Part B Assessment of Governments' Progress

B1 Introduction

Australia's National Competition Policy (NCP) reform program builds on a process that was launched with the Trade Practices Act in 1974.

While the contribution of trade practices legislation was significant, by the late 1980s and early 1990s, it had become clear that a more comprehensive approach to reform across the three spheres of government was required. After a series of inquiries, the Council of Australian Governments (COAG) agreed in April 1995 to implement the NCP.

In short, the objective of NCP is to:

- extend the reach of the anti-competitive conduct laws in Part IV of the Trade Practices Act (TPA) to virtually all private and public sector businesses;
- improve the performance of essential infrastructure through implementing nationally co-ordinated reform packages in the electricity, gas, water and road transport industries and establishing a legal regime for third party "access" to the services of nationally significant monopoly infrastructure;
- review and, where appropriate, reform all laws which restrict competition, and ensure that any new restrictions provide a net community benefit; and
- improve the performance of government businesses through structural reform, introducing competitive neutrality so that government businesses do not enjoy unfair advantages or disadvantages when competing with private businesses and considering the use of prices oversight.

Governments also agreed to apply these reforms to local governments within their jurisdiction.

Recognising that Australia is increasingly operating as a single market rather than a series of State and Territory markets, the NCP encourages governments to take a national focus in considering change. A national framework helps overcome inconsistencies that can arise from a more piecemeal approach and allows each jurisdiction to capitalise on what the others are doing. Within the national framework, however, most implementation is occurring on an individual government level, with each government controlling how the policies are implemented in their jurisdiction.

B1.1 The NCP Agreements

The NCP reform program is set out in three intergovernmental agreements signed in April 1995 (see Box B1.1), operating in conjunction with the *Competition Policy Reform Act 1995*.

Box B1.1 The NCP Agreements

The Commonwealth and State and Territory Governments signed three agreements in April 1995 to implement the National Competition Policy reform package.

1. The ***Competition Principles Agreement*** (CPA) establishes reform principles in relation to access to essential infrastructure facilities; prices oversight of government businesses; structural reform of public monopolies; fair competition between government businesses and private sector businesses; reviewing the merits of anti-competitive legislation and regulation; and the application of competition principles to local government. Clause 1(3) of the CPA also sets out a community benefit test to enable governments to assess the merits of proceeding with particular reforms.
2. The ***Conduct Code Agreement***, operating in conjunction with the *Competition Policy Reform Act 1995*, sets out processes for amending the competition laws of the Commonwealth, States and Territories to extend the coverage of Part IV of the *Trade Practices Act 1974* to all businesses in Australia, irrespective of their ownership.
3. The ***Agreement to Implement the National Competition Policy and Related Reforms*** incorporates COAG reform agendas for the electricity, gas, water and road transport industries into the NCP framework. The Agreement also sets out conditions for financial transfers from the Commonwealth to those States and Territories which implement the NCP reforms, and the timetable for implementing reform.

B1.2 The net community benefit test

The objective of NCP is not to pursue competition as an end in itself, but to inject competition to boost economic performance and provide benefits to Australia. However, recognising that some areas of the economy have not previously been exposed to competition and that NCP can touch on complex areas of social and economic regulation, the CPA includes a mechanism to assess whether a particular reform is in the interests of the community as a whole.

The net community benefit test (see Box B1.2) covers a wide range of factors, including the environment, employment, social welfare and consumer interests as well as business competitiveness and economic efficiency. The assessment of these factors gives equal weight to economic and social considerations. In this sense, the NCP package seeks to balance economic accountability with social responsibility.

The Council has consistently stressed the importance of independent, transparent and rigorous processes by governments in considering the community benefit. This is essential to maintain community confidence that community benefit considerations have been objectively examined.

In general, the process for assessing net community benefit should reflect the significance and complexity of the issue (taking into account such matters as the range of affected stakeholders and community sensitivity). For the more significant or complex matters, objectivity is best served where processes are independent of the matter under review. As a minimum, however, interested parties must have an opportunity to participate and should have confidence that their views will be taken into account and given due consideration.

Where community benefit considerations are rigorously assessed, the best course of action – including whether to retain an anti-competitive measure – will be clear, and the community benefit will be best served by governments acting accordingly. Retention of restrictions on competition is consistent with NCP where the restriction has been assessed through a transparent, independent and objective process. Conversely, retention of restrictions where there is no objective evidence of net community benefit would constitute failure to comply with agreed NCP principles.

Box B1.2 The NCP community benefit test

Under clause 1(3) of the Competition Principles Agreement, governments take into account the following factors when assessing the merits, or appropriateness, of reforms:

- government legislation and policies relating to ecologically sustainable development;
- social welfare and equity considerations, including community service obligations;
- government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;
- economic and regional development, including employment and investment growth;
- the interests of consumers generally or of a class of consumers;
- the competitiveness of Australian businesses; and
- the efficient allocation of resources.

The list is non-exhaustive, meaning that any other relevant matter may also be considered when assessing the case for a competition reform.

B2 Prices Oversight of Government Business Enterprises

Legislated monopolies, businesses that operate in markets with natural monopoly characteristics and firms in poorly contested markets all have the potential to restrict output and overcharge consumers. Moreover, in some cases, newly introduced competition may take time to develop. In these circumstances, prices oversight may be warranted to limit abuse of market power.

Under the CPA, prices oversight of State and Territory Government business enterprises is primarily the responsibility of the respective State or Territory. As part of this responsibility, the States and Territories are to consider establishing independent sources of prices oversight, of their business enterprises, where oversight arrangements do not already exist. Alternatively, with the agreement of the Commonwealth, the States and Territories can subject their business enterprises to a mechanism administered by the ACCC.

Prices oversight arrangements exist in all States and Territories except Western Australia and the Northern Territory.

- In NSW, the Independent Pricing and Regulatory Tribunal is responsible for prices oversight in electricity, gas, water, waste and urban passenger transport.

- Victoria's Office of the Regulator General provides independent prices oversight in electricity, gas, water, ports and grain handling.

- The Queensland Competition Authority provides independent prices oversight of government business activities that are public monopolies or near monopolies, and which the Premier and Treasurer declare to be Government Monopoly Business Activities. Queensland is assessing major government businesses against criteria for declaration, commencing with port authorities.

- In South Australia, the *Government Business Enterprises (Competition) Act 1996* establishes a prices surveillance mechanism for the State's monopoly or near monopoly government businesses. SA Water Corporation is declared for prices oversight until 21 November 1999.

- In Tasmania, the Government Prices Oversight Commission (GPOC) regulates the pricing policies of the State's monopoly or near monopoly GBEs and government agencies, including the Metropolitan Transport Trust, the Hydro-Electric Corporation and a range of other government (including local government) businesses. Five monopoly businesses — Hydro-Electric Corporation, the Metropolitan Transport Trust, the Motor Accidents Insurance Board, Hobart Regional Water Authority and the North West Regional Water Authority — were originally scheduled in the GPOC Act. In addition, there is a mechanism under which other monopoly services can be declared.

- In the ACT, the Independent Pricing and Regulatory Commission has the power to regulate prices, make access determinations and carry out other functions with respect to businesses declared by the Minister. Industries subject to price regulation include electricity, water, public transport (buses and taxis) and gas.

B3 Implementing Competitive Neutrality Principles

B3.1 Competitive neutrality: what is it and why?

Competitive neutrality principles seek to encourage competition and better use of the community's resources by ensuring that government businesses operating in a market in which there are actual or potential competitors do not gain any net competitive advantage because of their public ownership. In essence, competitive neutrality principles are aimed at ensuring that significant government owned businesses operating in contestable or potentially contestable markets face the same market disciplines as their private sector competitors.

There can be significant economic efficiency and equity implications if government owned businesses compete 'unfairly'. For example, if a government business has special exemptions from the payment of taxes and charges, it may be able to undercut its private sector competitors. Such advantages can also form a barrier to the entry of potential competitors.

Where artificially lower prices charged by a government business cause consumers to choose that business's product, the production and investment decisions of both the business and actual and potential competitors will be influenced. If the government business is not otherwise the least cost producer, the allocation of resources toward production by this business will not be in the best interests of the community. Where this also reduces competition, the result may be a fall in the quality and range of goods and services. Longer term, scarce investment funds will shift out of higher-priced efficient production into lower-priced loss making activities, harming employment outcomes and overall economic activity.

Competitive neutrality policy is aimed at removing the advantages which allow for under pricing by government businesses. This helps to ensure that resources go to their best possible uses. It also brings increased competitive pressure on public businesses, helping to improve the operation of those businesses. Consumers will benefit from more competitive pricing and improved quality of government services. And where taxpayers' funds are no longer used to provide goods and services better provided by the private sector, and remaining government activities are more efficient, a greater proportion of total public funds is available for other priorities, for example, health, schools and welfare.

B3.2 CPA requirements for implementing competitive neutrality

Under the CPA, competitive neutrality principles must be applied, where appropriate, to all significant government businesses, including at local government level. Box B3.1 describes the nature of the businesses considered significant for competitive neutrality purposes in each jurisdiction.

In general terms, implementation of competitive neutrality involves:

- adoption of a corporatisation model for significant government business activities;

- payment of all relevant Commonwealth and State direct and indirect taxes or tax equivalents;

- payment of fees (or commercial interest rates), directed towards offsetting the reduced risk provided by explicit or implicit government guarantees on commercial or public loans;

- attainment of a commercial rates of profit (to ensure government businesses face a return on capital requirement equivalent to private businesses);

- compliance with those regulations to which private sector competitors are normally subject, for example, regulations relating to the environment and planning and approvals processes; and

- pricing of goods and services provided in contestable and potentially contestable markets to take account of all direct costs attributable to the activity, including the competitive neutrality-imposed costs.

All jurisdictions have competitive neutrality policy statements and guidelines to assist the implementation of competitive neutrality policy, and report annually on their progress. In addition, arising from obligations under the CPA, each has established a mechanism for investigating allegations that relevant government businesses are not appropriately applying competitive neutrality principles. Governments' annual reports must discuss allegations of non-compliance raised with complaints mechanisms within the scope of the jurisdiction's competitive neutrality policy.

Box B3.1 Significant Commonwealth, State and Territory Government Businesses

- The Commonwealth policy covers all bodies established principally as business entities (including Government Business Enterprises (GBEs), Business Units, share limited companies and competitive tendering and contracting activities) regardless of their size, profitability or class of business. Other government bodies which have commercial activities with turnover in excess of $10 million are also covered. Competitive neutrality principles may be applied to smaller entities upon the recommendation of the Commonwealth Competitive Neutrality Complaints Office.

