14
Australian Broadcasting Corporation	10
Griffith University	7
Flinders University	6
Department of Agriculture, NSW	6
Australian Geological Survey Organisation	6
ACTEW Corporation	6
CSIRO	5
Other public	28
Total public sector contractors	**321**

a These data do not accurately reflect public sector exports through Australia's bilateral aid program in any particular year. First, AusAID contracts often span more than one year. Hence, the data in this table reflect new contracts let in 1996-97 as well as ongoing contracts let in previous years. Second, many exports by private contractors include significant public sector input.

Source: Commission estimates based on AusAID (1997b).

In contrast, few Australian agencies have so far been involved in EBRD projects. This is primarily because of Australia's distance from the Bank's target markets in Central and Eastern Europe and intense competition from European agencies and firms.

Box 2.3: Background on selected multilateral aid agencies

World Bank

The World Bank is the largest development lender, approving new loans worth about $US 19 billion in 1996-97. The World Bank comprises two agencies: the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA).

The majority of IBRD and IDA funding goes to the agricultural and transportation sectors. Other targeted sectors include energy, the social sector, finance and education. In 1996-97, a quarter of IBRD and IDA funds were directed to Europe and Central Asia. Other major recipients were countries in Latin America, the Caribbean, East Asia and the Pacific.

United Nations (UN)

In 1996, UN procurement on goods and services totalled about $US 1590 million and $US 1060 million, respectively.

Within the UN system, many organisations are involved in purchasing services, including the United Nations Purchase and Transportation Division, the United Nations Office for Project Services and the United Nations Industrial Development Organisation.

In 1996, the major country suppliers of services through the UN included the United States, the United Kingdom and Italy. Australia only supplied $US 5 million of goods and $US 20 million of services.

Asian Development Bank (ADB)

In 1996, the ADB approved about $US 5.8 billion in new development assistance. Of this, $US 5.5 billion was loans, around $US 100 million equity investments and $US 175 million technical assistance grants.

The leading borrowers and recipients of technical assistance grants are China, Indonesia, India and Pakistan. By sector, 1996 loan approvals were highest in energy, agriculture and natural resources, transport and communications, and social infrastructure.

Sources: ADB (1996), World Bank (1997) and information supplied by the Department of Foreign Affairs and Trade.

2.3 Future prospects

Perceptions on future prospects for Australian government service exports vary considerably. Some see vast opportunities driven by economic growth in the Asia-Pacific region and access to a large pool of multilateral aid funds. Others, however, are more circumspect. They argue that a relatively small part of the spending on service-related activities will be on technical and consultancy services of the sort supplied by Australian government agencies. They also point to constraints on Australia increasing its share of multilateral aid funds, the existence of foreign trade barriers, and domestic impediments to exporting.

Future demand growth

The recent expansion in Australia's government service exports has been underpinned by rapid growth in a number of developing countries, particularly in the Asia-Pacific region.

Recent economic events in a number of the Asian economies point to a slowdown in regional growth rates in the short to medium term.

Nevertheless, a widely held view is that longer term growth prospects in the region remain strong, implying a positive outlook for government service exports. While much of the extra spending will be on construction and equipment to provide services such as power, water and sewerage, most participants expected solid growth in demand for consultancy and technical services. Indeed, a number pointed out that the provision of infrastructure generates demand for related services.

Many participants suggested that Australia is well placed to capture a share of this demand growth. The Western Australian Department of Commerce and Trade, for example, stated:

> Significantly, Australia is well placed to satisfy the rapid growth in demand for services from the Asia Pacific Region which may be one of the key drivers of future Australian economic growth (sub. 13, p. 4).

More specifically, participants argued that:

- Australia's proximity to the Asia-Pacific region will provide agencies with an edge over European and North American competitors. For example, compatible time zones and short travelling distances to some Asian markets are expected to aid in the development of export linkages.
- Similarities in climate mean that the Australian and Asia-Pacific markets share some similar needs. For example, Queensland Rail Consulting Services said that its expertise in operating a modern narrow gauge railway system in subtropical and arid environments is unusual and is sought by South East Asian countries facing similar climatic conditions.
- The recent economic events in Asia will see spending on services focused more on institutional strengthening programs. This is an area in which Australia has considerable expertise and an established reputation (see box 2.4).

Further, while acknowledging that the Asia-Pacific region is likely to remain the focus for most Australian government service exporters, a number of participants said that there are likely to be emerging opportunities in other regions. For instance, the Great Barrier Reef Marine Park Authority said that there is market potential in the Middle East, while the Department of Social Security cited South Africa and Latin America as prospective markets.

The aid market

While the basic demand drivers auger well for Australian government service exports, the reliance of many agencies on the aid market may constrain future growth.

As noted above, Australia's bilateral aid program is only open to suppliers from Australia and New Zealand, providing them with a captive market. In broad terms, this suggests that unless total funding increases, the program is unlikely to be a significant source of demand growth for exports of Australian government services. However, a few participants suggested that, in the future, the program is likely to focus increasingly on social services, providing some additional opportunities for government agencies.

Similar considerations are also relevant to the future opportunities available through multilateral aid funding.

Some participants argued that given the size of the multilateral aid pool — around $30 billion a year from the UN and multilateral development banks — even a small increase in Australia's share would translate into a significant increase in exports.

However, as many participants pointed out, most of this spending is on construction and equipment rather than services as such (although there is usually a service component to infrastructure contracts). For example, of the $US 5.8 billion in development assistance approved by the ADB in 1996, only about $US 500 million was in the form of technical assistance.

Moreover, the existence of a significant pool and successfully accessing the pool are two different things.

Box 2.4: Prospects for some individual sectors

Education

There is significant potential for growth in Australia's exports of both onshore and offshore education services. The Australian International Education Foundation forecasts that export earnings from education (including spending by foreign students on goods and services) will increase from around $3 billion in 1997 to $5 billion by 2001.

Within the public sector, the higher education and school sectors are expected to attract 100 000 overseas students a year by 2001, earning about $1.2 billion in fee revenue — a 50 per cent increase on the current level. The emergence of new information technology systems will also create opportunities for an expansion in services delivered offshore. The higher education sector alone is expected to provide $60 million of education services in other countries by 2001 (DEETYA 1997). At present, total offshore education exports by government agencies total $50 million a year.

Infrastructure

Many Australian government agencies will have the opportunity to benefit from continued demand growth for infrastructure services in developing countries. For example, Telstra said that it is well placed to capture a share of the growth in China's telecommunications services. China is installing 15 million new telecommunication lines a year — equivalent to about half of Australia's total network. Similarly, Queensland Rail Consulting Services expects significant increases in demand for railway consulting services in Asia.

Public administration

Development across the Asia-Pacific region, and the move towards market economies in Eastern Europe and Central Asia, has created demand for a diverse range of public administration services.

Australia has established a strong reputation in a number of public administration areas including social security, health insurance and land titling. This has the potential to provide Australia with a competitive advantage, not only over developing countries, but also over developed countries with less proficient systems.

Participants suggested that most agencies will find it difficult to tap aid funds provided for projects outside the Asia-Pacific region. The Australian Geological Survey Organisation, for example, said:

> ... difficulties include Australia's isolation making marketing and market research (information gathering) expensive for some parts of the world (sub. 21, p. 5).

Some participants also argued that, based on past experience, Australia may have difficulty in securing its 'fair' share of multilateral aid funding in the Asia-Pacific region. For example, Queensland Rail Consulting Services argued that Australia's share of ADB contracts is low relative to its contributions to the Bank. (In 1996, Australia contributed about 6 per cent of the Bank's subscribed capital and nearly 5 per cent of ADB commitments, but won only 1 per cent of total contracts in value terms.) Participants attributed this outcome partly to the 'politics of aid'.

However, as far as contracts for consulting and technical services are concerned, Australia has been quite successful. In 1996, Australia won 10 per cent of ADB consultancy contracts and 11 per cent of contracts for technical assistance — almost double its share of contributions to the Bank (ADB 1996).

Similarly, Australia has provided 1.6 per cent of the IBRD's subscribed capital and 1.7 per cent of IDA subscriptions and contributions committed. In 1996-97, Australia's share of World Bank payments to supplying countries for foreign procurement was 1.4 per cent for total disbursements and 2.7 per cent for consultants (World Bank 1997).

These figures suggest that Australia's public and private sector entities are highly competitive in the area of consulting and technical assistance. In general terms, this augers well for future growth prospects.

But whether Australia can significantly increase its already high shares of multilateral aid funding for these services is more problematic. Any future shifts in the share of aid spending directed to services may provide additional market opportunities for government service exporters. That said, significant growth in exports will almost certainly depend on agencies operating successfully outside the aid market.

Overseas impediments

Future growth in Australian government service exports will also depend partly on the success of initiatives to reduce barriers to trade in services. These include investment restrictions, local content rules, restrictions on the temporary entry of foreigners and nationality requirements for staff.

Collectively, these barriers are significant. Hoekman (1995), in a paper which assesses the General Agreement on Trade in Services, ascribes tariff equivalents of between 20 and 200 per cent on services trade between member countries. Estimated tariff equivalents for the education, health and sewerage sectors were 50 per cent, and for telecommunications between 100 and 200 per cent.

Several participants commented on trade barriers of particular relevance to government service exporters. For example, the Queensland Government raised concerns about:

- local labour requirements such as work permits;
- mandatory joint venture requirements with local participants;
- taxation issues; and
- industry specific regulations such as requirements to join local professional associations.

The South Australian Department of the Premier and Cabinet noted similar problems and identified other impediments including currency restrictions, import restrictions and poor patent protection for intellectual property in some Asian countries. Other barriers noted by participants included visa requirements (particularly in relation to education and health exports) and the lack of transparency in the selection of contractors by foreign governments.

In contrast, the Victorian Government said that its agency case studies revealed:

> ... no particular international barriers to exports of Government services, other than those applying generally to exports such as delayed payments, especially in lesser developed countries, and problems associated with dealing with multiple layers of bureaucracy and intermediaries rather than directly with the client (sub. 30, p. 4).

Addressing trade barriers

Within the World Trade Organisation (WTO) and the Asia-Pacific Economic Cooperation forum there are initiatives in place to address barriers to services trade (see box 2.5).

However, reform of services trade is likely to be a long process. The major accomplishments under the General Agreement on Trade in Services have been to lock in liberalisation which was occurring anyway and to provide a framework for negotiating further liberalisation. The WTO Agreement on Government Procurement, to which Australia is not a signatory, liberalises trade in government procurement for goods and some services, though its implications for exports of government services are small. More generally, proposals for multilateral and regional reform focus on particular sectors. With notable exceptions such as telecommunications, most of the services that Australian governments export do not feature on priority reform lists. This is not surprising given the low value of most government service exports.

Box 2.5: Initiatives to reduce impediments to services trade

The General Agreement on Trade in Services (GATS)

The GATS, which operates within the WTO, provides a rules-based framework for international trade in services and for future liberalisation. It is similar to the framework for trade in goods under the General Agreement on Tariffs and Trade (GATT).

However, the GATS framework is weaker than the GATT, with 'scheduled' sectoral commitments making up the core of the agreement. All countries excluded some major service sectors from their core commitments. For example, Australia did not schedule coastal shipping. Moreover, many of the liberalisation commitments have not been significant. (A detailed discussion on the GATS, and its weaknesses, is contained in IC 1996a.)

The Agreement on Government Procurement (AGP)

The AGP is a WTO agreement which provides for bilaterally-negotiated liberalisation of government procurement for goods and specified services. However, Australia is not a signatory to this agreement.

It is unlikely that Australia's exports of government services would be expanded significantly by Australia signing the AGP. But signing could ensure Australian government agencies are not discriminated against in tendering (IC 1996b).

Asia-Pacific Economic Cooperation (APEC) forum

The APEC free trade initiative, announced in 1994, calls for open trade and investment for goods and services in the Asia-Pacific region by 2010 for industrialised members and by 2020 for other countries. While not formally binding on members, the initiative was a formal statement of intent by all APEC leaders to pursue regional trade liberalisation. In the services area, APEC working groups are dealing with sectors such as telecommunications, transportation and tourism.

For these non-priority exports, the most effective role that Australian governments can play will be to help agencies work around overseas impediments.

Examples of initiatives already in place include:

- the establishment of government offices overseas;
- bilateral agreements with partners in the Asia-Pacific region;
- trade missions; and
- government-run marketing seminars.

Conclusion

The market for government services is large and growing, particularly in the Asia-Pacific region. Australian government agencies are well positioned to benefit from this growth. In particular, many have the skills and experience required by developing countries.

However, it is important not to overstate these prospects.

Apart from the expected slow down in growth in a number of Asian economies, it is problematic whether agencies can increase their already high shares of aid funding. Thus, growth in government service exports will almost certainly require agencies to operate successfully outside the aid market. Further, the need for agencies to give priority to providing services to Australian residents will continue to limit the resources available for exporting.

Nonetheless, for some agencies and sectors the export outlook is promising. Making the most of these opportunities will require action to improve the policy framework underpinning government export activity (see chapters 5 and 6) and continuing improvements in practices at the agency level (see chapter 7).

3 GOVERNMENT AGENCIES AS EXPORTERS

Governments provide a range of services in Australia to meet various economic and social objectives. Important among these are ensuring the availability of services that would not be supplied on a commercial basis and promoting equitable access to services.

However, the role of government as a service provider is changing. Through contracting out or privatisation, governments are shifting some service delivery or provision into the private sector. At the same time, some public agencies are looking to complement their core functions with activities such as exporting. As set out in the previous chapter, Australian governments produce many services which are in demand overseas.

Many see exporting by government service providers as a natural and valuable extension of their domestic functions. Others, however, see it as potentially involving significant costs and going beyond the role of government. This chapter looks at these benefits and costs with a view to assessing whether exporting is a legitimate role for government service agencies.

3.1 The benefits of exporting — participants' views

Government service agencies have become involved in exporting for a range of reasons. In some cases, it has been a deliberate strategy to take advantage of commercial opportunities. In others, it has reflected a desire to benchmark performance against foreign agencies or to promote links of benefit to the exporting agency and Australia. This variety of motivations is reflected in agencies' views on the benefits of their export activity.

Some of the benefits are directly observable and potentially quantifiable. However, as is apparent from the following discussion, others are much more subjective and therefore difficult to quantify.

Improving the return on investments in public sector capital

Agencies saw exporting as improving returns on investments in the public sector in a number of ways.

Many pointed to its role in generating revenue. Revenue considerations are not limited to government businesses. They are also relevant to budget sector agencies required to generate part of their funding needs. Thus, for example, the

Bureau of Resource Sciences noted that the requirement for it to earn 30 per cent of its income from external sources had influenced its decision to export.

However, a significant number of agencies said that exporting also enhances the quality of their resources. In particular, they argued that it provides development opportunities for staff and encourages a more dynamic culture within an agency. For example, the Department of Social Security stated that exporting:

> ... provides professional growth opportunities for DSS staff through exposure to atypical issues and in so doing adds to the skills base of the Department and the broader public service (sub. 18, p. 13).

Improving domestic service provision

A generally applied principle is that exporting by government agencies should not detract from, and preferably enhance, the services provided to Australian residents. In some jurisdictions this is an unwritten requirement. In others, the principle is spelt out explicitly in export guidelines (see chapter 4).

Some participants acknowledged that diverting resources to exporting can affect an agency's capacity to carry out its core functions. The Great Barrier Reef Marine Park Authority explained:

> There is regularly a demand for the services of individuals for both core activities ... and for [export] consulting activities. This can lead to conflict over the relative priorities of external consulting and core responsibilities (sub. 4, p. 7).

For some agencies, this has inhibited involvement in exporting. For example, while the Australia New Zealand Food Authority sees strong demand for its services in the region, it:

> ... has not been in a position to commit more than minimal resources to the regional activities given the commitments to a wide range of resource-intensive core functions (sub. 22, p. 4).

However, most agencies saw this tension as minor and easily manageable, particularly given the generally small scale of their export activity.

Indeed, the widely held view is that exporting can be of considerable benefit to domestic service provision. Agencies argued, for example, that having to compete in the international market helps them provide better services domestically and allows their staff to learn more quickly about 'leading edge' technologies. Thus, the Department of Social Security said that exporting had improved its capacity to deliver services in Australia through:

- international benchmarking of its ability to improve social policy outcomes;

- enhancing its administrative processes through exposure to rigorous international tendering requirements; and

  enhancing the skills of its staff through placement in difficult operating environments.

Similarly, Queensland TAFE advised:

> Exporting has improved the quality of services provided domestically, as delivery and client services standards are enhanced to keep in step with international trends and the capabilities of our key competitors (sub. 17, p. 5).

Promoting international links

Many participants argued that government exports help to improve Australia's links with the rest of the world. For example, the Western Australian Department of Commerce and Trade said:

> ... as a people-centred activity, services are a culturally important way in which Australia can commercially and diplomatically integrate with Asia (sub. 13, p. 16).

They saw these links as contributing to broader economic and regional objectives and providing spin-offs for other Australian suppliers.

Facilitating economic and regional objectives

Agencies provided several examples of how exports of government services can help to improve systems in other countries, with benefits for Australia and the region. The Australian Customs Service considered its exporting helps to:

> ... influence the development of internationally accepted customs policies and procedures in the region, an outcome of significant importance to Australian exporters. It is an outcome that is also consistent with the broader objectives of the World Customs Organisation ... to modernise Customs administration (sub. 16, p. 3).

It added that there are also benefits for Australian suppliers:

> ... the export of our services ultimately benefits traders in the region by encouraging transparency, harmonisation and simplification of customs procedures (sub. 16, p. 4).

Similarly, CSIRO argued that its international activities provide a better basis for international trade through, for example, 'encouraging use of physical measurement standards' (sub. 25, p. 2).

And the Bureau of Resource Sciences mentioned that its export activities benefit Australia 'through reduced risk of incursion into Australia of exotic pests and diseases' (sub. 10, p. 3). (The Bureau exports in the fields of resource and environmental information systems, animal and plant health and fisheries management.)

Flow-on opportunities

As noted earlier, government service exports often involve private sector input. Indeed, the Queensland and Western Australian governments explicitly seek to involve private firms in government export contracts as a way of marketing the capabilities of their private sectors (see chapter 5).

In addition, many participants commented that government service exports, and the contacts made during the process, can lead to flow-on opportunities for other agencies and private firms. Reflecting this view, the Western Australian Department of Commerce and Trade observed that exports of government services:

> ... are increasingly acting as a lead into markets for all kinds of goods and services (sub. 13, p. 16).

Similarly, the Queensland Government considered that its agencies:

> ... can play a key role in the future economic directions of Queensland ... through the impetus it can provide in broadening and deepening Queensland's export base (sub. 17, p. 8).

And, at the Commonwealth level, the Health Insurance Commission saw its export and international promotional activities as:

> ... contributing to the elevation of the Australian health sector profile overseas as well as enhancing the nation's reputation within international fora and multilateral agencies (sub. 6, p. 2).

A few agencies provided specific examples of these flow-on benefits. Queensland Rail Consulting Services, for instance, pointed to 'employment generated in Maryborough by the export activities of rollingstock supplier Evans Deakin Walkers' (sub. 17, p. 10).

The Australian Geological Survey Organisation advised that it had undertaken consultancies involving design and supervision of major surveys which had subsequently been won by Australian companies. It went on to say that, as part of this process, it had:

> ... introduced Australian technology, especially world-class geoscience software, into several countries which represented new markets for those products (sub. 21, p. 3).

Looking forward, the Western Australian Department of Commerce and Trade suggested that the export of land management and titling systems may lead to exports of planning, surveying, valuation and architectural services.

3.2 Weighing the benefits against thecosts

Government service exports can provide a range of benefits to agencies and the Australian community.

However, as some agencies acknowledged, many of these benefits do not depend on a government entity making the export. For example, export revenue, employment generation, enhanced work skills and spin-offs for other suppliers will also accrue if a private firm undertakes the export on behalf of government. This already happens to a considerable extent. And, while government skills, contacts and imprimatur may be important to a project's success, this contribution does not necessarily depend on a government agency managing the project. For example, a private firm may buy in specialist public sector staff or, at a more general level, seek endorsement from government.

Moreover, exporting is not the only, or necessarily the best, way of achieving some of these benefits. For example, agencies may be able to improve their domestic service provision by undertaking international benchmarking or by seeking advice on best practice from specialist consultants.

Government involvement in exporting also entails a number of risks and potential costs.

Most obviously, failed export ventures can be costly. The New South Wales Public Accounts Committee (PAC 1995) documented examples of agencies — and therefore taxpayers — incurring significant financial losses on export ventures.

While the risk of failure is not confined to the public sector, the environment in which government agencies operate can hinder successful commercial operation. For example:

- Public service rules and regulations can increase costs and reduce agencies' ability to react quickly to opportunities and adapt to changing market conditions (see chapter 4).
- It can be difficult for agencies to blend a commercial focus with the often dominant non-commercial objectives that most must also meet.

Another consideration is that governments may be tempted to keep non-viable ventures afloat longer than is warranted on commercial grounds in the hope that they will avoid criticism associated with failed ventures. Further, competitive neutrality concerns inevitably arise whenever government competes with the private sector for business, an aspect discussed in chapter 5.

Given these potential costs, governments should be periodically reviewing whether it is appropriate to retain commercially viable export businesses in the public sector. In some cases, it may be preferable for agencies to withdraw from exporting and make their expertise available to the private sector. In this regard, the Victorian Government commented:

> ... where strong private sector companies can develop ... public agencies should withdraw from the provision of services over time (sub. 30, p. 3).

In cases where the export business is particularly significant and valuable, privatisation may be worth considering, as occurred when the Commonwealth privatised the Snowy Mountains Engineering Corporation.

Indeed, were it possible to get all of the benefits by exporting through the private sector (or by means other than exporting), then there would be little reason for government to undertake any direct exporting. In support of this view ACIL argued:

> ... government [should] focus on the development and promotion of its core activities through fostering partnerships with industry, rather than trying to take on an extra function and compete in the marketplace itself (sub. 15, p. 8).

However, the Commission concurs with the majority of participants who argued that direct exporting by government can increase the likelihood of winning contracts as well as the magnitude of the accompanying benefits.

It seems clear that the imprimatur flowing from government control can be important in winning some contracts. As the Department of Social Security put it:

> Our experience is that customers from other government agencies feel comfortable in taking advice from a Department of the Government of Australia. This realisation was the genesis of [the Department's] exporting activities (sub. 18, p. 12).

Similarly, the Commonwealth Department of Health and Family Services said that it:

> ... opens doors that may be closed to others by virtue of its stature as a national health ministry, as a funder and member of the governing bodies of the World Health Organisation ... and as a technical collaborator in international health matters (sub. 24, pp. 1-2).

Further, common sense would suggest that the spin-off benefits for domestic provision will usually be greater when an agency exports directly. That is, the closer agencies are to service provision/delivery, the easier it will be for them to learn the lessons from exporting and translate them to their core domestic activities. Indeed, it may be difficult in practice to separate out exportable services from core domestic activities. As the Victorian Government argued:

> ... in a number of sectors ... public agencies have developed significant capabilities and expertise ... That expertise is closely associated with [delivery of

> domestic services]. It is not possible simply to separate out the systems or the knowhow and market them separately ... As a consequence, some agencies have core skills which only they can export (sub. 30, p. 1).

In the Commission's view, such benefits will often outweigh the potential costs of governments becoming involved in exporting. This is particularly the case if the policy framework and institutional structures within which exporting occurs (see below) reduce the downsides and potential costs. Thus, the Commission sees it as appropriate for some government agencies to export their services directly.

3.3 The policy framework

At the outset, agencies need to be clear about their reasons for becoming involved in exporting, and to establish that exporting is the best way of achieving underlying objectives. As noted above, some objectives can be achieved in other ways.

For activities which pass this test, there is a need for a framework founded on accountability and transparency, to reduce and manage the risks of government export activity and increase the likely success of individual ventures.

The guiding principle for this framework should be that exporting by government agencies enhances, or at least does not reduce, services provided to Australian residents. Exporting by government service agencies cannot be viewed purely in terms of its commercial viability. Government agencies are funded to provide services to Australian residents, and this function must continue to be their primary role. In some cases, this will limit their capacity to respond to commercial export opportunities.

This guiding principle underlies the approach taken in all jurisdictions. For example, the Queensland guidelines state that exports:

> ... should not be seen as an end in themselves, but rather should ultimately contribute (either directly or indirectly) to the improvement of the delivery of core services to its primary clients ... the Queensland public ... it is essential that the delivery of core [domestic] services not be diluted by undertaking international business activities (sub. 17, p. 7).

Similarly, the New South Wales guidelines require that exports:

> ... do not result in an agency giving priority to an international project at the expense of an agency's domestic obligations [and] have demonstrable and supportive links with an agency's core function(s) (New South Wales Government 1993, p. 3).

And the Victorian Government advised:

> ... meeting core domestic requirements is absolutely fundamental for government agencies and ... exporting should not compromise this capacity (sub. 30, p. 3).

Application of this principle will usually be straightforward. Indeed, as already noted, exporting and domestic service provision are often complements rather than substitutes.

But there will be circumstances where exporting provides a longer-term benefit to domestic services, but at some short-term cost. This suggests that, in applying the 'no disadvantage' principle, governments should give their agencies some scope to tradeoff long-term and short-term effects. In this vein, the Queensland export guidelines (see next chapter) specify:

> Public sector export activities will ... *ultimately* contribute (either directly or indirectly) to the improvement of the delivery of core services to its primary clients (ie. the Queensland public). (italics added)

Beyond this guiding principle, the policy framework must also:

- encourage commercial practice;
- ensure that risk is managed properly;
- protect and reward the public sector's intellectual property; and
- provide for stringent accountability and reporting requirements.

It is also desirable for governments to separate their commercial export activities and any significant broader role in facilitating exports. And competitive neutrality principles must apply so that government competes with the private sector on an equal footing.

This policy framework is broadly consistent with the approach taken by all Australian governments. But the specific requirements in each jurisdiction vary. These matters are discussed in subsequent chapters.

Recommendation 3.1

Government agencies should only export their services where this enhances, or at least does not reduce, the level and standard of services provided to Australian residents.

In applying this principle, governments should provide their agencies with some scope to balance longer-term gains for domestic customers against any short-term costs.

4 EXPORT GUIDELINES

The previous chapter concluded that exports of government services can be beneficial, provided there is an appropriate policy framework in place. This framework should:

- set out a government's attitude to exporting by its agencies;
- spell out more detailed requirements in areas such as risk management; and
- ensure there are high levels of accountability and transparency.

Australian governments endeavour to provide this framework in a variety of ways. This chapter looks at these. It also examines some specific components of the framework including risk management, intellectual property and public reporting.

4.1 Current approaches

Exporting by government business enterprises (GBEs) is governed largely by agency-specific controls. Hence, the focus of broader policy frameworks in place to guide government service exports is on non-corporatised agencies.

Across Australia, there are several different approaches:

- New South Wales, Queensland and Western Australia have formal export guidelines.
- South Australia relies on a review panel process together with the centralisation of much export activity through a publicly-owned project manager.
- Victoria and the Northern Territory also have public project managers. Beyond this, their agencies are subject to general public administration requirements and Ministerial oversight of export activities.
- Other jurisdictions rely solely on general public administration requirements and Ministerial oversight.