- NSW has a Financial Policy Framework (FPF) which applies commercially based target rates of return, dividends and capital structures, regular performance monitoring, payment of State taxes and Commonwealth tax equivalents, payment of a risk related borrowing fee and explicitly funded 'Social Programs'. All significant GBEs that are monitored on a quarterly or half yearly basis are subject to the FPF. The corporatisation model is applied to local government entities with annual turnover above $2 million.

- All significant commercial Victorian Government Business Enterprises (now 22 following some privatisations since the first tranche assessment) are corporatised or commercialised and apply competitive neutrality principles. 'Other significant business activities' have applied appropriate competitive neutrality principles from 1 July 1997 or have been identified for competitive neutrality review.

- Queensland applies competitive neutrality principles to government business activities with annual current expenditure greater than $10 million and to businesses operated by its 17 largest councils. Size thresholds are used to identify three types of significant local government business activities.

- Western Australia defines significant government businesses by assessing the extent of actual or potential competition and the importance, to the Western Australian economy, of the market in which the government business operates. Western Australia considers that, in general, a business is unlikely to be significant unless it has annual turnover or assets greater than $10 million. Local government businesses with annual turnover of at least $200 000 are considered for competitive neutrality reform.

- South Australia applies competitive neutrality principles, where appropriate, to all significant business activities. Implementation of competitive neutrality principles was applied in the first instance to business activities with annual revenue greater than $2 million or assets greater than $20 million.

- All Tasmanian GBEs, except the Port Arthur Historic Site Management Authority, are subject to a full tax equivalent regime, dividend regime and guarantee fee. Tasmania has identified significant business activities within agencies and continues to regularly monitor activities in this area. Competitive neutrality arrangements are applied where appropriate.

- The ACT stated that it applies competitive neutrality principles where there is competition between a government business and another market participant. It has corporatised three business activities and is commercialising a range of other business activities, mostly within the Department of Urban Services.

- The Northern Territory applies competitive neutrality principles to all 11 of its Government Business Divisions and to the Territory Insurance Office (TIO). The TIO, the Power and Water Authority and the Darwin Port Authority are corporatised.

Source: Jurisdictions' 1996 policy statements and annual NCP reports.

What about Community Service Obligations?

A Community Service Obligation (CSO) arises when a government specifically requires a business to carry out an activity or process that:

- the organisation would not choose to do on a commercial basis, or that it would only do commercially at higher prices; and

- the government does not, or would not, require other organisations in the public or private sectors to undertake or fund.

CSOs are often established to meet government social policy objectives. Some examples of CSOs include:

- a direct payment by a State government, to certain disadvantaged consumers, to pay for some or all of their use of essential services, such as electricity and water;

- local councils providing waste disposal services to local nursing homes free of charge; and

- the requirement that Australia Post provide a standard letter delivery service throughout Australia for a uniform postage rate (currently 45 cents).

Applying competitive neutrality principles does not prevent the provision of CSOs, but it does place certain requirements on governments in terms of their costing, funding and interaction with other competitive neutrality obligations. The intention is to encourage more effective and transparent provision of CSO services, with minimal impact on the efficient provision of other commercial services.

For an activity to be recognised as a CSO, the provider organisation should be directed explicitly to carry out the activity on a non-commercial basis, for example, by legislation, government decision or a publicly available direction from a Minister. CSOs should be funded from the purchasing portfolio’s budget, with costs determined as part of a commercially negotiated agreement. CSO agreements should include similar competitive neutrality requirements as applied to other activities, that is, these activities should be able to pay taxes and earn a commercial rate of return (as if contracted out).

Where direct funding of CSOs entails unreasonably large transaction costs, portfolio Ministers may choose to purchase CSOs by notionally adding to the provider organisation’s revenue result, for the purpose of calculating the achieved rate of return. CSOs should be costed as if directly funded. This notional adjustment should be transparently recorded. However, for consistency with competitive neutrality requirements, there should be no adjustment to the commercial rate of return target of the service provider to accommodate CSOs.

The financial frameworks adopted by governments and supporting legislation provide for the identification of CSOs, including why the activity should be considered a CSO rather than a business function, and the explicit funding of identified CSOs from the purchasing agency’s budget. However, it is not clear that all governments routinely examine the effectiveness of different alternatives for delivering the CSO, or carry out on-going monitoring of the effectiveness of delivery once the CSO is in place, consistent with the resource allocation objective of the CPA. Moreover, the evidence from competitive neutrality complaints suggests that some governments need to ensure that, in practice, they provide clearly defined, budget funded CSOs in line with their stated policy approaches.

Common misconceptions – what the CPA does not require

Competitive neutrality applies to the significant business activities of governments, including those which government agencies operate as part of a broader suite of activities. It does not apply to non-business, non-profit activities of publicly owned entities. The Council encourages governments to consider business significance in terms of the effect of the business on its relevant market rather than only in terms of the size of the business.

Competitive neutrality does not require privatisation of government business activities, only corporatisation as appropriate. However, competitive neutrality does not prevent a government taking a policy decision to privatise a business activity. Neither does competitive neutrality require outsourcing of government activities. But when a government business participates in a competitive tendering and contracting process, it must comply with competitive neutrality policy. In-house business units should not have any unfair advantage over other public or private sector bidders.

Regulatory neutrality does not require the removal of legislation that applies only to the government business (and not to its private sector competitors) where the regulation is nevertheless considered to be appropriate.

Finally, competitive neutrality does not have to be applied as a matter of course. It should be applied only where the expected benefits from implementation outweigh the costs.

B3.3 Assessment of progress against neutrality objectives, by jurisdiction

Having examined the general policy approach of each jurisdiction in the first tranche assessment, the Council's second assessment looked for continuing progress with the application of competitive neutrality across significant business activities. The Council developed its assessment on the basis of information contained in governments' annual reports, including progress in applying competitive neutrality reforms to local government businesses, given the delays identified in the first assessment.

The Council also took note of alleged non-compliance with competitive neutrality policy, as provided by reports of complaints mechanisms, and governments' responses to those allegations. The view of the Council is that the recommendations of complaints bodies, and actions taken by governments to rectify identified breaches of policy, can be a useful indicator of the effectiveness of a jurisdiction's application of competitive neutrality policy. The Council expects recommendations of complaints mechanisms to be taken up by governments, unless the government can provide a convincing net public benefit case to support a different approach.

Commonwealth

Policy and scope of application

The Commonwealth Competitive Neutrality Policy statement (June 1996) (CNPS) deems all GBEs, Commonwealth share limited companies and Commonwealth Business Units to be significant business activities, and therefore subject to

competitive neutrality policy. Where other commercial activities of the Commonwealth meet the established definition of a 'business' and have turnover exceeding $10 million per annum, the merit of implementing competitive neutrality is determined on a case by case basis. This includes bids by in-house units for activities subject to the Commonwealth's competitive tendering and contracting guidelines.[11]

In general terms, Commonwealth competitive neutrality implementation requires:

- adoption of a corporatisation model for significant GBEs;
- payment of relevant Commonwealth and State, direct and indirect taxes, and tax equivalents;
- payment of debt neutrality charges or commercial interest rates;
- attainment of a commercial pre-tax rate of return on assets;
- compliance with regulations to which private sector competitors are normally subject; and
- pricing of goods and services provided in contestable markets to take account of all direct costs attributable to the activity and the competitive neutrality elements.

The actual implementation of these principles to particular businesses may vary depending on the market in which the business is operating. For example, where a business competes predominantly in a market where other participants have special arrangements for taxation, the business is required only to pay the same taxes as the majority of its competitors. Another example is that businesses, which are being corporatised or restructured along commercial lines, may have a lower pre-tax rate of return target for a transitional period of up to three years, to take account of identified public sector employment cost disadvantages.

Competitive neutrality complaints

The Commonwealth has established an autonomous unit within the Productivity Commission – the Commonwealth Competitive Neutrality Complaints Office (CCNCO) – for investigating allegations of non-compliance with competitive neutrality policy.

The CCNCO can investigate competitive neutrality complaints about any Commonwealth Government business. This is a desirable feature as it allows the CCNCO to recommend the application of competitive neutrality principles, where appropriate, to businesses below the Commonwealth's $10 million turnover threshold for significance.

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[11] To be considered a business by the Commonwealth, the following criteria must be apply: there must be user charging for goods and services; there must be an actual or potential competitor in the private or public sector; and managers of the activity must have a degree of independence in relation to the production or supply of the good or service and its price.

Where the CCNCO considers that competitive neutrality arrangements are not being appropriately applied, it may make recommendations directly to the government business on the identified inadequacies and action to improve compliance. If a suitable resolution is not achieved, the CCNCO may recommend a public inquiry or that appropriate remedial action be taken by the Treasurer.

One formal complaint was received by the CCNCO for the period ending December 1998. In September 1998, airline representatives complained that the Australian Protective Service (APS) should not apply competitive neutrality policy to charges for its counter terrorist services delivered at airports. The CCNCO recommended in December 1998 that competitive neutrality should continue to apply to these services. However, it also recommended that the APS not include additional interest and tax in its service costing as these were already covered by the required pre-tax rate of return, and that the Commonwealth Treasury seek to remove scope for misinterpretation of these matters in its advice to agencies. At the time of reporting, the Minister for Financial Services was following up the CCNCO recommendations with the Attorney-General and Minister for Transport and Regional Services.

Assessment

The Council assesses the Commonwealth as meeting its second tranche competitive neutrality obligations.

New South Wales

Policy and scope of application

New South Wales requires all GBEs to implement competitive neutrality principles unless they can show through a benefit-cost analysis that this would impose a net cost on the community. The State is delivering its competitive neutrality obligations through a program of corporatisation of several non-budget sector agencies.

At 1 March 1999, New South Wales had 19 GBEs already corporatised, with several others being considered for corporatisation under the State Owned Corporations Act. These businesses operate in various sectors including electricity, finance, gaming and recreation, housing, ports and waterways, transport, water and providing miscellaneous marketing and administration services.

Corporatisation involves the application of the State Owned Corporation model and requires application of the State's Financial Policy Framework. Apart from where a net cost can be shown, non-corporatised GBEs implement competitive neutrality principles through the Financial Policy Framework. Some 45 GBEs currently fall within the Framework. This implements competitive neutrality principles through:

- the application of commercially based target rates of return, dividends and capital structures;
- regular performance monitoring;
- payment of State taxes and Commonwealth tax equivalents;

- payment of risk related borrowing fees;
- explicitly funded social programs (CSOs); and
- private sector equivalent regulation.

For other significant businesses that compete (or potentially compete) with the private sector – some 142 commercial activities of general government sector agencies, GBEs yet to adopt the Financial Planning Framework and GBEs not subject to independent prices oversight – the Treasury has developed costing and pricing principles. Broadly speaking, the objective is that entities set prices for their goods and services such that they recover full costs. The Treasury has taken action to assist the application of its pricing principles, including through issuing guidelines and conducting workshops.