The distinction between these categories is not clear-cut. For example, South Australia's review panel has produced export guidelines against which it evaluates proposals from agencies. And, in those states with export guidelines, export activities are still subject to Ministerial approval and service-wide requirements. As the Queensland guidelines note:

> ... the decision on the possible degree of involvement (if any) by a Government agency in international business activities will ultimately rest with the [portfolio] Minister ... (Queensland Government 1997, p. 6).

Formal export guidelines

The guidelines in New South Wales, Queensland and Western Australia inform agencies about their government's attitude to public sector exporting and the principles to apply to such activity.

First and foremost, they specify that export activity should benefit (or not disadvantage) core service provision (see chapter 3). Beyond this, they indicate that agencies should operate in a commercial manner, implement risk minimisation strategies and have in place accountability and review procedures (see box 4.1). The guidelines develop these principles and specify a range of other matters, including:

- the nature of the export activity permitted;
- the nature of any association with the private sector;
- the processes that agencies must comply with before exporting, and any required authorisations;
- requirements with respect to risk management, financial commitments and audit review;
- other government policies that agencies must adhere to — for example, policies on competitive neutrality, costing and commercialisation of intellectual property; and
- Ministerial accountability and approval processes.

Applicability to GBEs

Export guidelines are primarily intended to guide the activities of non-corporatised agencies. Indeed, Queensland's guidelines explicitly exempt agencies corporatised under the *Government Owned Corporations Act 1993*:

> ... because corporate governance arrangements put in place under this Act are considered sufficient to cover the matters addressed in the Guidelines (Queensland Government 1997, p. 5).

Box 4.1: Guiding principles in export guidelines

New South Wales

The primary function of public sector agencies is to provide services to the people of New South Wales. The government supports and encourages agencies to pursue international market opportunities provided that these:

- do not result in the agency giving priority to an export project at the expense of its domestic obligations;
- have demonstrable links with the agency's core functions;
- are generally undertaken on the basis of supplying knowledge and expertise, rather than undertaking construction activities or providing equity;
- operate on a fully commercial basis, with separate financial reporting; and
- are subject to appropriate levels of review, risk analysis and risk coverage with a view to minimising liability for the government.

Queensland

Government agencies should give priority to initiatives which advance the internationalisation of the Queensland economy and, in so doing, must adhere to the following principles:

- international business activities must contribute to the agency's function of providing services to the Queensland public;
- commercial principles are central to all public sector export activities, and the interests of the Queensland private sector must be taken into account in all such dealings;
- measures must be put in place to manage and minimise risk, and maximise public accountability;
- internal administrative and review arrangements must be structured on a basis suitable to involvement in international business; and
- appropriate consultation and reporting is to be undertaken with key agencies of government.

Western Australia

While the primary function of public sector agencies is to provide services domestically, the government supports and encourages exports if they:

- provide demonstrable involvement of, and benefit to, private sector organisations in the project or market;
- can be subjected to appropriate levels of audit review, risk analysis and risk coverage;
- do not result in the agency giving priority to an international project at the expense of an agency's domestic obligations;

- have demonstrable and supportive links with the agency's core function;
- are generally undertaken on the basis of supplying knowledge and expertise rather than undertaking construction activities, providing equity or taking the lead/prime role;
- ensure that, if an agency takes a lead role, commercial and management risks are identified and minimised; and
- are structured on the basis of appropriate commercial practices.

Sources: New South Wales Government 1993, Queensland Government 1997 and Western Australian Government 1997.

Similarly, other than in respect of the requirement to obtain permission from the Treasurer and Premier for any proposed equity investment, the New South Wales guidelines do not apply to 'self sufficient competitive bodies'. These bodies are generally free to export in the course of their core businesses, subject to the requirements in their legislation. In contrast, in Western Australia, all agencies are covered by that state's export guidelines.

Review of export proposals by a government panel

The South Australian Government guides the export activities of its agencies through the Government Services Export Panel and the activities of SAGRIC International.

The Panel reviews and advises on proposed export ventures by government agencies. In broad terms, the matters considered by the Panel are similar to those listed in the export guidelines noted above (see box 4.2). Moreover, in contrast to the less formalised approaches in some other jurisdictions, the Panel's procedures, objectives and assessment criteria are documented and have been sent to all agencies.

However, not all export proposals go before the Panel. Exclusions include activities which already have Ministerial approval, individual projects of less than $100 000 and non-commercial professional cooperation programs. For these exports, government guidance is provided through Ministerial oversight and public administration requirements.

Box 4.2: South Australia's Government Services Export Panel

The South Australian Government provides guidance to its exporting agencies through the activities of:

- a **Government Services Export Panel**, which formally reviews proposals from agencies and advises on their viability; and
- a **Government Services Export Unit**, which advises agencies in developing export opportunities, and supports the Panel. The Unit is staffed by SAGRIC.

Unless exempted, a government agency seeking to export must submit a business case for each export proposal to the Panel. For proposals involving significant risk, the Panel will require a full business plan.

The Panel considers export proposals by reference to processes and criteria it has disseminated to agencies in a *Government Services Export Manual.* There are a number of policy criteria, including:

- whether the opportunity relates to the core business of the agency;
- the non-financial benefits and costs to the agency; and
- whether the agency would be exposed to political or ethical risks.

Operational criteria concern:

- funding and payment arrangements;
- likely costs and expected profitability;
- the agency's competitiveness, experience and technical capability;
- the strategic value of winning a contract;
- the allocation and management of risk; and
- appropriately structured private sector involvement.

In general, the Panel considers that an appropriate model is for the public sector to exploit any intellectual property with potential commercial export value that it develops in the course of conducting core business by inviting competitive bids from the private sector to acquire rights for the further exploitation of the intellectual property at private sector risk.

Agencies receiving assistance from the Government Services Export Unit have direct access to SAGRIC's services. However, they are not obliged to involve SAGRIC in the later implementation of projects.

Source: SAGRIC, *Government Services Export Manual*.

Ultimately, many of South Australia's government service exports are made through SAGRIC — the state's publicly-owned project manager (see chapter

6). The South Australian Department of the Premier and Cabinet said that, apart from education exports, SAGRIC 'is probably responsible for at least half of the value of exports' by agencies in that state (sub. 14, p. 1).

Oversight by a central coordinating body

Most of Victoria's government service exports are also made through a publicly-owned project manager — the Overseas Projects Corporation of Victoria (OPCV). There are no formal guidelines governing this export activity. Rather, government requirements are conveyed directly through Ministerial oversight of the Corporation and the accountability provisions under which it operates.

Similar arrangements apply to agencies exporting independently of OPCV. In this regard, the Victorian Government advised the Commission of its views that:

- meeting core domestic requirements is fundamental and exporting should not compromise this;
- exporting should be small scale in relation to total turnover, and preferably should avoid any significant investment costs;
- it should preferably be undertaken in consortia with the private sector;
- agencies are not expected to undertake entrepreneurial activity which exposes them to the type of risk that the private sector is best equipped to manage; and
- competitive neutrality provisions apply, but where strong private sector companies can develop, public sector agencies should withdraw from the provision of services over time (sub. 30, pp. 2-4).

The thrust of these requirements appears to be little different from the more formalised requirements operating in some other states, although they are much less publicly accessible.

The Northern Territory has broadly similar arrangements to Victoria, with most exports being made through a business unit within the Department of Asian Relations, Trade and Industry. Chapter 6 discusses the activities of the public project managers in detail.

Reliance on Ministerial oversight

Exporting by Commonwealth, Tasmanian and ACT agencies is subject only to Ministerial oversight and broader public administration provisions. For example, at the Commonwealth level, Department of Finance and

Administration guidelines cover such matters as commercialisation, risk management and accountability. In these jurisdictions, there is also an informal requirement that exports not be to the detriment of domestic service provision.

4.2 Clarifying the policy framework

While corporatised agencies have clear commercial objectives, the views of governments on commercial exporting by other agencies are not always clear. A broad general view may sometimes be discernible. However, participants said that, in practice, the attitudes of the Minister and chief executive officer are commonly the major determinant of an agency's involvement in exporting.

Several participants observed that where this attitude is ambivalent or non-supportive, exporting becomes very difficult. Moreover, changes in Ministers or chief executives — or in the strategies they are committed to — add an extra dimension of uncertainty. They said that, in such circumstances, it can be difficult to maintain the longer-term commitment often needed for successful exporting.

Accordingly, a significant number of participants saw merit in governments publicly and explicitly stating their views on exporting by their agencies. They argued that this would help agencies set any export activities within a framework of established government policy. And private firms involved in exporting services saw value in guidelines to promote fair competition between the public and private sectors. (Chapter 5 considers competitive neutrality issues in detail.)

The Commission also considers it desirable that governments clarify and publicise their attitudes to exporting by their agencies.

It accepts that the absence of formal export guidelines does not necessarily mean that agencies are exporting in a policy vacuum. A policy framework and accountability to government can exist without public guidelines — OPCV provides an example.

However, in the Commission's view, explicit and public guidelines are to be preferred over alternative approaches, as they provide greater certainty and transparency. They can:

- make a government's stance on public sector exporting clear to agencies, private firms and the community generally;
- provide greater clarity to agencies about the requirements that any export activity must meet;

- help ensure that the outcomes of export activity are transparent and that agencies are held responsible for those outcomes; and
- help dispel concerns about government using its position to unfairly compete for export business with private firms.

Significantly, the Victorian Government and the Commonwealth Department of Finance and Administration voiced support for the introduction of explicit guidelines in their jurisdictions. The Victorian Government saw formal guidelines as further enhancing decision making:

> ... by clarifying a number of issues including risk management and relationships between domestic market activity and exporting (sub. 30, p. 6).

The Commission stresses that such guidelines should not be seen as supplanting Ministerial approval for agencies' export activities. It sees continuing oversight as appropriate and desirable.

Moreover, it emphasises that the focus of the guidelines should be on exports by non-corporatised agencies. For corporatised agencies, legislative requirements and board direction provide an appropriate framework for any export activity. That said, the Commission would see little or no conflict between these agency-specific requirements and the requirements in general export guidelines.

What should the guidelines contain?

Export guidelines for non-corporatised agencies need to make clear:

- the relationship between an agency's export activity and its domestic responsibilities;
- a requirement for agencies to follow commercial practice (recognising that external benefits and flow-on effects to the exporting agency will sometimes justify deviations from purely commercial pricing);
- the basis for involving the private sector in projects;
- a government's attitude to capital investments;
- risk management requirements;
- internal administrative, review and reporting arrangements; and
- public reporting requirements.

Subsequent sections in this and the next chapter examine some of these matters in more detail.

Recommendation 4.1

Those jurisdictions which do not have explicit export guidelines for non-corporatised agencies should introduce them.

Export guidelines should include a statement of government policy on exporting by agencies. They should also address the relationship between export and domestic activities, pricing, private sector involvement, risk management, capital investments, the use of intellectual property, and accountability and public reporting.

4.3 Approaches to risk

Like other export activity, the export of government services is not without risks. Apart from poor commercial judgement, these can include adverse exchange rate changes, client default and natural disaster or civil disturbance requiring evacuation of staff.

The significance of these risks will vary according to such things as:

- who the client is;
- where the project is to be undertaken;
- the time frame over which resources are required; and
- whether the government agency is the prime contractor, partner in a consortium, or a contributor of resources to a team led by another entity.

Fee-for-service exports supplied through an aid program are generally considered to be low risk. As the Auditor General of Western Australia noted:

> ... usually the projects have clear objectives, milestones and agreed times for progress payments (sub. 1, p. 2).

If something goes wrong, the agency usually only stands to lose the resources committed to the project (and perhaps incur some damage to its reputation).

However, if agencies are exporting directly to foreign governments or private clients, the risk can be considerably greater. There can also be a time dimension to risk exposure if agencies have contracts to supply services over several years. In some cases, costs may be high in the early period, to be offset by later revenues.

From a policy perspective, the key point is that taxpayers, and thus the community, bear the risks attaching to government export ventures and the costs if things go wrong. As failures can have wider social and political implications, the risks are greater than for comparable private sector activity. For this reason, governments have been very concerned that agencies properly manage the risks associated with public sector export activity. As the Commonwealth Department of Finance and Administration put it:

> If the Commonwealth Government is to actively pursue export of its services, then it is essential that it not be exposed to undue risk or liability (sub. 34, p. 1).

Responses by governments

The general thrust of government policy in this area has been to limit risk exposure, contain the risks within the exporting agency (rather than having the government as a whole liable), and manage the individual components of risk (see box 4.3).

To reduce risk, governments have typically expressed a strong preference for fee-for-service exports. This is because risk is magnified if an agency invests capital in a project.

Some governments (such as New South Wales and Western Australia) explicitly forbid agencies to take equity positions without first obtaining the permission of the Premier and/or the Treasurer. Similarly, in Queensland, Cabinet approval is required for:

> ... capital [investment] to develop new capabilities (with the exception of minor costs relating to the possible customisation and/or repackaging of existing product capabilities to meet the needs of the international marketplace) solely to serve export activities (Queensland Government 1997, p. 6).

The Queensland guidelines also specify that details of 'proposed significant international commercial activities (or significant expansions of current activities)' must be submitted to Cabinet for consideration prior to commitment of resources. An activity is deemed 'significant' if it:

> ... is projected to constitute 10% or more of the agency's projected business volume in any financial year, or which in the opinion of the agency in consultation with the Department of Economic Development and Trade and Queensland Treasury is potentially risky or ground breaking in nature to the extent that it is considered appropriate that the matter be considered by Cabinet (Queensland Government 1997, p. 6).

Box 4.3: Approaches to risk — some examples

In **Victoria** and **South Australia**, much of the risk associated with exporting lies with the public project managers — OPCV and SAGRIC. However, agencies must also take steps to manage risk. For example, Vic Roads, which generally exports in conjunction with OPCV, said that it achieves this by:

- acting as a subcontractor in many contracts;
- undertaking head contract positions primarily with aid agencies;
- negotiating contractual obligations in line with each partner's responsibilities;
- requiring payment in hard currency (generally Australian dollars); and
- taking professional indemnity insurance with the Victorian Government Managed Insurance Fund (sub. 30, p. 2).

South Australia also scrutinises risk through the Government Services Export Panel (see box 4.2).

Other states rely on export guidelines and broader public administration and accountability requirements. For example, in **Western Australia**, export guidelines call for:

- project risks to be clearly delineated;
- liability to be limited, if possible, to the agency concerned; and

  risk to be 'quarantined to the greatest degree possible' through risk management guidelines and procedures including working primarily on a fee-for-service basis, seeking early legal advice, using standard contractual terms where appropriate, arranging for liability cover and undertaking financial and sensitivity analysis (sub. 31, pp. 5-6).

Agencies must also take account of *Guidelines for Managing Risk in the Australian Public Service*, Treasury Instruction 109 on risk management and the Australia/New Zealand Standard on Risk Management (AS 4360).

Queensland requires its agencies to put in place arrangements to 'manage and minimise risk'. This is to involve the production of business plans, appropriate financial management systems, insurance arrangements, feasibility studies, legal review of contractual arrangements, relying on fee-for-service arrangements and so on (Queensland Government 1997, p. 8).

Commonwealth agencies are subject to a range of requirements including *Guidelines for Managing Risk in the Australian Public Service* (MAB/MIAC 1996).

Are the current arrangements appropriate?

The need for effective risk management procedures is generally accepted. But it is also essential that governments ensure that their agencies adhere to these procedures, particularly given anecdotal evidence that this has not always been the case.

The question arises whether the risk management framework should be directed at minimising or managing risk. Put another way, should agencies be focusing solely on low risk projects, or accepting risks commensurate with likely rewards and managing risk effectively? At present, the emphasis seems to be on risk minimisation.

The economic and social costs to the community from failed commercial government ventures suggest the need for a cautious approach. As noted above, these costs will often be greater than for comparable private sector failures.

At the same time, there is a tension between governments requiring their agencies to operate in a commercial manner, and directing them to avoid more risky, but potentially more lucrative, projects. Indeed, in seeking to prevent failures, a risk minimisation strategy may see some worthwhile projects bypassed. This is no less a cost to the community than the cost of failed projects.

Many of the risks for government agencies from exporting can be managed. For example, the Auditor General of Western Australia commented:

> Most risks can ... be minimised by rejecting involvements with unstable governments, by proper risk management, and by having adequate insurance cover for most of the major risks (sub. 1, p. 2).

Similarly, OPCV's managing director observed that many risks:

> ... can be managed by taking adequate insurance cover, by building the cost of money into bids and by currency hedging. Proper professional management of projects is critical as is the ability to make critical assessments of risk during the bidding stage of a project (Hill 1996, p. 73).

However, if agencies are to be given greater commercial freedom, there must be a premium on effective project appraisal and risk assessment processes (and therefore on stringent accountability and approval mechanisms). Effective processes will reduce the likelihood of failures and increase the scope for identifying problem projects earlier.

To give effect to these requirements, agencies must have access to adequate risk management skills. (As discussed in chapter 7, this has been a problem in the past.)

In some jurisdictions, agencies can obtain assistance from central agencies and/or seek outside help. For example, the South Australian Department of the Premier and Cabinet reported that agencies in that state:

> ... manage risk through extensive use of Crown Law and the SA government captive insurance company, SAICORP. Where necessary, external consultants are also engaged ... Commercial alliances are also used for this purpose including joint ventures with SAGRIC to reduce the agency's direct exposure to risk (sub. 14, p. 10).

Nonetheless, some participants saw value in consolidating the risk management function through an OPCV or SAGRIC style body (see chapter 6).

Recommendation 4.2

Export guidelines should emphasise the need for rigorous risk assessment and management, and effective accountability mechanisms.

With such requirements in place, government agencies should have some capacity to undertake export projects which involve more than minimal risk.

What role for offshore investment of capital?

In looking at risk, another issue is whether government service providers (and budget sector agencies in particular) should limit themselves to fee-for-service exports. As noted above, this is the thrust of current approaches.

A few participants saw benefits for Australia from agencies investing capital (equity or otherwise) in offshore projects. They said that constraints on such investments may unduly limit profitable export opportunities.

But such investments generate contingent liabilities for the government and the community. And because government agencies are involved, aid and foreign policy considerations can become enmeshed with commercial objectives.

In any event, most saw such investments as of little practical relevance for budget sector agencies. Apart from the risk involved, they argued that the resources needed for even small equity investments would be beyond the capacity of most agencies currently involved in export activities.

The Commission agrees that capital investment in offshore projects is not a major issue, at least for budget sector agencies. It accepts that restricting exports to fee-for-service arrangements may occasionally prevent budget sector agencies from making the most of their marketable services. However, for most of these agencies, exporting is very much a marginal activity.

That said, with effective safeguards in place, there may be a stronger case for governments to permit such investments in particular circumstances. But these should be subject to high level approval on a case-by-case basis. As noted above, this is currently the practice in some jurisdictions.

Recommendation 4.3

Governments should not place a blanket ban on capital investments by non-corporatised agencies in offshore activities. Rather, export guidelines should make provision for case-by-case assessment of any such proposals. Responsibility for approving capital investments should reside with Treasurers.

4.4 Protection and use of intellectual property

Most government service exports embody intellectual property developed as part of agencies' domestic activities. This raises the issues of how to protect intellectual property in commercial dealings and ensure that agencies get an appropriate return for intellectual property passed on to others in commercial transactions.

Export guidelines in New South Wales, Queensland and Western Australia set out brief guiding principles for the protection of intellectual property. For example, the Western Australian guidelines state:

> If a prospective project will result in an agency giving another party or parties access to, or allowing the use of, an agency's intellectual property, the agency must ensure that its intellectual property is adequately protected ...
>
> The agency will need to include in the documentation of a project contract a clause or clauses which will have the effect of protecting its intellectual property and will need to ascertain that the clause or clauses will be effective in any overseas country involved (Western Australian Government 1997, p. 7).

The guidelines give government agencies the option to seek outside legal and commercial advice on these matters.

All jurisdictions have also developed general intellectual property policies for the public sector. For example, the Western Australian Government's Public Sector Intellectual Property Management Policy:

> ... establishes a whole-of-government framework to support successful commercialisation of public sector intellectual property, to determine intellectual property rights in the public sector environment and to provide for the appropriate allocation of net proceeds and rewards (Department of Commerce and Trade 1997).

Similarly, the Queensland Government's Information Policy Board has published a guide on commercialising government intellectual property which aims to:

> ... provide agencies with information on how to identify intellectual property which has the potential to be commercialised and practical advice on making decisions as to whether commercialisation of a particular item of intellectual property is appropriate, and how it should be handled (Information Policy Board 1995, p. 1).

The Commission considers that export guidelines should go beyond merely stating that intellectual property must be protected and rewarded in commercial ventures. The New South Wales guidelines provide an indication of the detail that could be provided. They use an example of the procedures to be followed where an agency brings its computer software to a commercial transaction. They specify that the agency should:

- assess the value of the software and decide whether it is too valuable to risk giving its joint venturer access to the software;
- ensure that its joint venture agreement prohibits the use or copying of the software and gives the agency appropriate rights if that prohibition is contravened; and
- ensure that the contract between the joint venture and the export client or customer contains similar protection (New South Wales Government 1993, p. 9).

There may also be value in including a synthesis of the key principles emerging from more general intellectual property requirements.

Recommendation 4.4

Governments should include specific provisions in export guidelines covering the use of their intellectual property.

Participants also raised some specific intellectual property issues relating to the provision of public resources to private firms and the pricing of intellectual property to meet competitive neutrality requirements. These are discussed in the next chapter.

4.5 Some operational matters

General public sector operating arrangements can constrain the commercial activities of government agencies. This section looks briefly at some constraints of particular relevance to export activity.

Public sector rules

A common perception is that public sector rules increase the cost of providing services and reduce the capacity of managers to respond to export opportunities.

Several agencies said that constraints on the quick transfer of resources between uses can be a problem, particularly in an environment where clients require agencies to be ‘on call’. They added that this makes it difficult for public agencies to compete with private firms which have greater resource flexibility.

Expenditure on overseas travel is sometimes seen as a special case requiring more stringent approval processes. Some agencies still require Ministerial authorisation for such travel. This can make it difficult to send people overseas at short notice in response to new opportunities or to service existing projects. As the Queensland Office of Racing argued:

> The delays incurred in [obtaining approval] often exclude Government agencies from competing with private sector counterparts. It is of little use telling a client that it would take up to five weeks to obtain permission to travel, when he/she wants you there by the end of the week to begin negotiating (sub. 17, p. 2).

Similarly, the Victorian Government advised that case studies provided by exporting agencies had shown travel approval processes to be ‘cumbersome’ and a constraint on exports.

While less of a problem than in the past, there may still be further scope to free up arrangements in this area. For instance, with proper accountability arrangements in place, it should be possible to fully devolve responsibility for overseas travel to agencies. This would see spending on overseas travel handled in the same way as spending on domestic travel.

Accountability and public reporting

At present, reporting of the outcomes of government service export activity is very mixed. For this reason, it is difficult to gauge exactly how successful past ventures have been (see chapter 2).

Yet accountability for outcomes, and public reporting of those outcomes, are central to protecting the community’s interests in this area. Without accountability and public reporting, there can be no guarantee that agencies’ exports are complying with the requirements spelt out above. Public reporting can also help to demonstrate that agencies are complying with competitive neutrality requirements (see chapter 5).

Accordingly, export guidelines should set out specific accountability and reporting requirements, as is the case in New South Wales, Queensland and Western Australia. They should establish the need for clear identification of commercial and non-commercial export activities. And where commercial export activity is significant, reporting should include:

- details of revenues, costs and profits for these activities using commercial accounting conventions; and
- details of cost allocation procedures.

By themselves, however, such requirements are unlikely to be sufficient. Apparently many agencies find it difficult to report satisfactorily because of inadequacies in accounting and reporting systems. These inadequacies can make it difficult for agencies to allocate costs and value their assets properly.

Public sector accounting reform, including the adoption of accrual accounting, will help address some of these deficiencies. For example, the Victorian Government said:

> The adoption of accrual budgeting and reporting ... in 1998-99 will ... enhance public sector financial management by providing the Government and the public with improved information on all financial operations of government, rather than transfers of cash alone. This ... will enable better management of all costs of service delivery (sub. 30, pp. 2-3).

There is also a need for agencies to ensure that their internal structures and practices allow them to meet enhanced reporting requirements.

In this regard, there may be value in creating specialist business or export units inside non-corporatised agencies, where commercial export activity is significant. This would replicate *some* of the disciplines available under the corporatised framework. A number of agencies have moved in this direction — for example, DEETYA International Services. Extending this approach more widely may help to enhance future export outcomes.

Recommendation 4.5

Budget sector agencies should report separately on the performance of any significant commercial export activity. Apart from information on revenues, costs, profits and rates of return, such reports should indicate the basis for cost allocation between commercial export and other activities.

5 COLLABORATION AND COMPETITION WITH PRIVATE FIRMS

5.1 Interface with the private sector

Government agencies can involve private firms in their export activities in a variety of ways, ranging from seeking advice through to entering into formal joint ventures.

The nature of these arrangements and the selection of private partners are the responsibility of individual agencies.

However, in New South Wales, Queensland and Western Australia, the government export guidelines spell out broad requirements for agencies when dealing with the private sector. For example, the New South Wales guidelines state:

> Where a public sector agency proposes to provide the relevant skills or expertise in conjunction with one or more other private (or public) sector agencies, the agency must fully negotiate and document exactly what each participant will contribute to the project, how risks and rewards will be shared, how consortium decisions will be made, and other matters relevant to the relationship of the participants with one another (New South Wales Government 1993, p. 6).

Similarly, the Western Australian guidelines call for:

- the adoption of best commercial practice;
- a competitive selection process in identifying a private sector partner; and
- provision of all relevant information to be made available to the Office of the Auditor General (Western Australian Government 1997, p. 4).

The Queensland and Western Australian guidelines go beyond procedural requirements and set private involvement in public sector exports as a policy goal. The Western Australian guidelines state that export activity must provide:

> ... demonstrable involvement of and benefit to private sector organisations in the project or market (Western Australian Government 1997, p. 2).

The Queensland guidelines state:

> Whenever appropriate, public sector export activities should be conducted in co-operation or consortia with the private sector; ... In all such commercial dealings, the interests of the Queensland private sector must be taken into account (Queensland Government 1997, p. 7).

However, the Queensland Government said that, where no applicable private sector expertise is available — for example, in government institutional strengthening programs — agencies may take an independent or even lead role.

In jurisdictions with no formal guidelines, private sector involvement is subject to Ministerial oversight and broader accountability requirements (see chapter 4).

Benefits from collaboration

Participants identified benefits for both the private and public sectors from effective collaboration.

For the private sector, participants considered that collaboration can provide firms with access to skilled government resources. For example, ACIL commented:

> The key to winning contracts in these markets is submitting the best team with the relevant expertise and experience ... Australian government bodies can be a significant source of this specific technical expertise ... (sub. 15, p. 4).

Some also saw collaboration as a means for smaller firms to access foreign markets. The South Australian Department of the Premier and Cabinet noted:

> Collaboration also provided a means for SMEs to access foreign markets which they would not otherwise be able to and to draw from governments' expertise to gain a cultural appreciation of the target market (sub. 14, p. 9).

And a number of participants observed that a link to a government agency can be a powerful marketing tool and, in some cases, the deciding factor in winning contracts with other governments. For example, the South Australian Department of the Premier and Cabinet argued:

> In some markets where government is important in the day-to-day transaction of business, an association with an Australian government agency might be essential to successfully compete in that market (sub. 14, p. 9).