Application to local government

Larger local government businesses (annual turnover of $2 million or more) must report separately from the other general business of the council and apply full cost attribution, including all competitive neutrality components. For smaller businesses, local governments are able to determine the extent of separation of the business activity and must apply full cost pricing where practicable. In all cases, subsidies to the business activity must be made transparent and there must be a system for dealing with complaints about non-implementation of competitive neutrality.

Following the Council's first tranche (June 1997) concerns about all jurisdictions' rate of progress in applying competitive neutrality principles to local government businesses, the New South Wales Government surveyed the progress of local governments within its jurisdiction in January 1998 and again in September 1998. At the time of the second survey, about 85 per cent of councils had completed the task of identifying and categorising their business activities. This categorisation showed there were 129 businesses with annual turnover exceeding $2 million and 529 smaller businesses.

The September 1998 survey also indicated a high level of compliance with the required reform program. Almost 90 per cent of the larger (category 1) businesses have separate internal reporting (the corporatisation model). There is evidence of good progress in applying taxation equivalents and debt guarantee fees, but some reluctance to require a commercial rate of return because of perceived impacts on prices. Subsidies to businesses were being made explicit in 70 per cent of cases and private sector equivalent regulation was being applied in all cases. Some 63 per cent of smaller (category 2) businesses were applying full or partial cost attribution.

Competitive neutrality complaints

New South Wales provides for an actual or potential competitor of a GBE to make a complaint if that competitor perceives it is being adversely affected by a net competitive advantage available to that GBE as a result of its public ownership. The complainant must first seek to resolve the matter with the relevant government agency. Where the complainant is not satisfied with the response of the agency, he or she may then refer the matter for independent assessment by a complaints mechanism. New South Wales has two independent mechanisms: the IPART for generic

competitive neutrality matters and the State Contracts Control Board for complaints relating to tendering.

Prior to the establishment of IPART as the mechanism for dealing with generic competitive neutrality matters, complaints were dealt with by the New South Wales Cabinet Office. During 1998, the Cabinet Office received two complaints about unfair competitive advantage due to public ownership. In each case, the initial investigation by the relevant agency found that there was no contravention of competitive neutrality principles. New South Wales reported that, to date, both complainants have not wished to refer the matters to the independent bodies.

The Cabinet Office also considered three other matters during the second tranche period. One of these matters, concerning the University of Newcastle Sports and Aquatic Centre, while not a contravention of competitive neutrality policy, did raise the question of whether universities are appropriately categorised as a government business for competitive neutrality purposes.[12] One other complaint, which concerned a commercial business operated by the Sydney Eye Hospital, was addressed by application of New South Wales pricing principles and appropriate allocation of costs to the business. New South Wales reported that full compliance with competitive neutrality pricing was achieved at the end of May 1999.

Competitive neutrality complaints about local government businesses are dealt with in the first instance by the local government business owner, with recourse to the Department of Local Government if the matter is not resolved. New South Wales reported that nearly all councils now have a formal competitive neutrality complaints handling mechanism. The New South Wales Government's latest survey of local government showed that only six of 197 councils received a competitive neutrality complaint in 1997-98 and that all of these were resolved. The Department of Local Government received six complaints directly, all of which it referred to the relevant local government for consideration and response.

Assessment

The Council assesses New South Wales as meeting its second tranche competitive neutrality obligations.

Victoria

Policy and scope of application

The Victorian Government applies the following competitive neutrality principles, where appropriate:

- corporatisation of Victorian GBEs and other significant business activities;
- commercial rate of return targets;

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[12] The application of competitive neutrality principles to the higher education sector is now being addressed by a subgroup of the COAG Committee on Regulatory Reform.

- State taxes and utility charges and Commonwealth income and wholesale sales tax equivalents;
- risk related borrowing fees; and
- relevant regulations to which the private sector is normally subject.

The Victorian Government applies a corporate business model approach and/or Tax Equivalent System (TES) model to its GBEs, covering for example, water corporations, the Transport Accident Commission, the Victorian Workcover Authority, and the Urban Land Authority. Other GBEs are to be reviewed for potential inclusion within the TES framework. Many business activities adopt a commercialised structure and full cost attribution in pricing, including competitive neutrality components.

Application to local government

Victoria reported that all local councils are applying competitively neutral pricing principles to in-house agreements entered into since July 1997. Where contracts which have been entered into prior to July 1997 are re-tendered, local governments will be required to apply competitively neutral pricing principles. Councils with significant businesses are either applying competitively neutral pricing principles or are reviewing the operation of those businesses, including to apply competitive neutrality policy.

Competitive neutrality complaints

Complaints about the business activities of the State Government and local councils are investigated by the Competitive Neutrality Complaints Unit (CNCU), within the Department of Treasury and Finance, for analysis and decision. Competitive neutrality principles now apply to all Victorian Government business activities, providing a significant role for the CNCU. Complaints about tendering procedures of local governments are handled by the Office of Local Government

Given the broad scope of application of competitive neutrality policy, the CNCU now also monitors how agencies have implemented its recommendations. Where the CNCU has found a breach of policy, it seeks information from agencies on how compliance with competitive neutrality policy has been achieved, six months after it has made its recommendation.

The CNCU also plays an active role in promoting the application of competitive neutrality policy through presentations to relevant groups and advice to government and local government agencies. The Municipal Association of Victoria and the CNCU are planning the joint development of case studies on the implementation of competitive neutrality by local governments.

The CNCU dealt with 15 cases of alleged non-compliance with competitive neutrality policy from 1 July 1997, finding a breach of competitive neutrality policy in seven cases. The Victorian Government took action to facilitate implementation of competitive neutrality consistent with the CNCU recommendation in each case.

One case likely to be relevant in other jurisdictions centred on the Department of Human Services. The complainant alleged that the Department breached competitive neutrality policy because government-owned childcare centres were eligible for higher subsidies from the Department than private providers and that some programs operated by the Department were not available to private providers. In this case, the CNCU found that, in the absence of underlying policy reasons for targeting funding arrangements under the Youth and Family Services program specifically to non-profit service providers, the Department of Human Services had breached competitive neutrality policy by not allowing existing private sector providers to apply for funding. The Department subsequently indicated that it will amend its funding policies to ensure that any legally constituted service providers can apply for funding. The CNCU also raised issues relevant to Commonwealth programs with the Commonwealth Competitive Neutrality Complaints Office.

There have been four competitive neutrality complaints concerning local governments considered by the CNCU since 1 July 1997. One complaint was upheld, with the CNCU finding that the City of Port Phillip had breached competitive neutrality policy by:

- providing financial assistance to council managed childcare centres which is not available to competing private centres; and

- not applying full cost pricing principles in setting the price of its child care services.

The CNCU is working with the City of Port Phillip to achieve compliance with competitive neutrality policy.

Another case involved the management of a gymnasium facility by the Shire of Campaspe. The CNCU found that, while competitive neutrality principles were not applied in relation to the existing management contract, there is technically no breach since the contract pre-dated the application of competitive neutrality rules to local government. The Office of Local Government and the CNCU are working with the Shire to develop options for achieving compliance with competitive neutrality policy under the current contract.

Assessment

The Council assesses Victoria as meeting its second tranche competitive neutrality obligations.

The Council gave consideration to the number of competitive neutrality complaints recorded by Victoria in assessing the State's progress and the actions taken by the Government to implement CNCU recommendations. While there have been a larger number of complaints in Victoria than in other jurisdictions, there are several explanations for this. Unlike some other jurisdictions, the complaints mechanism in Victoria applies to all government business activities. From its introduction in July 1997, the operation of the CNCU has been widely publicised. More broadly, the Government has been pursuing governance reform for a considerable period across a wide range of business activities, and it requires contestability in service provision at both State and local levels (for example, compulsory competitive tendering in local

government). The Council therefore does not consider the number of complaints to indicate poor implementation of competitive neutrality policy in Victoria.

Queensland

Policy and scope of application

Queensland's policy approach defines the application of competitive neutrality obligations to include:

- corporatised GBEs;
- commercial rates of return dividend and capital structures;
- regular performance monitoring of business activities;
- payment of state taxes and Commonwealth tax equivalents;
- payment of risk related borrowing fees;
- explicitly funded social programs (CSOs); and
- application of equivalent private sector regulation to government businesses.

Queensland's NCP annual report outlines the State's recent progress in applying competitive neutrality principles to nine candidate significant Queensland Government businesses. For several of these businesses, there has been some delay in applying reforms, despite reviews early in the life of NCP recommending commercialisation or corporatisation. This is particularly the case for the urban water authorities, where matters such as the ownership and control of assets by the State and local governments and the arrangements preferred by major consumers, have influenced approaches to commercialisation.

Queensland reported that its ability to incorporate the South East Queensland Water Board under the Corporations Law (its preferred approach), is being adversely affected by disincentives and uncertainty in the taxation environment. Queensland stated that this arises in relation to:

- section 51 AD and Division 16D of the Income Tax Assessment Act, which it claims provide a significant disincentive for State Governments converting asset-intensive entities into Commonwealth tax paying entities;
- the Deferred Company Tax proposal flagged by the Review of Business Taxation (Discussion Paper 1999), which Queensland stated could have an impact in relation to SEQWB potentially as large as Division 16D; and
- the potential income tax implications for corporatised businesses of the proposed National Taxation Equivalent Regime.

The Council has previously acknowledged local government concerns about disincentives created by the possible implications for taxation of corporatised local government businesses. The Council notes that, on this matter, the Commonwealth

has given local government a commitment that it will not be financially disadvantaged, at an aggregate level, from the corporatisation of its business activities.

The Council has also stated previously its view about the desirability of resolving business taxation arrangements as soon as possible. The proposal relating to Deferred Company Tax referred to by Queensland is at present only a possible option (one of three) identified in a Discussion Paper prepared by the Review of Business Taxation. Since releasing its Discussion Paper, the Review has taken further submissions and is due to report on 31 July 1999.

In addition to these delays, there have also been questions raised with the Council about the coverage of Queensland's competitive neutrality reform program. For example, the Child Care National Association believes that government-owned child care businesses are not competing with private providers on a competitively neutral basis. The Association is not able to have its concerns investigated by the Queensland competitive neutrality complaints handling body, the Queensland Competition Authority (QCA), because child care is not declared as a significant business activity. The Council raised this matter with Queensland earlier this year, proposing that Queensland examine the case for including childcare as a significant business activity consistent with its undertaking in the first tranche assessment in 1997 to progressively consider smaller government business activities for competitive neutrality reform.

Application to local government

The State's 17 largest local councils have assessed the net public benefit of applying one of the three identified competitive neutrality reform models – namely, corporatisation, commercialisation or full cost pricing – to their business activities. These councils identified 25 significant business activities for application of competitive neutrality.