In the same vein, Queensland Rail Consulting Services (QRCS) noted that it has:

> ...been invited to participate in projects because it is a government organisation. The government 'coat of arms' gives the project some official bearing and consortium partners want to take advantage of this respectability (sub. 17, p. 13).

For public sector agencies, participants saw the benefits of collaboration as including:

- access to private sector networks and commercial acumen;
- allowing agencies to participate in projects which would be too large for one entity to handle;

- providing opportunities to benchmark performance and to transfer best practice skills to domestic service delivery; and
- spreading marketing risk.

Impediments to effective collaboration

Some participants drew attention to problems in allocating and managing risks in joint ventures. For example, agencies in South Australia reported:

- the public sector's conservative attitude to risk does not sit easily with many private operators and may affect a successful relationship;
- the 'implied guarantee' which accompanies a venture in which a government has even a minority interest makes it difficult to share risk equally; and
- the inability of government to contribute investment capital to ventures can constrain effective collaboration (sub. 14, p. 9).

The Commission's views on public sector risk management and capital investment by agencies are set out in chapter 4.

Several participants raised the issue of how to protect public sector intellectual property when entering into collaborative ventures with private firms. The Australian Nuclear Science and Technology Organisation suggested that exposing intellectual property is a 'downside' of collaboration, although it went on to say that teaming with industry is essential for export success.

For private sector interests, access to public sector resources was a significant issue. Their major concern was that, in Victoria and South Australia, it can be difficult to secure public sector resources independently of OPCV and SAGRIC. This concern (and the responses to it) are discussed in section 5.2.

The Commission's assessment

Effective collaboration in the export of government services can enhance the quality of project bids, increase returns from projects and/or reduce project risk.

Nevertheless, for commercial government export ventures, private involvement should not be an end in itself. Governments should only seek to involve the private sector when it can contribute to project outcomes, as it often will. That is, the public sector should engage with the private sector on the same basis as the private sector engages with the public sector. As the Western Australian Department of Commerce and Trade commented:

> ... Governments need to take a commercial approach to dealing with private sector organisations in order to work effectively with them (sub. 13, p. 13).

This is not to downplay the wider role for government in using its influence to 'open doors' for the private sector in export markets. As discussed in chapter 3, governments can help to foster linkages with other countries, with spin-off opportunities for both private and public businesses.

But there can be problems in mixing a broader export facilitation role with commercially-motivated export activity. In particular, it can make it difficult to monitor the costs of the non-commercial activities and to subject the commercial performance of an agency to proper scrutiny. It can also provide management with an excuse for unsatisfactory commercial performance.

Recommendation 5.1

If governments wish to provide general support to the private sector to develop export markets, they should do so independently of commercial export ventures by their agencies and fund the activity separately.

Concern to protect public sector intellectual property in dealings with private firms is part of a broader issue of whether the government is getting an adequate return on the intellectual property embodied in resources used in exporting (see chapter 4).

However, two specific issues arise in relation to the provision of public sector resources to private firms.

The first is whether fees charged by government agencies for their staff provide for a return on any agency intellectual property that goes with those staff. Charge out rates for non-corporatised agencies are often subject to service-wide guidelines. For example, Department of Finance and Administration guidelines for Commonwealth agencies suggest charge out rates of around 2.5 times salary. While there were suggestions that some agencies, particularly in the tertiary education sector, undercharge for staff, no participants indicated this was a significant problem.

But in discussions, a number of agencies did express concern about the practice of giving staff leave without pay to work on projects with the private sector. They considered that where staff have developed specialist skills from working in a particular agency, granting leave without pay deprives the agency of any direct financial return on its intellectual property attaching to those staff.

The Commission agrees with the thrust of this argument.

However, it notes that, in some cases, much of the intellectual property that an individual can bring to a project is private rather than agency capital. In such cases, the leave without pay approach may be justified. Moreover, leave without pay may be a way of attracting, rewarding or retaining skilled staff. Importantly, it can also provide development opportunities for staff, adding to the skills base of an agency.

Recommendation 5.2

To provide for a return on their intellectual property, government agencies should generally charge for staff participating in private projects, rather than grant those staff leave without pay.

5.2 Competitive neutrality issues

From Australia's point of view, when either a public or private sector organisation could undertake a project, the most competitive entity should do it. This will sometimes be the private sector and sometimes the government sector.

Most of the time, competition for business will see the best supplier prevail and therefore deliver the right result for the community. But inefficient outcomes can result if government policies or practices advantage particular suppliers, be they government or private.

Competitive neutrality policies aim to remove these competitive advantages and disadvantages so that government businesses and private firms can compete on the basis of their comparative skills, efficiency and experience.

Participants' views

Private sector participants raised a number of concerns about the pricing of government service exports.

One contention is that budget sector agencies are effectively cross subsidising export activity from funding provided for domestic service provision. In essence, this amounts to recouping overheads on non-commercial domestic services and pricing exports at add-on cost. ACIL argued:

> ... marginal cost pricing, free provision of services and recovery of 'add on' costs only ... seem at odds with competitive neutrality legislation, and their use by public sector bodies would raise concern over the real efficiency and benefits of their export activities (sub. 15, p. 4).

Another contention is that, when tendering for projects, many government agencies do not incur all of the costs faced by their private competitors. The main concern in this area is the perceived failure of budget sector agencies to factor in tax equivalent payments. Some firms also said that problems have arisen when general government, rather than individual agencies, has met superannuation payments for public sector staff. And ACIL argued that a lack of clear guidelines on dividend policies, rates of return, debt guarantees and the like provides an unfair advantage to some government business enterprises.

Private sector interests also raised concerns about their access to public sector resources in Victoria and South Australia. The contention is that it can be difficult to secure public sector resources independently of the public sector project managers — OPCV and SAGRIC. For example, the Commission heard claims that in Victoria, if the private sector wants to deal with individual departments, it usually has to go through OPCV. In this regard, ACIL commented that the role of the public sector project managers in assembling and managing bids often involves:

> ... forming exclusive associations or partnerships designed to 'lock out' competitors, with the government body as the 'lead firm' that assumes the associated risks (sub. 15, p. 2).

It went on to say:

> Monopoly access to services is ... one of a range of issues that must be addressed under competitive neutrality (sub. 15, p. 4).

Not surprisingly, public sector agencies disputed the contention that they are competing unfairly with private firms. They pointed to guidelines establishing the need for full cost pricing of commercial government activities (including a return on capital invested) (see box 5.1). They also referred to the application of competitive neutrality principles to agencies' commercial activities. In this regard, the Auditor General of Western Australia said:

> ... these criticisms are not warranted in Western Australia as public sector agencies are required to observe the principles of competitive neutrality and ensure all projects are fully costed (sub. 1, p. 3).

Box 5.1: Examples of guidelines for costing commercial government activities, including exports

The then **Commonwealth** Department of Finance (1991) set out guidelines for costing of commercial government activities. Amongst other things, the guidelines specify:

- full cost recovery (including a return on capital) is a primary benchmark equating with what private sector organisations must satisfy in the long term, and would therefore be the policy objective of any public sector agency or unit that has a self-sufficiency or commercial charter;

- where full cost pricing would render a public sector supplier uncompetitive, it should market-price in the short term whilst pursuing efficiencies; if the cost disadvantage cannot be removed in a reasonable period of time, termination should be considered; and
- in multi-product cases, full costs of overall production should be recovered, joint costs being recovered in a way that reflects market prices and/or price elasticities.

The **New South Wales Government** export guidelines state:

- in preparing a budget for any project, the relevant agency must identify and incorporate the full direct and indirect costs of providing the relevant skills and expertise, including imputed Commonwealth and State taxes and charges where these do not otherwise apply; and
- costing for export projects must also include a profit margin consistent with requirements in the *Financial Distribution Policy for NSW Government Trading Enterprises*.

The **Victorian Government's** (1997) guide to implementing competitively neutral pricing principles specifies:

- agencies should price to cover the net competitively neutral cost of producing the output over the medium to long term. Where agencies are involved in producing a number of outputs as part of one accounting unit, it is the accounting unit which should achieve full cost recovery in the medium to long term: full cost recovery is not required for each output produced.

The **Queensland Government** export guidelines state:

- all costs (including all direct and indirect costs, amortisation of intangibles, depreciation of capital, and the costs of examining project feasibility) are calculated and considered in the pricing of commercial ventures. In particular, all agencies (other than fully commercialised agencies) will be required to comply with the 'full cost pricing guidelines' set out in the Queensland Government's Financial Management Standards; and
- international business activities are priced on a competitively neutral and profitable basis, especially having regard to the level of risk-adjusted return required to justify project participation.

Under the Queensland Government's Financial Management Standards, significant business activities (that are not government owned corporations or fully commercialised business units) are given flexibility to price in a competitive manner according to market conditions. For example, the policy permits the setting of 'loss-leader' prices provided that a prescribed rate of return is achieved in the medium term (Queensland Treasury 1994).

The **Western Australian Government** export guidelines state:

- in preparing a budget for any project, the agency must identify and incorporate the full direct and indirect costs of providing the relevant skills and expertise, including imputed Commonwealth and State taxes and charges where these do not otherwise apply; and
- costing for export projects should also include a profit margin where appropriate.

The Victorian Government stressed that, as a state-owned enterprise, OPCV is liable for all taxes and charges or equivalent payments faced by private firms. It also pointed to steps taken by other agencies to ensure compliance with competitive neutrality:

> ... the Centre for Forest Tree Technology ... works on the basis of full recovery for Victorian research and full cost recovery plus profit basis for external clients (sub. 30, p. 4).

Similarly, the Department of Social Security noted that it:

> ... seeks full cost recovery for the work it undertakes. Cost recovery includes all salary and overheads, travel, all costs in the field like accommodation and costs associated with supporting the consultants abroad (sub. 18, p. 28).

A number of agencies freely admitted that they have used the flexibility provided in pricing guidelines to set prices which reflect market conditions, and to pursue ‘loss leader’ strategies. For example, in summarising views from individual agencies, the South Australian Department of the Premier and Cabinet observed:

> Sometimes marginal cost was seen as the way to enter a market with a strategy to move pricing upwards as market positioning improved and there was an opportunity to differentiate the service. Many agencies noted the importance of meeting market prices (sub. 14, p. 8).

However, agencies went on to point out that such behaviour must still be consistent with meeting cost recovery and rate of return requirements in the longer term. They also pointed out that marginal costing and loss leadering are common strategies in the private sector.

Both the Victorian and South Australian Governments also strongly disputed claims that OPCV and SAGRIC have privileged access to public sector resources in those states. The Victorian Government stressed that its agencies are free to export independently, and to work with private firms or government organisations outside the state. It explained:

> The Victorian Government refutes categorically any suggestion that OPCV has a monopoly on public sector resources. Many examples exist where the private sector and Victorian agencies have worked together without any involvement from OPCV and in some instances they continue to maintain an ongoing relationship in terms of market development e.g VicRoads and SMEC in the case of road safety (sub. 30, p. 5).

Similarly, as noted in chapter 4, the South Australian Department of the Premier and Cabinet pointed out that SAGRIC's involvement in helping agencies to prepare export proposals carries with it no guarantee of managing the project.

The Commission's assessment

Pricing issues

Resolving whether there are, or have been, widespread breaches of competitively neutral pricing by government agencies is not easy.

- It can be difficult to separate endemic 'underpricing' from loss leader behaviour where an agency prices a bid below cost in an attempt to gain or retain access to a market. As government agencies pointed out, this can be a rational commercial decision if short-term losses are covered by the longer-term gains from better market access.
- It is common commercial practice to vary recoupment of fixed costs across individual contracts according to demand conditions. Thus, by themselves, low margins for particular projects, or on export activity as a whole at a point in time, are not necessarily evidence of a competitive neutrality problem.

However, while conclusive evidence to substantiate claims of breaches of competitively neutral pricing is lacking, it would be surprising if they were totally without foundation, particularly as far as budget sector agencies are concerned. For example, as noted earlier, some budget sector agencies are not in a position to cost their exports properly because of deficiencies in their accounting systems.

That said, over the last couple of years, there has been much greater emphasis on commercial practice and competitive neutrality within the government services sector. For example, as state-owned enterprises, the OPCV and SAGRIC are now subject to strong commercial disciplines. Governments are also improving their accounting systems, notably through the introduction of accrual accounting. Moreover, in all states and territories, firms with a grievance can now access competitive neutrality complaints handling mechanisms.

To reinforce these developments, the Commission considers that export guidelines for non-corporatised agencies should spell out pricing principles which meet competitive efficiency and neutrality requirements. In particular, they should:

- spell out all components to be included in an agency's cost base, including all taxes (or equivalent payments), charges and other costs normally faced by a private supplier, and the policy for allocating costs to the commercial activity; and
- provide agencies with similar pricing flexibility open to private sector competitors, subject to their meeting a longer term rate of return target.

The guidelines already in place in some jurisdictions are based around these principles (see box 5.1).

In endorsing the general principle that government agencies should be looking to achieve a return on their investments in export projects, the Commission stresses that the principle must be applied intelligently.

There will obviously be a need for some flexibility in target rates of return on an agency's overall export activity, as well as on individual projects. As in any commercial business, the appropriate rate of return will vary with the risk attached to the export activity. More importantly, where exporting generates spin-offs for core domestic service provision, a lower than commercial rate of return may be appropriate, even over the longer term. Thus, agencies such as the Australian Customs Service and the Insurance and Superannuation Commission saw such benefits as a reason to provide technical assistance at less than full cost or even free of charge. The Australian Customs Service contended:

> The export of technical services/advice is an important way for the ACS to influence the development of internationally accepted Customs policies and procedures in the region, an outcome of significant importance to Australian exporters (sub. 16, p. 2).