The task of assessing whether local governments are achieving a satisfactory level of reform is delegated to the QCA. The QCA conducts an annual independent and objective assessment of local government performance in implementing CPA-style reforms. The QCA delivered its first report in November 1998. The report indicates that all councils were delivering on their promises and implementing appropriate reforms. Of the 25 businesses, 15 were commercialised and full cost pricing was applied to the remainder.

The Queensland Government stated in its annual report that it is now making concerted efforts to apply this approach to significant businesses activities in other large and small councils.

Queensland earmarks approximately one-fifth of its competition payments for local governments which implement NCP reforms. The Government's commitment is to share up to $150 million over five years, commencing on 1 July 1997. The Queensland Government provides a Financial Incentive Package which funds training for local governments and the conduct of NCP reviews by local governments, and rewards local governments which implement the full array of NCP reforms appropriate to their circumstances. The Council strongly supports the approach being taken by Queensland.

Competitive neutrality complaints

In Queensland, complaints may be raised on the grounds that a significant business is not complying with relevant competitive neutrality principles, or that arrangements in place are not effective in removing or offsetting the advantages arising from public ownership. However, unlike in some other jurisdictions, complaints cannot be lodged about businesses which the Government has not identified as subject to competitive neutrality principles.

The Government has adopted a two-stage approach to handling complaints. Initially, a complainant must raise his or her concerns with the government business that is the source of the complaint. If the two parties are unable to reach agreement, then the matter can be referred to the Queensland Competition Authority (QCA) for investigation. The QCA must decide whether the Government's competitive neutrality policies apply and, if so, recommend to Cabinet on the complaint. Complaints about local government businesses are made to the local government owner of the business, and referred to the QCA if resolution is not achieved at the local government level.

The Coachtrans complaint

Queensland reported that the only competitive neutrality complaint referred to the QCA in the period relevant to the Council's assessment was by Sita Queensland (trading as Coachtrans), the operator of a bus service between Brisbane and the Gold Coast. Coachtrans alleged that the price charged by Queensland Rail (QR) for the passenger service on the Brisbane to Gold Coast route, and certain associated procedural and regulatory processes available to QR, breached the principle of competitive neutrality.

In July 1998, the QCA found that the fares charged by QR for its Brisbane to Gold Coast services breached competitive neutrality principles. According to the QCA, the level of fares charged by QR was insufficient to recover its operating costs, an appropriate return on its own capital, and the cost of maintaining the track and associated infrastructure. The QCA found, on the other hand, that Coachtrans is in receipt of no subsidies or other assistance from the Queensland Government, and is required to meet all its costs, including a return on its own capital. The QCA also stated that "available evidence suggests that bus operators (in general) recover the capital costs of road infrastructure to government". However, the QCA found no breach in respect of the procedural or regulatory processes available to QR's Brisbane to Gold Coast services (QCA 1998).

The QCA recommended that the Queensland Government develop a CSO framework for the Brisbane to Gold Coast public transport service which complies with the principle of competitive neutrality, achieves efficient resource allocation in the public transport market in South-East Queensland and promotes competition. The QCA also recommended that, until a CSO framework is in place, the Queensland Government should, within six months of the release of its report, ensure that passengers currently travelling by bus retain access to those or equivalent public transport services.

On the 6 August 1998, the Queensland Premier and Treasurer gave notice that they:

- rejected the QCA finding that there was a breach of competitive neutrality policy in relation to QR's fares on the Brisbane to Gold Coast route, reasoning that the information available was not sufficiently conclusive to support the QCA's decision; and

- accepted the QCA finding that QR has no procedural or regulatory advantages which breach competitive neutrality principles.

The Ministers advised that they had requested the Department of Transport to develop a CSO framework for the Brisbane-Gold Coast service that takes account of competitive neutrality principles.

Subsequently Coachtrans commenced two actions – a case under section 46 of the Trade Practices Act (Federal Court) and a judicial review action in relation to the decision by the Ministers to reject the QCA finding (Supreme Court of Queensland). The section 46 matter was listed for hearing in June 1999 and the judicial review set down for August 1999.

The Ministers' decision notice did not provide the reasoning supporting their decision to reject the QCA recommendation. Neither does the Queensland NCP annual report address the matter, stating that no comment is made pending the decision of the Supreme Court.

The Council's views

The Council considers that the efficacy of each government's complaint handling, including its response to the recommendations of its complaints mechanism, is an important indicator of whether competitive neutrality principles are being appropriately applied. To be assessed as complying with NCP obligations, the Council expects governments to implement the recommendations of competitive neutrality complaints mechanisms unless the government can provide a justification for acting differently. As a general rule, however, the Council expects relevant government businesses to have presented their case during the investigation of the complaint. In view of this, the Council considers that a government would need to provide a rigorous justification for departing from the recommended course of action if it is to be considered as complying with competitive neutrality obligations.

As with government decisions in other areas, a government's rejection of the recommendations of its competitive neutrality complaints mechanism can be tested, such as Sita Queensland has chosen to do, by seeking judicial review of the decision. While a judicial review will generally examine the soundness of the government decision making process, rather than the merits of the decision, it does involve similar considerations to the Council's assessment of a government's compliance.

Given that the judicial review action by Sita Queensland is still underway, the Council finds it inappropriate to conclude its assessment of the Queensland Government's compliance with competitive neutrality principles at this time.

Assessment

The Council considers that the matter of the judicial review of the decision by the Ministers to reject the QCA finding of the competitive neutrality breach complaint is relevant to its second tranche assessment of Queensland's competitive neutrality compliance. Because of this, the Council proposes to conduct a supplementary assessment of Queensland's competitive neutrality performance. The supplementary assessment would consider the Queensland Government's approach on the QR matter after the outcome of the Sita Queensland Supreme Court action is known and, to the extent necessary, the Government has had time to consider the outcome. As part of this assessment, the Council would take account of the progress achieved by Queensland towards developing a public transport framework for South-East Queensland consistent with the QCA recommendation.

As well as this, the Council sees some value in Queensland examining whether there is benefit in extending the application of its competitive neutrality policy beyond the significant business activities so far nominated. Any such action would need to involve extending the mandate of the QCA to investigate competitive neutrality complaints, for example, to enable the QCA to recommend to the Government on whether it is appropriate to apply competitive neutrality principles to businesses where they currently do not apply. Consideration of this matter by Queensland would be consistent with the Government's assurance to the Council during the first tranche assessment in 1997 that its intention is to progressively consider smaller business activities for application of competitive neutrality principles.

Western Australia

Policy and scope of application

Western Australia has taken a number of steps to apply competitive neutrality principles to its significant business activities. These include:

- corporatisation of Western Power, AlintaGas and the Water Corporation, which collectively earn 80 per cent of all revenues derived by government businesses in the State, and the application of the competitive neutrality principles in accordance with the CPA;

- commercialisation of the State's port authorities and application of competitive neutrality principles;

- commercialisation of the Western Australian Land Corporation (Landcorp), relocation of Landcorp's regulatory and policy functions, application of competitive neutrality principles including independent and transparently provided CSOs, and independent performance monitoring; and

- commercialisation of the Western Australian Treasury Corporation and application of competitive neutrality components including a required return on capital through a dividend payment to the Consolidated Fund.

Western Australia has a number of competitive neutrality reviews of medium and small sized government agencies currently underway.

Application to local government

Western Australia categorises its local governments as category 1 (with annual revenue exceeding $2 million) and category 2. There are 54 category 1 councils and around 90 category 2 councils. Significant local government businesses (annual turnover exceeding $200 000) are most likely to be operated by category 1 councils.

Western Australia has required all local governments to review their significant business to determine whether these businesses warrant competitive neutrality reform. The Government reported that, at 31 March 1999, 136 local governments had fully met their commitment to examine their business operations. While the majority of businesses fall under the threshold for significance, a total of 129 businesses have now been reviewed, with competitive neutrality principles now implemented in about half of these.

Competitive neutrality is applied most commonly through full cost pricing, although some businesses have also been established as commercialised business units. Similarly to Queensland, Western Australia devotes a proportion of its NCP competition payments to local governments which achieve their obligations under NCP.

Competitive neutrality complaints

Western Australia's Cabinet Government Management Standing Committee (GMC), comprising senior Ministers of the Western Australian Government, supported by a Complaints Secretariat within the Western Australian Treasury, handles allegations of non-compliance with competitive neutrality policy. Complaints may be made by individuals, businesses and industry groups in the private sector and government agencies of other jurisdictions (which are already subject to competitive neutrality) who:

- are, or may be, directly and adversely affected by the competitive advantage alleged to be enjoyed by the Western Australian Government agency carrying out the significant business activity; and

- compete or seek to compete in a particular market with a Western Australian Government agency, but are prevented from doing so by the competitive advantage alleged to be enjoyed by that agency.

Initially, complainants make contact with the relevant government business to attempt to resolve the allegation of non-compliance. If the complainant is unable to resolve their concern, they can lodge a written complaint with the Complaints Secretariat. The Complaints Secretariat then investigates the complaint to determine that it is a competitive neutrality matter, and where this is the case, makes recommendations for consideration by the GMC.

Where the GMC finds a breach of competitive neutrality, it determines the action necessary to rectify the problem on a case by case basis taking account of the seriousness and nature of non-compliance. Once the actions necessary to rectify a competitive neutrality problem are decided, implementation is monitored by the Treasury. There is no avenue for appeal against a finding by the GMC that there is no breach of competitive neutrality policy.

The Complaints Secretariat has received one complaint since the establishment of the formal GMC mechanism in October 1998, which it decided fell outside the scope of competitive neutrality policy.

Assessment

The Council assesses Western Australia as meeting its second tranche competitive neutrality obligations.

South Australia

Policy and scope of application

After some early delays, South Australia is progressively applying competitive neutrality principles to the Government's significant business activities, to the extent that the benefits outweigh the costs. As set out in its June 1996 policy statement, this includes corporatisation, tax equivalent payments, debt guarantee fees and private sector equivalent regulation. Where corporatisation is found not to be appropriate, prices must reflect full cost attribution. The State gazetted some 30 larger government businesses[13] for competitive neutrality and, following some delays, on 13 May 1999 gazetted a list of smaller businesses. South Australia's timetable should see competitive neutrality principles applied to smaller government businesses by June 2000 at the latest.

South Australia has reviewed its Competitive Neutrality Policy Statement and the relevant sections of the *Government Business Enterprises (Competition) Act 1996* (the GBE Act), with the objective of clarifying the scope of application of competitive neutrality policy and revising the implementation timetable. The revised policy statement and amendments to the Act are expected to be put in place during 1999.