The Commission sees such practice as consistent with competitive neutrality requirements which are primarily directed at profit-making government businesses, rather than at agencies for whom any commercial activity is marginal. Moreover, the Competition Principles Agreement makes provision for 'exemptions' from competitive neutrality principles where the benefits exceed the costs.

The Commission also notes the importance of calculating rates of return on the correct asset base.

Where a government agency's export activity is ongoing, the base should comprise the additional assets required to make those exports, and revenue should be sufficient to sustain reinvestment in the export business.

However, where exporting involves the ad hoc sale of intellectual property or systems developed for the domestic market, provision for reinvestment may be irrelevant. In these situations, an efficient and competitively neutral price would not need to incorporate any allowance for, or return on, overheads.

Finally, the Commission reiterates the need for continued efforts to improve public sector accounting and reporting systems (see chapter 4). Without such improvements, it may be difficult to ensure that agencies are pricing in a competitively neutral way.

Recommendation 5.3

Export guidelines for non-corporatised agencies should spell out pricing principles that meet efficiency and competitive neutrality requirements. In particular, they should:

- spell out all components to be included in an agency's cost base, including all taxes (or equivalent payments), charges and other costs normally faced by a private supplier, and the policy for allocating costs to the commercial activity; and
- provide agencies with similar pricing flexibility open to private sector competitors, subject to their meeting an appropriate longer-term rate of return target.

Access issues

Despite the claims by certain private project managers, it is difficult to sustain the argument that OPCV and SAGRIC have privileged access to public sector resources in Victoria and South Australia. Under the arrangements in those states, individual agencies can export their services independently of these organisations. That particular agencies may *choose* to deal through OPCV and SAGRIC is not of itself evidence of privileged access.

Nonetheless, in the case of OPCV, there appears to be considerable confusion about its rights of access to Victorian public sector resources. This may have deterred some organisations seeking to use Victorian resources in export projects from approaching individual agencies directly. In the Commission's view, there would be benefit in the Victorian Government clarifying that its agencies are free to export through project managers other than the OPCV.

Such clarification could be included in the general export guidelines for non-corporatised agencies. As noted in chapter 4, the Victorian Government supports the introduction of such guidelines for its agencies.

6 COORDINATION OF EXPORT ACTIVITY

Most state and territory governments (but not the Commonwealth) have arrangements to coordinate their exports of government services. 'Coordination' can simply involve providing agencies with access to information on export-related matters. However, it can also extend to such aspects as the management of projects, particularly where more than one agency is involved.

A number of participants (and recent reports such as the New South Wales Public Accounts Committee (PAC 1995) and Ives and Higgs 1996) stressed the importance of effective coordination mechanisms, particularly for exports by non-corporatised agencies. This chapter looks at the various coordination issues that arise in the government services area.

6.1 Current coordination arrangements

As set out in chapter 4, exporting by corporatised GBEs is generally subject to agency-specific controls. Thus, the focus of existing coordination arrangements is on non-corporatised agencies.

At the Commonwealth level, non-corporatised agencies are free to export their services without recourse to any coordination agency. However, they are subject to general Commonwealth guidelines (see chapter 4), the requirements of any agency-specific legislation and the directives of their Ministers.

Some agencies such as the Health Insurance Commission and the Department of Employment, Education and Training and Youth Affairs (DEETYA) have set up international consulting units to coordinate their export activities. These units both provide consultancy services, drawing on in-house expertise, and facilitate consortia of Australian expertise drawn from the private sector and other government agencies.

Other Commonwealth agencies such as the Department of Social Security do not have discrete consulting units. They draw consultancy teams together when export opportunities arise.

Under this decentralised approach to exporting, agencies can seek outside input if in-house expertise is inadequate. At the same time, they can also hire out their expertise to other organisations. For example, DEETYA International Services has both employed subcontractors from other government departments, the universities and the private sector to work on its projects, and supplied staff for projects led by other organisations.

At the state level, Victoria and South Australia each have a state-owned company to coordinate the marketing of services from agencies in their states. As well as coordinating export activity through their management of projects, OPCV and SAGRIC aim to centralise marketing expertise in one agency. More generally, their activities promote the export capabilities of their states.

In South Australia, there are also project monitoring arrangements separate from SAGRIC's commercial operations (see chapter 4). As part of these arrangements, the Government Services Export Unit provides specialist advisory services to government exporters.

Queensland has a unit within the Department of Economic Development and Trade to provide export advice and support to individual agencies. In addition to overseeing export guidelines, it provides agencies with general guidance on market opportunities, business plans, contractual arrangements, pricing issues and the like. It also organises seminars to assist agencies in this regard. Its main aim is to position agencies so that they can respond to opportunities. As such, it does not act as a project manager. Marketing, bidding, and project management are left to individual agencies to arrange, subject to the state's export guidelines. The central unit may, however, advise agencies on where they can go to get more detailed assistance on such matters.

Similarly, in Western Australia, the Department of Commerce and Trade oversees the state's export guidelines and provides general export advice and support to individual agencies. It explained:

> Under the Trade Through Aid Strategy, Commerce and Trade has organised 20 seminars advising local organisations how to access the aid programs of various agencies and outlining how Commerce and Trade can assist them identify and win international projects ...
>
> Commerce and Trade has also organised missions that have taken Western Australian organisations to present their credentials and bid for projects ... (sub. 13, p. 7).

The Western Australian Government has also provided incentives to SMEC to set up an international projects management office in Perth to help market the services of the state's agencies (if they choose to use it). The Department said:

> The role of the office is to form consortia of Western Australian private and public sector organisations to bid for and implement international aid and commercially funded projects, particularly in the infrastructure, health, education, agriculture and environment sectors (sub. 13, p. 7).

The Northern Territory has an International Project Management Unit within the Department of Asian Relations, Trade and Industry. However, its functions are broader than its Queensland counterpart. In addition to facilitating government service exports, it acts as a project manager. The Northern Territory Government noted:

> The International Project Management Unit (IPMU) is the department's prime exporter of government services ... [Since its inception in 1988] the role of IPMU has ... been expanded and strengthened to include the roles of:
>
> - management of overseas aid projects;
> - provision of training programs for overseas clients; and
> - acting as a management agent for Asia Pacific specialists (sub. 28, p. 3).

IPMU was declared a Government Business Division in 1995. Thus, the Northern Territory approach is broadly similar to the OPCV and SAGRIC approaches.

New South Wales agencies export individually, subject to the state's export guidelines (see chapter 4). Many New South Wales agencies rely on expertise developed in-house to manage export projects. For example, the Departments of Health and Education have set up their own contracting arms to bid for and manage projects. However, agencies in the state can, and do, use outside expertise. The New South Wales Technical and Further Education Commission, for instance, said that New South Wales TAFE has had an ongoing involvement in a cooperative venture with TAFE SA and SAGRIC through Austraining International:

> This strengthened our position in Indonesia and other areas of the Asia Pacific Region (NSW TAFE Commission 1996, p. 51).

There are no formal coordination arrangements for the export of government services in Tasmania or the Australian Capital Territory. Few agencies in these jurisdictions have been involved in exporting. Those that have — for example, Tasmania's Hydro-electric Corporation, the ACT's electricity and water agency, ACTEW Corporation, and some education institutions — have been responsible for undertaking or organising all aspects of their export activities.

In addition to the specific arrangements in Western Australia, the private sector plays a more general coordination role through its management of export projects that draw on government expertise. For example, ACIL noted:

> ... government associates on [its] current projects include the Australian National Training Authority, the Northern Territory Government through its International Project Management Office, Queensland TAFE and all Australian Police Forces (sub. 15, p. 1).

Apart from ACIL, private sector specialists in this field include SMEC, Kinhill Engineering, Coffey MPW, and Hassall and Associates.

6.2 The merits of coordination arrangements

Participants' views

In looking at the merits of coordination mechanisms, it is important to distinguish between an export facilitation role and a more formal project management role.

Most participants saw value in some form of centralised arrangement to facilitate government service exports. They argued that there are benefits in providing agencies with access to general advice on export matters. A number said that access to such information is particularly useful in reducing the costs and risks for 'novice' export agencies. More generally, participants said that centralisation of expertise avoids the waste inherent in each agency reinventing the export wheel.

Further, some argued that a centralised agency can help foster closer links between government, industry and overseas institutions. For instance, Queensland Rail Consulting Services commented:

> One advantage of a coordinating government agency is that they can act as an information channel and lobbying platform to government and can also facilitate introductions to government officials. Such facilitation can assist in the development of strong relationships with senior decision makers from client bodies (sub. 17, p. 16).

However, there were divergent views on whether coordination should extend to the centralisation of the project management function. Most of the comments were in relation to project management at the state level. But there were also comments in this context at the Australia-wide level. (Australia-wide coordination is discussed in section 6.3.)

Those seeing benefits in a centralised project management function argue that it concentrates skills in one organisation. For example, OPCV's managing director observed:

> It centralises skills in proposal preparation (each multilateral agency has a different approach as does the Australian aid program), project management, financial management (including matters such as professional indemnity insurance, taxation implications and overseas travel requirements) (Hill 1992, p. 205).

Similarly, the Health Insurance Commission said:

> The main benefit of umbrella project agencies seems to be that such organisations would ideally possess the in-house marketing and commercial skills to win and implement projects profitably (sub. 6, p. 6).

And, from the clients' perspective, there is an argument that a centralised coordination agency provides a single point of entry into the Australian public sector. Some participants said that this, in turn, helps a state to present a unified image in overseas markets and to brand name its services. The Victorian Government explained:

> ... OPCV confers benefits not only to specific project participants, but also more broadly in terms of branding and promoting the assets and capabilities of Victoria, in a way which the private sector would not be able to or be expected to do so (sub. 30, p. 5).

For these sorts of reasons, the New South Wales Public Accounts Committee recommended (in 1995) the introduction of a body similar to the OPCV in New South Wales (PAC 1995). It saw such a body as adding a 'much-needed dose of professionalism', arguing that the export performance of New South Wales agencies fell short of those in South Australia and Victoria. The New South Wales Government is still considering the recommendation.

However, many participants argued against extending the OPCV or SAGRIC model to other jurisdictions. Some saw considerable advantages in agencies retaining full control over their export activities, and the resources allocated to them. They considered that such activities are closely linked to core domestic activities, and were concerned that the benefits for domestic activities could be lost if exporting was shifted to single entity. For instance, the Queensland Government advised:

> [The 1994 Queensland Government Review] suggested that a separate and central contracting vehicle such as the Overseas Projects Corporation of Victoria was not considered appropriate for Queensland, primarily because such an entity could:
>
> - take entities and expertise away from their parent Departments;
> - reduce departmental control over their own resources;
> - restrict access to departmental resources.
>
> Instead it was felt that a central coordinating unit, tasked with providing advice and support, would be a more cost effective and practical option for Queensland (sub. 17, p. 11).

Similarly, the Commonwealth Department of Social Security noted:

> While there are some benefits in centralising the response area within government, those benefits are outweighed by the loss of contact with the core departments (sub. 18, p. 27).

A particular concern is that a centralised agency may constrain the way agencies can operate. For instance, Australia TAFE International observed:

> ... such coordination may reduce flexibility and market responsiveness, and may impair an individual provider's incentive to succeed (sub. 2, p. 12).

Australia Post's opinion was that there may be:

> ... a risk in loss of flexibility in the use of a central agency that would attempt to coordinate exports from government bodies (sub. 26, p. 5).

And the Health Insurance Commission argued:

> The disadvantages of broadly based umbrella project bodies are that they: are likely to have difficulty in effectively covering the variety of the government service sectors; would not be able to take full advantage of the marketing networks of the operating agencies; and, they may not be sufficiently responsive to the specific needs of the particular sector (sub. 6, p. 4).

Participants holding these views went on to argue that responsibility for exporting should therefore lie with individual agencies rather than with a centralised agency. The Department of Social Security concluded:

> So as to develop notions of: promoting regional cooperation; furthering DSS's institutional capabilities and image; and strategically placing Australia into the future, there needs to be a closer link to the agency doing this rather than a centralised group with commercial responsibility (sub. 18, p. 27).

Moreover, some participants suggested that the opportunity to extend the OPCV or SAGRIC models, whatever their intrinsic merits, is now past. They argued that it would be more difficult and costly to establish these agencies today. The South Australian Department of the Premier and Cabinet also told the Commission that an additional consideration in the South Australian situation was (and is) that few agencies have the critical mass to support the marketing and project management systems necessary to sustain a commercial operation in their own right. It went on to suggest that this is not necessarily the case in the larger states.

A number of participants also suggested that, where there is a case for centralising the project management function, this should be the responsibility of private project managers. Thus, Coffey MPW argued:

> The private sector in Australia has a well developed consulting services group that is more than willing to work with Government agencies in the export of their services ... If there is scope for export, agencies could call for expressions of interest from the private sector to work with them for mutual benefit. In this way there is a sound mix of public sector expertise and private sector risk and project management skills resulting in greater accountability (sub. 33, p. 1).

Some went on to argue that governments should abolish or sell public agencies competing in the general consulting market. For instance, Hassall and Associates observed:

> ... there is little to be gained by having [OPCV and SAGRIC] remain in public ownership and ... they should be privatised (sub. 32, p. 4).

The Commission's view

The Commission sees value in the Commonwealth and each state and territory government having a 'whole of government' arrangement to facilitate and, at least to some extent, coordinate the export of government services by non-corporatised agencies.

Across-the-board introduction of export guidelines would provide some centralised guidance to agencies in all jurisdictions as well as a degree of coordination. However, the Commission sees benefits in extending this guidance to include:

- the provision of generic information to agencies on such aspects as bid preparation, marketing and best practice approaches; and
- advice on where to obtain more detailed assistance on such matters.

Such arrangements should be especially useful to agencies which are new to exporting, or new to exporting in particular countries or fields. They could also help to avoid the cost of each agency reinventing the export wheel.