Application to local government

Competitive neutrality continues to be extended to local government business activities. All councils determined by 30 June 1998 which competitive neutrality instruments were to be applied to their business activities. Councils identified both large and small businesses, although most are small scale activities. Implementation for the smaller local government businesses will be completed by June 2000.

Councils are reviewing by-laws and the South Australian Government is reviewing the Local Government Act including for conformity with competitive neutrality requirements.

Competitive neutrality complaints

Under GBE Act, the Competition Commissioner investigates complaints that government businesses are infringing competitive neutrality principles. According to

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[13] That is, those government businesses with revenue greater than $2 million or assets valued at greater than $20 million.

the Government the Act allows complaints from a competitor or potential competitor of a government or local government agency that:

- an activity has not been identified as a "significant government business activity";
- the most appropriate competitive neutrality measure (corporatisation, commercialisation, or cost reflective pricing) has not been chosen for the activity;
- the chosen competitive neutrality measure has not been properly or fully implemented, or that there has been a breach of a provision that has purportedly been implemented; and/or
- a time-line set out in the South Australian Government Policy Statement has not been met.

South Australia handles complaints in two stages. First, the complaint is referred to the State agency or local government business owner for initial response. If the complaint is not resolved, then the matter can be referred to the Competition Commissioner, who undertakes an investigation and recommends to Cabinet as appropriate.

The Commissioner had three incomplete complaints investigations at the beginning of 1998. During the year, the Commissioner received a further five complaints and finalised three. One of these, relating to the Cleland Wildlife Park, was upheld after a 13 month investigation. In this case, the Commissioner recommended that the Department for Environment, Heritage and Aboriginal Affairs conduct an analysis of the application of competitive neutrality principles to the Park. The South Australian Government accepted this recommendation, and the Department undertook to conduct the recommended analysis within twelve months.

Another of the investigations completed during 1998 concerned the distribution by the Department of Human Services of a funded energy rebate to pensioners via ETSA Power, a government-owned electricity retailer. A private gas distributor, Envestra, complained that distributing the rebate via ETSA Power was anti-competitive. In this case, the secretariat to the Competition Commissioner terminated this complaint following Crown Law advice that the complaint was *ultra vires* the GBE Act, i.e. outside the scope of the Act. The principal reasons given for this were that:

- the rebate was the initiated by the Department of Human Services which is not engaged in a significant business activity;
- the decision to pay a rebate and distribute it in the manner chosen are matters of government policy – complaints against government policy cannot be brought under the GBE Act; and
- in distributing the rebate ETSA Power was fulfilling a community service obligation – these are not subject to competitive neutrality (South Australian Government 1999).

Assessment

South Australia has made recent advances in delivering its competitive neutrality policy obligations, although there is still some way to go in relation to smaller State Government businesses and local government. That said, the Council acknowledges that there are unlikely to be a large number of local government businesses in South Australia which are significant for competitive neutrality purposes.

The Council has considered two matters arising from South Australia's handling of competitive neutrality complaints. In the case of the Cleland Wildlife Park, the Competition Commissioner upheld the complaint and the Government accepted the recommendation. Although the investigation took some thirteen months, the Council was assured that this did not impose an unnecessary economic burden on the complainant and was necessary to allow the investigation to take a fully consultative approach acceptable to all parties to the complaint.

In the case of the complaint concerning ETSA Power and the energy rebate, the Council was concerned that the stated reasons for terminating this complaint (see above) appeared inconsistent with the Government's own statement of policy. In particular they left considerable uncertainty as to scope of applied competitive neutrality policy in South Australia and, especially, the degree to which CSO activities are subject to competitive neutrality principles.

The Council would be concerned if, as could be implied by the stated reasons, merely by labelling measures "government policy" or "community service obligations", they were made exempt from competitive neutrality complaints. These concepts are potentially so broad as to severely undermine the value of competitive neutrality policy. The Council has addressed these matters with the South Australian Government, which has clarified its basis for the termination and confirmed the continued application of the requirements of its CSO Policy Framework of December 1996 that "undertaking of CSO activities does not conflict with Competitive Neutrality principles". The Council is therefore satisfied that in this case the Government's competitive neutrality obligations have been appropriately fulfilled.

Tasmania

Policy and scope of application

Tasmania's *Government Business Enterprises Act 1995* places GBEs on a more competitive footing. As umbrella legislation overarching the portfolio Act establishing each GBE (for example, the Hydro-Electric Corporation Act 1995), the GBE Act has provided the framework for improvement in the efficiency, effectiveness and accountability of the State's GBEs and is consistent with the principles underpinning corporatisation. Since July 1997, all GBEs except the Port Arthur Historic Site Management Authority have been subject to full competitive neutrality arrangements by way of:

- tax equivalent regimes;
- debt guarantee fees;
- dividend requirements; and

- all regulations normally applying to the private sector.

Tasmania is currently considering its approach to the Port Arthur Historic Site Management Authority. The Government has released a public discussion paper on the future of Port Arthur. The Government's NCP annual report stated that it will take the outcome of this process into account in its future plans for the Management Authority.

Tasmania identified all significant business activities operated by budget sector agencies in June 1997. Competitive neutrality arrangements are being applied in these business activities, with progress reported to the Tasmanian Treasury every six months. Many government services are now outsourced to private sector providers. Where government services continue to be provided by government business activities, in most cases, fees are set on a full cost attribution basis.

Tasmania has a CSO policy designed to ensure that delivery of the Government's social and other objectives does not impact on the commercial performance of its GBEs. Consistent with the approach set out in section B3.2 above, Tasmania requires that CSOs be clearly identified through a directive from the Government, justified and separately accounted for. The Government has negotiated contracts for the provision of agreed CSOs with the Hydro-Electric Corporation, Metro Tasmania, the Public Trustee and Aurora Energy.

Application to local government

The Council's supplementary first tranche assessment noted that Tasmania's application of competitive neutrality principles to local government businesses had been delayed pending finalisation of a program of local government amalgamations then underway. At the time, the Tasmanian Government gave an undertaking to negotiate with local governments to reinvigorate the application of NCP within the local government sector.

Tasmania has now renegotiated a new timetable for competitive neutrality application. The timetable provided for full cost attribution for all significant business activities by no later than 1 January 1999 and a process of public benefit assessments to determine whether local government trading enterprises should be corporatised. That process should see businesses corporatised, where assessments show this to be appropriate, by July 2000 at the latest.

Competitive neutrality complaints

Tasmania established an independent competitive neutrality complaints handling mechanism within the Government Prices Oversight Commission (GPOC) through the *Government Prices Oversight Amendment Act 1997* and *Government Prices Oversight Regulations 1998.* Prior to the formal commencement of the GPOC mechanism, an interim mechanism operated within the Department of Treasury and Finance.

Under the GPOC mechanism, an individual may lodge a complaint against a State Government and local government business activities, having first attempted to resolve the complaint with the relevant entity. A desirable feature of the GPOC

process is that a competitive neutrality complaint may be lodged about any government business activity. Tasmania has now widely publicised its complaints handling process.

There have been no formal competitive neutrality complaints in Tasmania as at March 1999. While the State's interim complaints mechanism received three informal complaints in late 1997 and passed these to GPOC for action, in each case the complainant chose not to proceed.

Assessment

The Council assesses Tasmania as meeting its second tranche competitive neutrality obligations. The Council will continue to monitor progress with the implementation of competitive neutrality arrangements at local government level.

Australian Capital Territory

Policy and scope of application

The ACT has implemented competitive neutrality arrangements within its significant business activities, including:

- taxation equivalents and Territory taxes and charges are payable by government owned corporations and many larger authorities, and are progressively being applied on a wider basis, including to small business activities embedded within public agencies; and
- debt guarantee fees are imposed on government businesses, using a credit rating system to distinguish between the risk classes of different public enterprises;
- competitive tendering processes are increasingly used by the Government for publicly provided services to test the cost effectiveness of existing service arrangements and to establish benchmark costings for services.

Competitive neutrality complaints

The ACT Government has established a mechanism for investigating and recommending on competitive neutrality complaints – the Competitive Neutrality Complaints Unit (CNCU) – within the Chief Minister's Department. The CNCU is able to investigate complaints only about businesses that have been formally exposed to competitive neutrality principles.

The CNCU received one complaint during the second tranche assessment period, relating to the provision of long day childcare. This matter is currently under consideration by the ACT complaints body and is not relevant to this assessment of progress.

In assessing second tranche progress, the Council also took account of developments relating to an earlier complaint raised with the CNCU following the ACT Government's announcement that it would fund an aquatic centre with an indoor 50 metre pool and associated facilities in the Belconnen area. The owners of two privately owned swimming facilities in Belconnen were concerned that, while the new

business would be competing with them for the same customers, the new pool would have the benefit of a public subsidy.

The CNCU's investigation in 1997 found that the proposed facility would be in direct competition with the existing pool complexes. It recommended that the ACT Government conduct a public benefit test to assess whether the benefits to the community of the proposed development would outweigh the costs. Following this recommendation, the ACT Government commissioned the Allen Consulting Group (Allen Group) to examine the proposal's net community benefit.

The Allen Group concluded that only the Government could determine the net benefit, if any, because the benefits were largely intangible and some of the costs (and therefore the size of any public subsidy) were dependent on subsidy and pool design choices. It did, however, recommend that to minimise the costs:

- any subsidy be applied on a per-swimmer basis and only for services not commercially available elsewhere in Belconnen;
- that the Government could incorporate "*social objectives such as low entry fees for different categories of user (unemployed people, pensioners, students, etc) …in a subsidy program*"; and
- that both the building and the business of operating the pool be competitively tendered (Allen Consulting Group 1999).

Subsequently the ACT Government has decided there is a net public benefit in proceeding with the aquatic facility in Belconnen. It has placed certain limits on the maximum permissible capital subsidy for the proposed building and instituted a tendering process which is underway at the time of reporting.

Assessment

The Council assesses the ACT as meeting its second tranche competitive neutrality obligations.

The Belconnen Pool complaint illustrates how the provision of services consistent with community objectives can sometimes introduce tensions with policies aimed at achieving benefits through competition. These tensions can be reduced if governments ensure community services are clearly defined, well justified, and delivered effectively.

The Council considers that the ACT Government has pursued this complaint appropriately. The Allen Group recommendations appear to provide a sound approach to maximising the community benefits while minimising the costs, including the potential for harm to competing private pool owners. This goal may be further promoted by adoption of the Allen Group's suggestion that the subsidy be targeted to particular classes of users who may not otherwise be able to afford to pay market prices for entry. For competitive neutrality compliance, prices charged for pool entry, together with any subsidy, should cover the cost of providing the service.

Given that the competitive neutrality complaints process can be a useful tool for monitoring the potential for extending reform, the Council suggests that the ACT's mechanism allow for investigation of complaints that a business has not been exposed to competitive neutrality principles. This would enable the CNCU to consider whether it is appropriate to apply competitive neutrality reforms to businesses where they currently do not apply.