The Commission does not, however, see a strong case for establishing public sector management agencies like OPCV and SAGRIC in other jurisdictions. The marketing of Australia's government services is much better developed than when these agencies were established. Private sector project managers and some individual agencies have acquired considerable skills in managing and marketing government services over the years. Thus, it is doubtful whether new public sector managers would add much value to an already competitive market. And for individual agencies, centralising commercial responsibility would weaken the link between exporting and core domestic activity — often one of the (main) reasons for agencies exporting in the first place.

In rejecting the wider application of the OPCV and SAGRIC project management models, the Commission is not downplaying the role that these organisations have played. They appear to have operated effectively in a highly competitive market. More generally, the two organisations have played a valuable role in developing government service exports in Australia.

6.3 Australia-wide coordination

While there is no formal Australia-wide coordination of exports of government services, there is a degree of national coordination taking place.

For instance, OPCV and SAGRIC can, and do, draw upon the services of government agencies (and private firms) in other states when bidding for projects — for example, through Health Partnerships International (see below). Similarly, private project managers have strong commercial incentives to mobilise the best public and private resources from around Australia. Thus, ACIL said:

> ... success in the international aid market is about providing the right skills and the right people ... it requires the flexibility to find the best people and the best organisations in Australia so as to put together the most competitive team (sub. 15, p. 7).

There have also been a variety of initiatives to coordinate export activity in particular areas such as marine services, public works, education and health (see box 6.1).

Participants' views

A number of participants acknowledged that competition between jurisdictions in the export market can sometimes involve wasteful duplication of effort and create confusion in the minds of clients. The Western Australian Department of Commerce and Trade said that problems are most likely to arise when either the Commonwealth or states could supply a service:

> While the specific services that States and Commonwealth might be selling may differ, a lack of coordination would preclude a 'comprehensive' service. In addition, the duplication of effort is a cost to the marketing of services overseas and it also sends out negative messages as to the competency of governments in Australia (sub. 13, pp. 8-9).

Box 6.1: Examples of national coordination initiatives

- Australian Marine Science and Technology Ltd — a consortium of 13 marine research and management agencies — is a vehicle for coordinating the export activities of member agencies.
- GeoJag Australia is a consortium of private and public sector agencies which coordinates the export of geoscience services and products.
- The Australian Procurement and Construction Council (APCC) — comprising Commonwealth, state and territory public works and procurement agencies — noted:

  > The [APCC export] initiative has established a strategic alliance between APCC members and regional public works authorities. It assists APCC members to network to co-ordinate their individual efforts and maximise Australia's export potential (sub. 7, p. 1).

- Australia TAFE International (ATI) — comprising Commonwealth, state and territory TAFE systems — aims to raise the profile of Australian TAFE in overseas markets. The ATI observed:

  > ... the new ATI will not only provide an array of market-oriented services to its members, but also represent TAFE's international interests in national fora (sub. 2, p. 1).

- The Australian Health Ministers Advisory Council has commissioned a consultancy on options for a health export vehicle made up of Australian governments. The Commonwealth Department of Health and Family Services considered:

  > The perceived benefits of this approach are the optimisation of bids through the pooling of expertise, the elimination of the risk of competing Australian bids cancelling each other out, economies of scale in market assessment and marketing, and national branding (sub. 24, p. 10).

  The Department went on to observe that the concept has:

  > ... already found an operational expression in the form of Health Partnerships International: a consortium of AusHealth International (NSW), OPCV (Vic) and SAGRIC (SA) which recently successfully tendered for a major AusAID health project in PNG worth $50-60 million over several years. It is possible that this, by default, could grow into the vehicle for intergovernmental collaboration (sub. 24, p. 10).

But at the same time, several participants argued that competition between jurisdictions for export business can also be healthy. Indeed, the Western Australian Department of Commerce and Trade said that 'drawing a line between wasteful and healthy competition is difficult and ultimately probably arbitrary' (sub. 13, p. 8).

As well as stifling healthy competition, participants also saw any formal national coordination mechanism as lessening the control of individual jurisdictions over exporting by their agencies, and constraining the capacity of those agencies to respond to export opportunities. Accordingly, there was universal rejection of the concept of a dedicated national agency to sell 'Australian public services' .

However, many saw value in the sort of sectoral initiatives documented in box 6.1. For example, the Queensland Department of Transport argued:

> There is a need for the coordination of Australia wide exporting activities within our respective fields. We are often calling on industry to network to increase opportunities and jointly target larger projects. However, there appears to be no existing forum for public international business units within industry sectors (such as transport, health, agribusiness, education) to network across Australia ...
>
> A national network of government bodies involved in industry sectors could add considerable value to our services and assist in identifying ... how best we can collectively gain advantage from visiting delegations, or target overseas projects (sub. 17, p. 13).

Similarly, the Bureau of Resource Sciences commented:

> These collaborative ventures [AMSAT and GeoJag] between public and private organisations present an effective 'Australia Inc.' image into the Southeast Asian and Pacific regions (sub. 10, p. 2).

The Commission's view

The current initiatives indicate that, when circumstances warrant, government service exporters from different jurisdictions can work together to further Australia's interests. In some specific sectors, there may well be significant benefits from this sort of coordinated approach.

However, like all participants, the Commission sees significant downsides in a formal national coordination mechanism. Indeed, such a mechanism could only have an appreciable impact if it were compulsory for agencies to work through it. But such compulsion would result in loss of flexibility at the agency level and could preclude beneficial competition between jurisdictions. Given these downsides, much more evidence of failure to coordinate well at the national level would be needed to support another layer of bureaucracy in this area.

That said, the Commission sees value in Ministerial forums, central units and professional networks exploring opportunities for beneficial national coordination of exports in particular sectors. The focus of such discussions would sensibly be on developing generally applicable mechanisms and protocols rather than on how to coordinate individual projects. Such forums would also provide opportunities for information exchange between the jurisdictions on export experiences and policy implementation issues.

7 AGENCY BEST PRACTICE

7.1 Introduction

Getting the policy framework correct is a necessary but not sufficient requirement for efficient exporting by government service agencies. Agency practices are also important. In this regard, there is a general perception that many agencies could operate more effectively.

The Service Exporters Survey (LEK Partnership 1994) highlighted a number of requirements for the successful export of services (see figure 7.1). Drawing on these responses, the LEK study concluded that there are three elements in successful exporting:

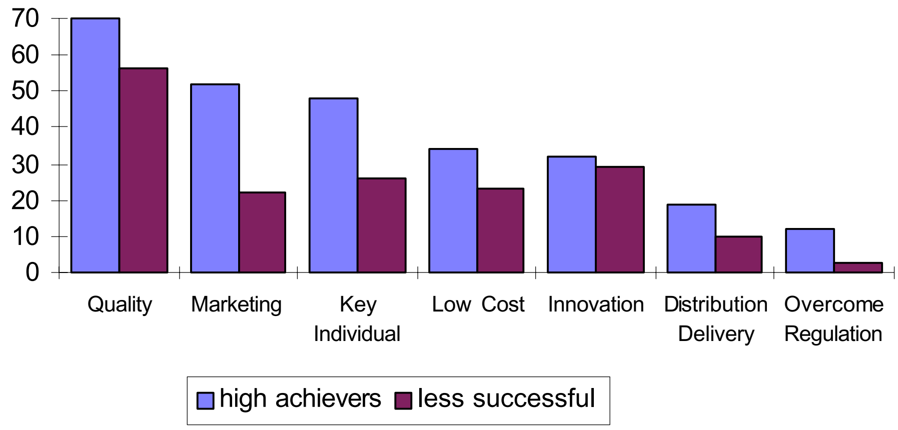
- developing the right commercial formula which includes product development, identifying market opportunities, pricing and marketing;
- identifying and securing the funding necessary to make the business work; and
- overcoming marketing challenges, regulations and logistical difficulties in accessing overseas markets.

Participants' views on the ingredients of export success in the government services market broadly conform with the LEK findings. This chapter draws on participants' views and experiences to illustrate what works in exporting government services and some of the potential traps for agencies seeking to sell their services overseas.

7.2 Preparing an agency for exporting

According to participants, making an agency 'export ready' is one of the crucial ingredients to export success. They said that, without adequate preparation, an agency may miss opportunities, fail in its endeavours and even damage the reputation of other exporting agencies.

Figure 7.1: Main sources of competitive advantage in exporting (percentage of respondents)



Note: 'High achievers' were those with more than 15 per cent growth in annual export revenues from 1982 to 1992 and whose exports were more profitable than domestic operations. 'Less successful' exporters had lower growth in annual export revenues and their exports were less profitable than their domestic operations.
Source: LEK Partnership (1994), p. 47.

Participants observed that, prior to commencing exporting, an agency must:

- be clear about the objectives of, and commitments entailed in, entering the export market;
- have a quality service which can be tailored to the needs of the target market;
- have access to the resources and commercial skills required for exporting; and
- be cost efficient relative to its competitors.

Exporting commitments and objectives

As noted in chapter 3, many agencies commence exporting in response to a particular opportunity. For others, exporting can be the logical extension of not-for-profit work in overseas markets. The Australian Customs Service described its experience:

> The Australian Customs Service (ACS) has, for many years, played an active role in the international customs community, both bilaterally and through its involvement in such bodies as the World Customs Organisation ... APEC's Sub-Committee on Customs Procedures ... and the Customs Heads of Administration Regional Meeting ... a grouping of Oceania customs administrations ...
>
> As a leader in customs procedures and technology, many regional customs administrations seek technical assistance from the ACS (sub. 16, p. 1).

But whatever the reason for commencing exporting, participants emphasised that an ongoing export business requires a long-term commitment. As the Auditor General of Western Australia commented, 'gaining access to markets takes time and money' (sub. 1, p. 2). Box 7.1 outlines DEETYA's approach to give effect to this commitment.

Box 7.1: DEETYA's experience and approach

DEETYA's entry into the international consultancy market followed on from its involvement in bilateral activities, Australian aid projects and the provision of technical assistance overseas. These activities provided a means for DEETYA to establish its market credentials and gain international business expertise.

The lessons learned in these activities underpinned the next stage of the Department's commercial development — bidding for international projects. DEETYA's first success came in 1992 winning a World Bank project.

To facilitate its commercial activities, the department created a dedicated business unit in 1993. This unit — DEETYA International Services — aims to promote DEETYA expertise and to compete for international project work on a fee-for-service basis. This has involved the development of:

- a marketing strategy to promote DEETYA expertise and capabilities; and
- administrative guidelines specific to international commercial requirements (for example: taxation treatment for financial consultancies; financial management; administration of travel allowance; administration of study tours; and identification and tracking of projects).

It has also involved identification of:

- Australia's competitive advantage in international education and training services; and
- particular exportable services (labour market analysis and planning; employment service delivery and program management; developing and implementing labour market assistance programs; developing and managing computerised systems to support labour market program management; industry restructuring; and vocational education in partnership with industry).

Source: Ives and Higgs (1996), p. 19 and information supplied by DEETYA.

Participants also commented that commitment must go hand in hand with clear objectives for export activity.

In this regard, they noted that effective corporate and business planning can enhance the setting of objectives. The Queensland Government's *Business*

Planning Framework (1996) suggests that business planning processes can be used by an agency to identify:

- its role and objective in undertaking export activity;
- the future potential for exports;
- export priorities;
- resourcing requirements; and
- performance criteria and targets.

Business plans can also be used to factor in service-wide constraints on export activity and mechanisms to address these. As discussed in chapter 4, such constraints include time-consuming processes in relation to travel approval and resourcing projects.

According to the New South Wales Public Accounts Committee (PAC 1995), inadequate planning has contributed to a number of failed government export ventures (see box 7.2).

Box 7.2: Some reasons for past failures

The New South Wales Public Accounts Committee cited examples of agencies in that state which had:

- entered export markets without studying them first — in one case, without first determining whether anyone was willing to fund a project, and having to withdraw at a loss when unable to secure financing;
- financed a project with the investment return denominated in a foreign currency which could not be hedged due to the closed nature of the foreign economy; and
- failed to properly evaluate their competitors — in one case, having to terminate a program after finding that the agency could not compete with similar but subsidised programs offered by overseas suppliers.

Source: PAC (1995), p. 52.

Having the right service

In setting objectives and making the commitment to export activity, participants stressed that agencies must have the 'right' service for export. They explained that this requires services to be appropriate to the needs of end users, as well as of intrinsically high quality.

Participants observed that agencies entering export markets often tend to focus on what they have to sell, rather than on what the market demands:

> "We have an excellent service to offer. Where can we find a market for it?" and then going about the world seeking a market (PAC 1995, p. 55).

They went on to say that this 'supply driven' approach will not usually sustain a viable export business. The Queensland Department of Mines and Energy, Safety in Mines Testing and Research Station considered:

> The key determinants relating to export success relate to the suitability of the product for the projected market ... unless a training product, for instance, is presented by properly qualified people at the right level it will not be accepted by the locals (sub. 17, p. 2).

Similarly, the Department of Social Security commented that it:

> ... does not try to "sell" the Australian social security system abroad. Rather it works with the customer to devise a system both in a policy sense as well as administrative sense, that allows the customer to advance their public administration in the way most suitable for them (sub. 18, p. 19).

Appropriate skills and resources

The Australian public sector has a wide range of highly regarded skills. Indeed, as discussed in chapter 2, in a number of areas Australia is a leader in its field.

However, there is also widespread agreement that many agencies lack the business expertise to translate these skills into successful exports. As Queensland's *Report on the Review of Policy on the Export of Government Services and Products* commented:

> Most departments have identified deficiencies in this area. In most cases, International Business Units are staffed by enthusiastic people who need proper training and relevant experience to be able to manage and operate within an international and commercial context (Queensland Government 1994, background paper, attachment 3, p. 4).