Northern Territory

Policy and scope of application

The Northern Territory has instituted appropriate competitive neutrality policies that achieve allocative efficiency, effective resource use and transparency.[14] This involves:

- all 11 Government Business Divisions (GBDs) paying tax equivalents and debt costs;
- facilitating the efficient use of resources by having GBDs pay the cost of all resources used in service provision and ensuring prices of goods and services fully reflect costs;
- identifying and costing CSOs;
- reviewing capital structure and dividend policies of GBDs against private sector benchmarks; and
- performance monitoring of all GBDs, involving reporting annually on relevant economic, financial and non-financial performance indicators, as well as analysing and interpreting these indicators.

The Territory Insurance Office, a government owned statutory corporation supplying insurance and financial services, is corporatised and subject to competitive neutrality policy. In addition, the Government is establishing Territory Discoveries, a tourism wholesaling operation established by the Northern Territory Tourist Commission, as a GDB subject to competitive neutrality policy. The Government accepts that Territory Discoveries is a significant business operating in competition with private sector providers.

Competitive neutrality complaints

The Northern Territory Treasury handles all complaints regarding breaches of competitive neutrality policy. Complaints can be made that significant business activities are not applying relevant principles or that the principles being applied are not effective.

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[14] The Council accepts that local government businesses in the Northern Territory are unlikely to be significant for purposes of competitive neutrality policy.

The Treasury has received one complaint. On 22 March 1999, it received a complaint from the Australian Council of Tour Wholesalers relating to Territory Discoveries. At the time of the Northern Territory's annual report, the Treasury was investigating this complaint.

Assessment

The Council assesses the Northern Territory as meeting its second tranche competitive neutrality obligations.

Given that the competitive neutrality complaints process can be a useful tool for monitoring the potential for extending reform, the Council suggests that the Northern Territory's mechanism allow for investigation of complaints that a business has not been exposed to competitive neutrality principles. This would enable the Treasury to consider whether it is appropriate to apply competitive neutrality reforms to businesses where they currently do not apply.

B4 Structural Reform of Public Monopolies

B4.1 The structural reform commitment

Historically some government businesses have enjoyed protection from competition, and consequently, structures have developed that do not readily respond to market conditions. In these cases, if measures to introduce competition are to be successful, structural reform may be needed first.

Structural reform involves removing any regulatory responsibilities from the monopoly business so that the business has no regulatory advantage over rivals and potential entrants. Structural reform may also involve splitting any monopoly elements of the business from potentially competitive elements, in order to avoid the risk of unfair competition via cross-subsidisation from monopoly activities.

Structural reform is particularly important where a public monopoly is to be privatised. Privatisation without appropriate reform risks allowing the monopoly increased scope to abuse its position, to the detriment of consumers and potential competitors.

Under NCP, governments agreed to apply certain procedures to systematically consider business structure issues prior to introducing competition into markets served by public monopolies or privatising their businesses. However, these principles do not require privatisation or the introduction of competition. Clause 4 of the CPA obliges governments to relocate regulatory functions away from the public monopoly before introducing competition into the market served by the monopoly. Also under clause 4, before introducing competition into a sector traditionally supplied by a public monopoly or privatising a public monopoly, governments agreed to review:

- the appropriate commercial objectives of the public monopoly;
- the merits of separating potentially competitive elements of the public monopoly from the natural monopoly elements;
- the merits of separating potentially competitive elements into independent competing businesses;
- the best way of separating regulatory functions from the monopoly's commercial functions;
- the most effective way of implementing competitive neutrality;
- the merits of any community service obligations (CSOs) provided by the public monopoly, and the best means of funding and delivering any mandated CSOs;
- the price and service regulations to be applied to the relevant industry; and
- the appropriate financial relationship between the owner of the public monopoly and the public monopoly.

B4.2 Structural reform activity by jurisdiction

Governments have undertaken a range of structural reforms in the period leading up to the second tranche assessment. Several of these were associated with other elements of the NCP program, particularly related reforms of the electricity, water and gas industries. Structural reform activity in these sectors is discussed in the sections of this report dealing with electricity, gas and water reforms.

This section discusses other structural reform activity relevant to the assessment of jurisdictions' performance against clause 4.

Telstra

The partial privatisation of Telstra in 1997 gave rise to an obligation on the Commonwealth Government to examine the merits of structurally separating the monopoly elements from the non-monopoly elements of Telstra's business. In its first tranche assessment the Council reported the Commonwealth's view that it had broadly satisfied its clause 4 obligations through a series of related reviews prior to the partial privatisation and through more general GBE governance and competitive neutrality processes. The reviews led to a decision not to pursue structural separation but to supplement general prohibitions against anti-competitive conduct (Part XIB of the TPA) and to facilitate access to services through an industry-specific regime (Part XIC of the TPA).

More latterly, the Commonwealth has passed amendments to Part XIB of the TPA that will enhance the ACCC's ability to issue competition notices in relation to anti-competitive conduct and to arbitrate access disputes. These amendments also enable the ACCC to disclose information kept by carriers pursuant to 'accounting separation' record-keeping rules which will assist access seekers in negotiations with access providers.

In preparation for the second tranche assessment the Council commissioned Tasman Asia Pacific (TAP) to assess the ACCC's proposed record-keeping rules and the Commonwealth Government's proposed arrangements for accounting separation of the local fixed network. In addition, TAP was asked to assess the likelihood that the new record-keeping rules will work effectively to facilitate competition in the telecommunications industry.

TAP concluded that the proposed new record-keeping rules are an improvement on their predecessors and will provide the ACCC with the information necessary to detect anti-competitive behaviour. TAP also found that the recent legislative amendments are potentially positive steps towards a ring-fencing model. However, TAP did not consider these arrangements, nor ring-fencing per se, would be adequate to remove Telstra's sources of market power and to combat anti-competitive behaviour. TAP suggested separating the Customer Access Network (CAN), being the natural monopoly element, from transmission facilities and operating the CAN independently under supervision by the ACCC or another regulatory authority.

The Council invited comment from the Commonwealth Government on the TAP advice. The Commonwealth considered the analysis insufficient to show that the current regulatory regime had failed to promote competition. It noted that the ACCC is at a critical stage in the development of the regulatory regime, with the declaration

of local call services likely, and that it is too early to say whether or not the regime has worked. The Commonwealth also considered that the TAP report contained insufficient analysis of the nature, extent and effect of economies of scale and/or scope in CAN services, and inadequate substantiation of the costs and benefits of structural separation.

The Commonwealth noted that a statutory review of Part XIB of the TPA is scheduled for 2000, and this will allow for a thorough assessment of the telecommunications regime, including the effectiveness of current accounting separation arrangements.

The Council agrees that the legislative amendments just passed, and the regulatory development being undertaken by the ACCC, go some way towards satisfying the Commonwealth Government's CPA clause 4 obligations arising from the partial privatisation of Telstra. To test whether these obligations have been fully satisfied, the Council will be looking for the statutory review of Part XIB in 2000 to examine the costs and benefits of alternatives to the current regime, including structural separation of the local fixed network from non-monopoly elements. As suggested by the Commonwealth, such an examination would require thorough analysis of the nature, extent and effect of any economies of scale and scope in the telecommunications industry, including the CAN. Such analysis goes to the heart of the purpose of the obligations created by clause 4 of the CPA. The Council is not aware of any comprehensive Commonwealth analysis of this issue. The Council will consider further progress made by the Commonwealth on this matter in its third tranche assessment.

Sydney Basin airports

In its first tranche assessment, the Council raised the issue of the Commonwealth's failure to conduct a clause 4 review prior to the sale of the long-term leases operated by the Federal Airports Corporation (FAC).

The Council recognised at that time that arrangements already in place or being contemplated by the Commonwealth, might encompass many of the questions of structure which would be addressed in a clause 4 review of the FAC.

In September 1998, the FAC was abolished and the Commonwealth's remaining airport holdings were leased to newly created Commonwealth-owned companies. The Sydney Airport Corporation Limited (SACL) managed the Sydney Basin airports, Sydney (Kingsford Smith), Bankstown, Camden and Hoxton Park. In addition, Essendon Airport was created as a subsidiary company of SACL.

The SACL airports are regulated under the *Airports Act 1997*. This removes the responsibilities from the lessees for the regulation of land use and environmental planning and control, commercial and retail trading and liquor licensing. In relation to on-airport activities, including commercial and retail trading and liquor licensing, the approach has been to subject airport lessees to State regulations.

The Commonwealth has put in place arrangements aimed at encouraging competition between airports. The *Airports Act 1996* prohibits airlines from owning more than 5 per cent of an airport operator company, and imposes cross ownership restrictions of

15 per cent between the Sydney airports (Kingsford Smith and Sydney West) and Melbourne, Brisbane and Perth airports.

An economic and regulatory regime has also been established, administered by the ACCC. The prices oversight scheme provides for a CPI-X cap on defined aeronautical services. There is also price monitoring of aeronautical-related services outside the price cap. The SACL airports are currently not subject to section 192 of the *Airports Act 1996*, which provides for declaration of airport services. However, they are subject to Part IIIA of the *Trade Practices Act 1974*, which allows access seekers to apply for declaration.

Assessment

The outstanding issue for a clause 4 review is the determination of the appropriate structure for the Sydney Basin airports, including the proposed second airport, prior to privatisation. The Commonwealth has given an undertaking that its future processes will consider structure and competition issues for Kingsford Smith and the proposed second international airport, although there is currently no timeframe for these questions to be considered.

The Council is satisfied that, to date, the Commonwealth has introduced an industry structure and regulatory framework that is appropriate in terms of the issues raised by clause 4.

TasRail

In November 1997, the Commonwealth Government sold the Tasmanian rail services (TasRail) to Australian Transport Network (ATN). This included both track and above rail facilities. TasRail did not conduct any passenger services. The Commonwealth originally acquired TasRail as part of its buyout of state railways.

The Commonwealth has advised that it did not conduct a formal clause 4 review prior to the sale of TasRail. It is currently examining the extent to which the issues raised by clause 4 have been otherwise considered and whether the intent of clause 4 has been fulfilled.

Assessment

The Council considers that, as a review was not conducted, the Commonwealth has not met its clause 4 obligations in respect of TasRail.

Australian National

Australian National, a Commonwealth Government enterprise, operated above and below rail businesses in South Australia. The Commonwealth separated these businesses and sold them off over the period 1993-1998.

- Australia Southern Railroad leased the track corridor used to provide intrastate freight services (no passenger) for 50 years and bought the corresponding above and below rail assets. Access arrangements were established by the South Australian Government through the *Railways (Operations and Access) Act 1997*.