Similarly, SMEC pointed to problems created by intermittent agency involvement in exporting:

> International consulting requires a number of specialist skills in evaluating opportunities, drafting proposals, structuring projects and negotiating contracts; intermittent involvement in international development prevents many agencies from developing in-house the "critical mass" of expertise necessary for consistent success in an increasingly competitive marketplace (sub. 23, p. 7).

Box 7.3 outlines the lessons learnt by the Department of Social Security in this regard.

Box 7.3: Lessons learnt by the Department of Social Security

The department observed that its entry into export markets had highlighted the need for commercial skills and business experience:

- its potential consultancy personnel had recognised skills in public sector management and in policy development, but not in direct consultancy abroad;
- the bureaucratic background of its managers meant that they lacked commercial experience, entrepeneurship and risk-taking abilities;
- the department lacked the marketing skills necessary to overcome prejudices based on its lack of contracting experience and its public sector linkages; and
- it lacked expertise in estimating and costing, both of which had to be improved to be competitive in the international marketplace.

Source: sub. 18, pp. 13-14.

To minimise such problems in the future, participants stressed the importance of ensuring that agencies have access to the commercial skills necessary to export successfully, including:

- international business experience;
- commercial acumen;
- financial and risk management;
- exporting know-how, including costing, bidding, negotiating, contracting and hedging; and
- market intelligence.

As discussed in chapter 6, agencies can develop these skills in-house or source them externally from central coordinating agencies or private sector specialists. Where agencies choose the in-house route, Queensland's *Report on the Review of Policy on the Export of Government Services and Products* suggested a number of avenues for skill development, including:

- offering marketing and export skills courses for staff;
- providing corporate internships; and
- giving international units greater flexibility to recruit people with suitable qualifications.

Cost efficiency

As in any market, price and therefore cost competitiveness are important in competing in the market for government services.

However, agencies considered that the significance of price competitiveness varies considerably depending on the nature of the export.

For many aid contracts margins are very tight. Indeed, a number of participants observed that, with consultants skilled at packaging bids to suit a project's technical requirements, many bids for AusAID projects are within one or two points on the technical score. Thus they said that, while notionally price only has a 30 per cent weighting in AusAID contracts, it is increasingly becoming the determining factor.

Overall, however, participants stressed that price is only one of a range of factors which will determine export success. According to the Australian Geological Survey Organisation:

> Price is important but innovation, quality of service and effective implementation of appropriate technology and training are most important in our experience ... AGSO exports its services on a full cost basis and relies on the expertise, depth and capacity of the organisation as its competitive edge (sub. 21, p. 5).

That said, agencies acknowledged the importance of operating in a cost efficient manner. As the Department of Social Security commented:

> Domestically DSS strives to be prudent about its expenditure on administration. That prudence applies equally to consultancy work it undertakes (sub. 18, p. 19).

7.3 Understanding the market

Participants said that the success or failure of export activities often depends on the effort put into understanding the target market. As the Queensland Department of Main Roads and Queensland Transport explained:

> It is pointless to encourage public sector agencies to export unless they ... have the ability to research markets and target market needs (sub. 17, p. 12).

Without a good understanding of the market, it will be difficult for an agency to tailor a specific service to the needs of the end user (see section 7.2). But it is also important that agencies understand the broader market environment in which they are operating. According to participants, this involves:

- analysis and qualification of opportunities;
- understanding of aid agency/client relationships (see section 7.4);
- knowledge of resource availability;
- competitor analysis for each opportunity; and
- appreciation of the entry conditions and regulatory requirements of markets (see chapter 2).

In addition, submissions pointed to the importance of understanding the logistical difficulties of operating in markets often quite different from Australia. Box 7.4 reports some of the lessons learnt by Queensland Rail Consulting Services in its dealings in Vietnam.

Box 7.4: Exporting rail services to Vietnam

Queensland Rail Consulting Services has had extensive experience in Vietnam in recent years. This has involved frequent contacts between the QRCS and Vietnam Railways at a variety of levels — including chief executive, senior managers and technical staff of both railways.

According to the QRCS, some of the lessons to emerge from these dealings include:

- have a third party interpreter for the duration of visits;
- arrange a schedule of meetings before arrival;
- understand and know your audience if possible;
- use a well-credentialled agent with local knowledge;
- gain access to good business facilities;
- understand transport costs and delays;
- don't try to do too much on the first visit due to possible delays.

Source: Garrett (1996), pp. 67-71.

Agencies underlined the value of visiting target markets in overcoming these sorts of problems and in gaining a better understanding of the market. For example, according to the PSI Consulting Group review of DEETYA International Services, visits enable agencies to:

- understand the economy and the market place;
- meet with potential joint venturers in their home environments;
- explore possible distribution channels, their structure and trends;
- understand customer preferences, demand drivers, buying behaviours and values;
- understand competitor behaviour;
- understand the requirements of government channels of approval; and
- gain a qualitative appreciation of culture, values and the way business is conducted.

And to gain the maximum benefit from visits, it is necessary to have them well prepared:

> The value you gain from overseas visits will be considerably enhanced by the quality of the research you have undertaken at home before you leave, and the systematic way you have prepared for your visits (AusIndustry 1996, p. 5).
>
> ... visits should be properly planned and phased, ensuring that each builds constructively on the last (PSI Consulting Group 1997, p. 7).

Obtaining market information

Participants pointed to a range of sources of market information for agencies involved in exporting. Apart from expertise available from central coordinating agencies and private firms, or gathered from visits to target markets, these include:

- Commonwealth, state and territory government offices in other countries;
- Austrade; and
- AusAID and multilateral aid agencies.

Some participants noted that Austrade had helped them to establish whether a particular system or service had export potential and to identify prospective markets. Some agencies have also used Austrade to identify and track aid projects. As Australia TAFE International said:

> ... the education and training section of Austrade ... provided valuable marketing, information and support services to the education and training industry (sub. 2, p. 7).

However, many agencies have made little or no use of Austrade.

7.4 Operating successfully in the market

Effective marketing

Participants emphasised that effective marketing is a major contributor to export success, particularly in the Asia-Pacific region.

However, they noted that marketing will be successful only if the product is 'right' and cost competitive. In this regard, the New South Wales Department of School Education commented:

> The key determinant of export success will be the ability to competitively market our quality education services, the desirability of Australia as a destination for international students, the continuing availability of the services, and competitive pricing (sub. 9, p. 2).

Further, participants said that effective marketing cannot be a purely mechanical exercise. According to a study prepared for DEETYA, it is:

> The ability to present the ... services at the right time and in the right way that elicits a positive response to the customer's perceived needs (PSI Consulting Group 1997, p. 19).

And some saw effective marketing as being as much about raising an agency's profile as about selling a particular service. As the New South Wales Department of School Education put it:

> Other Australian states have been able to have a higher profile, particularly within Asia, through extensive marketing strategies and visits by State delegations (sub. 9, p. 2).

Dealing successfully with aid agencies

As discussed in chapter 2, a significant proportion of Australia's government service exports are made through AusAID and multilateral aid organisations. Indeed, for many budget sector agencies, aid projects are the major or sole source of export demand. Accordingly, participants stressed that agencies contemplating exporting must be aware of how the aid organisations operate.

One key requirement identified by participants is understanding the relationship between price and technical merit in the awarding of bids. As discussed earlier, they suggested that the practice can be somewhat different from the principles. Participants said that it is also important to understand the process by which aid agencies award contracts, including the timing of the process.

Further, agencies emphasised the need to treat the relationship with aid agencies as a long-term strategy, noting that:

- tracking aid projects prior to the formal tender process can give agencies more time to prepare bids; and
- long lead times for projects, and the effort required to establish a reputation, skills and expertise, can mean an ongoing commitment of at least 3 to 5 years.

Agencies stressed that experience and reputation are crucial to winning aid contracts. Thus, AGSO attributed its competitiveness to establishing:

> ... a reputation as a world leader in the provision of high-quality geoscientific information through innovative research programs and applying state-of-the-art technology efficiently and effectively (sub. 21, p. 5).

Using local agents

Many participants said that a local agent is a must when seeking to market services in the Asia-Pacific region. As QRCS commented:

> In many countries in Asia it is considered essential to have a local agent to act as a facilitator for business negotiations, especially when dealing with government organisations and agencies (sub. 17, p. 11).

Similarly, Australia Post observed:

> In respect of technology exports into the Asia-Pacific region links with private sector local resident companies as partners are essential. In fact the laws of several countries demand this. There is often great difficulty in making the correct choice and that is critical to success.
>
> In the sale of stamps to overseas collectors, we use a network of local sales agents. These are usually private enterprise stamp dealers, but in some countries, eg. People's Republic of China may be an arm of the postal administration (sub. 26, p. 4).

Agencies considered that local agents can provide a range of functions to exporters including:

- introductions to decision makers through their network of contacts;
- market intelligence, including early notice of upcoming projects; and
- a means to minimise logistical difficulties in delivering a service (see box 7.4).

Follow-up procedures

For the Department of Social Security, a criterion for the success of an export venture is whether the purchaser will be a source of repeat business:

> DSS wants its customers to think of DSS first when it comes to seeking suggestions for social policy and public administration reform (sub. 18, p. 19).

Relationships established during an export venture can help an agency when bidding for similar projects in the future. As the Great Barrier Reef Marine Park Authority said:

> ... staff generally maintain relationships beyond the end of the project with clients, thereby providing follow-up opportunities (and potentially further business) (sub. 4, p. 8).

7.5 Conclusions

The experience of participants outlined above provides some useful guidance for agencies considering exporting their services.

To many experienced in this field, the observations may seem obvious. Yet the problems that many agencies have faced suggests that there is value in summarising the lessons learnt (see box 7.5).

Box 7.5: Doing it right — what agencies in the export market had to say

Preparing the agency

Agencies should:

- be clear about the objectives of, and commitments entailed in, entering the export market;
- have a quality service which can be tailored to the needs of the target market;
- seek advice on the key factors influencing export competitiveness for their services; and
- be cost competitive.

Understanding the market

Agencies should:

- become familiar with the market and the competitive environment, including the nature of any regulatory and other barriers to entry; and
- visit the target market to gain an understanding of its particular requirements.

Operating successfully in the market

Agencies should:

- be prepared to invest resources in effective marketing;
- become familiar with the requirements of operating through aid agencies;
- consider employing a local agent to assist during all stages of the project cycle (from identification to implementation), and to facilitate access to key decision makers in government and aid agencies; and
- evaluate projects after completion to identify any inefficiencies in the process and possible future opportunities.

Source: Submissions.

A PUBLIC CONSULTATION

The Commission received the terms of reference for this study in July 1997. The study was advertised widely, and an Issues Paper sent to individuals and organisations with an interest in exports of government services.

During the course of the study, the Commission held two rounds of informal discussions with a range of individuals and organisations (see section A1). In the (more limited) second round, some participants had the opportunity to comment on the Commission's proposed findings and recommendations.

The Commission received 36 submissions, representing the views of more than 60 individuals or organisations. These are listed in section A2.

The Commission thanks all those who contributed to this study.

A1 Visits and meetings

In preparing this report, the Commission had informal discussions with the following individuals and organisations:

Australian Capital Territory

ACT Government

AusAID

Austrade

Canberra Institute of Technology

Department of Defence

Department of Employment, Education, Training and Youth Affairs

Department of Finance and Administration

Department of Foreign Affairs and Trade, East Asia Analytical Unit

Department of Health and Family Services

Department of Social Security

Health Insurance Commission

Therapeutic Goods Administration

SMEC International

New South Wales

Austrade

Azarias, Ms Patricia, Director, Public Accounts Committee, Parliament of New South Wales

Energy Australia

Land Titles Office

Department of State and Regional Development

New South Wales TAFE Commission

Treasury

Victoria

ACIL Australia

Agribusiness International

Department of Premier and Cabinet

Department of State Development

Kinhill Engineers

Lisle-Williams, Dr Mike, Partner, Deloitte Touche Tohmatsu International

Overseas Projects Corporation of Victoria

RMIT International

Queensland

Department of Economic Development and Trade

Department of Public Works and Housing

Queensland Chamber of Commerce

Queensland Government Services Export Forum

Queensland Rail Consultancy Services

Queensland Transport

South Australia

Department for Education and Children's Services

Department of Employment, Training and Further Education

Department of the Premier and Cabinet

Department of Treasury and Finance

Primary Industries South Australia

SAGRIC International

South Australian Research and Development Institute

Services SA

Western Australia

Department of Commerce and Trade

Department of Contract and Management Services

Department of Land Administration

Department of Minerals and Energy (The Geological Survey of WA)

Department of the Premier and Cabinet

Department of the Treasury

Health Department of WA (The Australia Clinic)

Public Sector Management Office

Water Corporation

Western Power

Worksafe WA

A2 Submissions received

ACIL Australia	15
Auditor General of Western Australia	1
Aus Health International	20
Australia New Zealand Food Authority	22
Australia Post	26
Australia TAFE International	2
Australian Customs Service	16
Australian Geological Survey Organisation	21

Treasury

Queensland Government: 17

Austa Energy Corporation

Cairns Port Authority

Capricornia Electricity Commission

Department of Economic Development and Trade

Department of Emergency Services

Department of the Environment

Department of Local Government and Planning

Department of Main Roads

Department of Mines and Energy, QTHERM Program

Department of Mines and Energy, SIMTARS

Department of Natural Resources

Department of Primary Industries

Department of Public Works and Housing

Department of Training and Industrial Relations, TAFE International

Education Queensland

Office of Consumer Affairs

Office of Racing

Port of Brisbane Corporation

Powerlink Queensland

Queensland Health

Queensland Rail Consulting Services

Queensland Transport

South East Queensland Electricity Corporation and Southern Electricity Retail Corporation

Snowy Mountains Engineering Corporation 23

Victorian Government 30

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