- Great Southern Railway bought the above rail infrastructure used to provide interstate passenger services. The track for these interstate services was transferred to Australian Rail Track Corporation (ARTC) which is currently developing an access regime to cover all track that forms the 'national interstate track system'.

The Commonwealth has advised the Council that a formal clause 4 review wasn't undertaken prior to the sale of Australian National.

Assessment

Given that a review has not been conducted, the Council is of the view that the Commonwealth has not met its clause 4 obligations in respect of Australian National.

Australian Wheat Board

In December 1997 and July 1998, the Commonwealth Government legislated to privatise the Australian Wheat Board (AWB) into a grower owned and controlled company (the AWB Ltd) as of July 1999. The legislation extends the existing wheat export monopoly indefinitely and vests its management in a new statutory body, the Wheat Export Authority (WEA). It confers an exclusive export (monopoly) right on AWB Ltd for five years.

The privatisation of the AWB and the extension of its export monopoly have implications for both the Commonwealth's clause 4 and clause 5 obligations. Clause 4 obliges the Commonwealth to review the structure and commercial objectives of the AWB prior to privatisation.

The primary functions of the WEA will be to manage and approve requests to export wheat from organisations other than the AWB Ltd and to monitor the use of the monopoly by the AWB Ltd.

The WEA will comprise three members – a Chairperson, an industry representative and a government representative. It will be funded for the first five years from AWB reserves not transferred to the AWB Ltd.

In considering requests by third parties to export wheat, the WEA must consult with AWB Ltd, and can only approve bulk wheat exports where AWB Ltd has approved the export. The WEA will be required to develop guidelines, in consultation with AWB Ltd, for assessing export applications. The Explanatory Memorandum to the *Wheat Marketing Legislation Amendment Act 1998* suggests that these guidelines could reflect the current AWB discretion to grant consent for non-bulk exports, that is, niche and speciality wheat and wheat exported in bags or containers. In the Explanatory Memorandum, the Commonwealth Government recognised that AWB Ltd will have a 'considerable degree of market power' with respect to exports and has exempted the AWB Ltd's export activities from the *Trade Practices Act 1974* under section 51(1).

The WEA must report to the Grains Council of Australia (a wheat growers industry body, formerly the Australian Wheatgrowers' Federation) on its activities at least twice annually.

In the year 2004, the Commonwealth will conduct a review to examine the WEA's management of the export monopoly and the use and appropriateness of the AWB Ltd's monopoly export right.

The Commonwealth has stated that statutory and commercial arrangements for the wheat export market will be clearly separated. However, the legislative inter-relationships between the WEA and AWB Ltd, in particular AWB Ltd's effective veto power over WEA decisions on export requests by third parties, raise significant questions about the effectiveness of separation in practice.

Assessment

There is some doubt as to whether the Commonwealth has so far considered structural matters relating to the privatisation of the AWB through a clause 4 process.

A clause 4 review would need to consider:

- the appropriateness of granting a five year exclusive export monopoly right to a private company;
- reforms made or impending in related grain industries, and whether reformed former monopoly marketing businesses (such as ABB Grain Ltd) and other market participants are at risk of unfair competition by virtue of the wheat export monopoly;[15]
- the appropriateness of the WEA structure; and
- the effectiveness of structural separation of regulatory and commercial functions, with particular attention to:
  - the appropriateness of the inter-relationships between the statutory body and the private company;
  - the potential for conflicts of interest to emerge between the WEA and the AWB Ltd; and
  - the potential for regulatory capture.

On this basis, the Council does not consider that the Commonwealth has met its clause 4 obligations with respect to the privatisation of the AWB. The Council expects that these issues will be considered as part of the clause 5 review of the AWB legislation.

TABs

During the second tranche assessment period, several governments have moved towards privatisation of their Totalisator Agency Boards. For example:

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[15] See below a description and assessment of the reforms by Victoria and South Australia to the Australian Barley Board.

- New South Wales has privatised its TAB;
- Queensland is currently debating the sale of its TAB; and
- the ACT has undertaken a scoping study for the possible privatisation of the ACTTAB.

This privatisation activity might appear to raise obligations under clause 4, to the extent that TABs operate as public monopolies. However, TABs face competition from a range of providers of gambling services, including other jurisdictions' TABs. While this competition does not take exactly the same form, for example, other jurisdictions' TABs are accessible by telephone rather than through a physical presence, the Council accepts that each jurisdiction's TAB is not a monopoly provider of gambling services. Clause 4 is therefore not relevant.

There are some remaining competition questions, however, relating to regulatory neutrality. The New South Wales TAB, which was privatised under legislation passed in December 1997, has a 15-year exclusive licence to provide a Centralised Monitoring System (CMS) for all gaming machines operated by registered clubs and hotels throughout New South Wales. Subsequent legislation (May 1998) granted the New South Wales TAB an exclusive 15-year licence to enter into agreements with clubs and hotels to install and run gaming machines on their premises and share in the profits derived from their operation.

The role of the CMS is to collect data on gaming machine operations throughout New South Wales. In part, these data are used to assist calculation of taxation obligations arising from the operation of gaming machines – previously, inaccurate assessment of gaming machine turnover had resulted in losses of taxation revenue to the State). However, the regulatory role of the CMS has possible implications for competition – particularly in relation to the access the TAB might have to information on machines operated by its competitors.

As discussed in the section of this report dealing with the NCP legislation review program, the Council will consider progress in relation to legislative restrictions on gambling activity in its third tranche assessment, following the Productivity Commission review of the economic and social impacts of gambling currently underway. The Council will take account of any implications for competition flowing from relevant matters, including the regulatory role of the New South Wales TAB, as part of this assessment.

Australian Barley Board

In 1997, the Victorian and South Australian Governments' commissioned a joint review of their *Barley Marketing Acts 1993*. The review recommended deregulation of domestic and export barley marketing arrangements in both States.[16]

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[16] See Section B5 for a discussion of relevant legislation review matters.

As part of their barley market reforms, the States decided to privatise the Australian Barley Board (ABB), a statutory body established under the Barley Acts with the power to compulsorily acquire and market the barley crop in both States, by mid-1999. The two governments established a government/industry Restructuring Committee to work through the issues associated with privatisation. The Committee's privatisation recommendations included:

- the establishment of a grower owned and controlled company to succeed the ABB (ABB Grain Ltd) to conduct domestic barley trading;
- the establishment of a wholly-owned subsidiary of ABB Grain Ltd (ABB Grain Export Ltd) to receive existing stocks of pooled barely and to have statutory marketing powers over bulk barley exports until mid-2001; and
- trading rules for both companies to ensure all grain sales and grain swaps are transparent and auditable (Parliament of South Australia 1999).

Victoria enacted legislation to give effect to these arrangements in April 1999. South Australia passed mirror legislation in May 1999.

Assessment

In general, the Council does not support the granting of statutory marketing powers to private companies. However, with respect to ABB Grain Export Ltd, the Council acknowledges:

- the relatively short period of time until the export barley market is opened to competition (that is, mid-2001); and
- the structures designed to ensure transparency in the dealings between the domestic and export operations of the companies until the export market is opened to competition in order to minimise the risk of domestic market distortions.

Therefore, the Council considers the Victorian and South Australian Governments have met their clause 4 obligations with respect to the ABB.

Victorian public transport system

The Victorian public transport system has been subject to considerable structural reform.

Until 1993, the Public Transport Corporation (PTC) provided a significant part of Melbourne's public route bus transport services. In December 1993, the National Bus Company assumed responsibility for about 75 per cent of the service previously provided by the PTC. In April 1998, the Melbourne Bus Link Company assumed responsibility for the balance of the services provided by the PTC.

In 1997, the Government commissioned a major review of the structural reform options for the metropolitan tram and train networks. The review examined matters covered by clause 4 of the CPA and made recommendations that were subsequently adopted by the Government.

The Government has adopted a two-stage approach to structural reform of the public sector train, tram and rail freight businesses.

- From 1 July 1998, five separate corporations were created under the Rail Corporations Act to provide metropolitan train and tram services and country rail passenger services (Bayside Trains, Hillside Trains, Swanston Trams, Yarra Trams, V/Line Passenger). The PTC remains as a statutory corporation with a limited life to manage residual non-operational functions and to provide certain integration services for the new operating corporations.

- The Transport Reform Unit of the Department of Treasury and Finance has almost completed a process of franchising the five businesses to the private sector.

A Public Transport Division within the Department of Infrastructure has been established to manage all contractual arrangements with public transport service providers.

Guarantees of third party access to infrastructure have been established in the privatisation arrangements.

Public transport industry regulation is fully separated from service provision. A separate Public Transport Safety Directorate has been established within the Department of Infrastructure to regulate safety across all the public transport modes.

Assessment

The Council is satisfied that Victoria has met its clause 4 obligations in respect of the introduction of increased competition and privatisation of the public transport system.

V/Line Freight

The V/Line freight business has been sold with a long-term lease over the country rail infrastructure. Operational control and maintenance responsibilities for the leased infrastructure lie with the private operator. The entire country network leased to the new operator of the V/Line freight business, plus its Dynon freight terminal, will be subject to a third party access regime. The Office of Regulator General will be the regulator under the regime.

In the public sector, V/Line conducted an uneconomic business of transporting parcels and palletised freight. This was considered to have a significant community service obligation (CSO) element. Continuation of this was a condition of sale and a specific and defined CSO payment will be made to the private sector operator.

The Government made these decisions after conducting a review of the structural reform options for the intra-state freight network. The review found that the gains in terms of competition from a vertically separated track and freight business would be outweighed by the technical inefficiencies that separation would introduce.

Assessment

The Council is satisfied that Victoria has met its clause 4 obligations in respect of the introduction of increased competition and privatisation of the intra-state freight network.

ACT Milk Authority

In 1998, the ACT Government reviewed its *Milk Authority Act 1971* (the Milk Act). The review considered, amongst other things, the dual regulatory and commercial roles that resided in the Milk Authority.[17]

Under the Milk Act, the Milk Authority of the ACT was responsible for acquiring and marketing milk in the ACT (commercial functions), but also for determining maximum retail prices for milk, market entry and franchising arrangements (regulatory functions). In practice, these dual functions gave the Milk Authority a monopoly over milk marketing in the ACT. The review noted that the Milk Act "*was not meant to preclude competition in the ACT market, but this has occurred as a result of the dual roles of regulation and marketing being merged*"(ACT 1998).

To address this problem, the review recommended that:

- regulatory functions be administered within a government department;
- a commercial entity be created to market and promote the *Canberra Milk* brand; and
- the Minister refer determination of maximum retail prices to the Independent Pricing and Regulatory Commission (IPARC).

Since the review, the ACT Government has moved to separate the Milk Authority's regulatory and commercial functions. The ACT Government has done this by dividing the Milk Authority's regulatory, commercial and price determination roles between three agencies within government, such that:

- the Department of Urban Services is responsible for regulatory functions, notably public health and safety;
- the Office of Financial Management within the Chief Minister's Department is responsible for commercial functions through its oversight of the Milk Authority, which is now responsible for managing existing distribution franchise contracts and purchasing raw milk contracts; and
- the IPARC will shortly be made responsible for advising the Minister for Urban Services on maximum retail price determinations.

[17] See section B5 for a discussion of relevant legislation review matters.

Assessment

The Council is satisfied that the ACT has separated the commercial and regulatory functions of the Milk Authority and, therefore, met its second tranche clause 4 obligations. However, as the Australian dairy industry is undergoing a period of significant change, the Council will continue to monitor developments in the dairy industry in all jurisdictions, including the ACT, in future assessments of progress.

B5 Legislation Review and Reform

B5.1 The legislation review and reform commitment

Under clause 5 of the CPA, all governments agreed to review and, where appropriate, reform all legislation which restricts competition by the year 2000. The principle guiding these reviews, set out in clause 5(1), is that legislation should not restrict competition unless it can be demonstrated that:

- the benefits of the restriction to the community as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.

Application of the guiding legislation review principle involves review of both existing legislation that restricts competition and the testing of all new anti-competitive legislation to ensure that it is consistent with the guiding principle. The aim is better regulation rather than less regulation.

Consistent with this, the CPA recognises there will be circumstances where restrictions are justified. However, the justification must be in terms of a net benefit to the Australian community as a whole – not benefits to particular groups or regions.

Clause 1(3) of the CPA sets out a range of public interest matters that governments should take into account, where relevant, in assessing the net benefit of legislative restrictions. These factors include the environment, employment, social welfare and equity, economic and regional development, consumer interests, business competitiveness and economic efficiency.

B5.2 The Council's approach to assessing legislation review and reform progress

All governments established their NCP legislation review programs in June 1996 in accordance with the CPA.[18] These programs list for review all existing legislation considered to restrict competition. The obligation on governments is to complete all reviews and implement required reforms by the end of the year 2000.

Governments are also obliged to ensure that all new legislation restricting competition meets the guiding principles. To provide for this, the Council expects that each government's process for examining the potential impacts of anti-competitive legislation involve a rigorous assessment of the costs and benefits of alternative means of achieving the objective(s) of the legislation.

The Council has assessed jurisdictions' review and reform performance, covering the period to 31 December 1998, against two broad criteria.

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[18] Each government published a legislation review timetable in 1996 and reports progress against this timetable each year. The NCC publishes a consolidated listing of progress against all timetables (NCC 1998b).

First, the Council looks for progress against review timetables as documented through annual reports to be generally consistent with the CPA objective that the whole program be completed by the end of the year 2000.

The CPA specifies that the review program should be complete by the year 2000, but gives governments the discretion to delay the implementation of resultant reforms beyond 2000 through the provision that reform should be 'where appropriate'. However, consistent with this provision, where phasing of reforms takes implementation beyond the year 2000, governments should demonstrate that the more gradual approach provides a community benefit. The Council's discussions with jurisdictions indicate that all accept the need to justify any delays in reform implementation beyond 2000.

Related to this, the Council acknowledges that governments' review agendas are evolving documents and will reflect changes in priorities. Most governments have added to their review schedules where they have identified additional pieces of legislation restricting competition. In other cases, governments have removed legislation from their timetables where preliminary review has shown that the legislation does not contain significant restrictions on competition. It is the evolving review timetable, rather than that published in June 1996, which is the basis for the Council's assessment.

Second, the Council looks for governments to meet the spirit of the legislation review and reform program as set out in the CPA. There are two considerations here: that governments adopt rigorous review processes leading to robust outcomes, and that governments implement reforms in line with review recommendations, except where they can demonstrate a net community benefit from acting differently.

Good review processes require, as a starting point, that terms of reference permit consideration of all competition questions. The CPA contains clear obligations as to the analytical approach to reviews. Without limiting the terms of reference for reviews, a review should:

- clarify the objectives of the legislation;
- identify the nature of the restriction on competition;
- analyse the likely effect of the restriction on competition and on the economy generally;
- assess and balance the costs and benefits of the restriction; and
- consider alternative means for achieving the same result including non-legislative approaches.

As well as clear terms of reference, and particularly where restrictions are significant or complex, the Council expects review processes to be independent, objective and consultative. Analysis should be rigorous, with recommendations consistent with the evidence. Where reviews are conducted in accordance with these principles, the Council does not comment on the appropriateness or otherwise of review outcomes,

provided the conclusion reached by the review is one that an objective observer might have reached on the basis of the evidence.

Having conducted a robust review, governments are obliged to implement reforms that have regard to review recommendations without undue delay. Nonetheless, where a government decides not to introduce recommended reforms or to introduce new restrictions, it is able to do so under the CPA providing that it demonstrates its approach is warranted on net community benefit grounds. Similarly, where it is necessary to phase a reform beyond the year 2000, the Council does not see an assessment problem provided that there is a robust supporting net community benefit case.

There have been suggestions that the Council, in considering overall NCP implementation, should focus on significant reforms over individual legislation reviews that often have a relatively minor economic impact. The Council does not support this approach. Taken as a whole, successful completion of the legislation review program will produce substantial economic benefits, even though many of the individual reforms may be relatively minor. Disregarding individual legislation reviews or, conversely, disregarding individual compliance failures, would see the downgrading of the importance of much of the legislation review program. Accordingly, in assessing each jurisdiction's progress, the Council has identified every case where it considers that performance has not satisfactorily met its assessment criteria.

B5.3 Jurisdictions' progress against legislation review and reform schedules

The legislation review timetables established in June 1996 scheduled almost 1800 pieces of legislation for review over the period to the year 2000. The timetables have since developed further as governments identify additional restrictions for review and reshape their review and reform priorities.

Up to the end of 1998, which covers the period of the second tranche assessment, there were some 1100 reviews scheduled for completion across all jurisdictions. Of these, almost half were completed, with about another 400 underway. Governments have announced their responses in over 370 cases.

A summary of review progress achieved by each jurisdiction to the end of 1998, derived from jurisdictions' NCP annual reports, is provided in Table B5.1. Because some jurisdictions schedule their reviews on a financial year basis, others on a calendar year and there is occasionally incomplete reporting, the data in the table should be taken as indicative of progress only.

Table B5.1 Progress of reviews scheduled up to end-1998 by jurisdiction, at 31 March 1999

	Reviews scheduled[a]	Reviews completed and reform implemented	Reviews completed but reform still to be implemented	Reviews underway	Reviews scheduled but not yet commenced
Commonwealth	67	27	13	17	10
New South Wales	143	44	16	65	18
Victoria	121	57	19	20	25
Queensland	68	26	5	24	13
Western Australia	164	43	49[b]	47	25
South Australia	121	28	13	73	7
Tasmania	186	95	18	47	26
ACT	161	36	20	43	62
Northern Territory	85	17	9	55	4
Total (all jurisdictions)	1116	373	162	391	190

a Data on reviews scheduled do not include Acts where jurisdictions' preliminary reviews indicated there were no significant restrictions.

b The Western Australian Government has endorsed a response to 45 reviews but is yet to take legislative action to implement the approach endorsed.

Source: Jurisdictions' Annual Reports (1999)

Progress with review and reform programs by jurisdiction

All governments stated that their review and reform agendas are progressing, consistent with the CPA objective of removing unjustified restrictions on competition by December 2000. All up, governments have completed or commenced over 80 per cent of the reviews originally scheduled for completion by the end of 1998. Given the size and complexity of some of the larger reviews, this is a reasonable outcome.

Progress differs amongst jurisdictions, in part reflecting the different priorities at the time governments put their programs in place. Some governments, such as the ACT, scheduled the bulk of their program early on whereas others left most of their review program until later in the NCP period. Governments that scheduled their programs for early completion have tended to find it necessary to defer their programs, as the demands of ensuring rigorous examination of some highly complex matters became more apparent. In addition, because national reviews have not proceeded as anticipated, all governments have had to reschedule a range of matters for individual review. This reluctance to adopt national processes has increased the complexity of

the subsequent by-jurisdiction reviews because of the need to consider national consistency in regulatory arrangements.

As well as undertaking reviews, the CPA also obliges governments to implement the recommended changes by the year 2000, unless the responsible government can mount a robust net community benefit case to do otherwise. The Council has continually stressed the importance of meeting the year 2000 target if a jurisdiction is to be considered to have complied with its NCP obligations. On the indications to date, it is likely that some recommended reforms will not be in place by 2000. However, such delays would not infringe upon NCP obligations if they were shown to be in the public interest.

Significant reform outcomes have been achieved in a range of areas. Unjustified restrictions have been removed, for example, by repealing redundant legislation or streamlining licensing processes to ensure that community objectives are met while minimising imposts on business from unnecessary ‘red tape’. Conversely, governments have sometimes retained restrictions on competition or introduced new ones. Such action is consistent with the objectives of NCP, where rigorous assessment of the restriction shows that the benefits it offers the community outweigh the costs.

This section presents a broad overview of each Government’s progress against its legislation review and reform obligations. The matters have been identified following the Council’s scrutiny of governments’ NCP annual reports and/or questions raised with the Council by individuals and businesses that believe (unjustified) regulations are having an adverse effect on their livelihood.

Commonwealth

The Commonwealth scheduled 67 reviews to be completed by the time of the second tranche assessment. Of these, 40 have been completed, with the Government’s response announced in 27 cases. Of the 27 scheduled reviews not yet completed, three are underway, a further three Acts are expected to be repealed without review and one review has been deferred on the basis that it will now be examined through a national process.

The Commonwealth has delayed reviews of five Acts, but has commenced four third tranche reviews early. There are 20 reviews that have been scheduled for completion in the period 1998-1999 and a further 10 for 1999-2000.

The Commonwealth has completed NCP reviews in several significant areas. These include:

- the Wallis review of the regulatory framework of Australia’s financial system;
- review of legislation governing the operation of Australia Post;
- tariff reduction programs for both the automotive and the textiles, clothing and footwear industries;

- aspects of the health industry legislation restricting the market for private health insurance; and

- aspects of the Migration Act relating to student, business and visitor visas and registration of migration agents.

New South Wales

New South Wales had scheduled 143 reviews for completion by the second tranche assessment. The New South Wales Annual Report indicates that 60 reviews are now completed and 65 are underway. Of those reviews not yet completed, 17 are drafting final reports for Government consideration, two are now part of national review processes and three are to be conducted jointly with Victoria.

The Government has announced its response to 44 reviews, repealing 42 pieces of legislation. Five pieces of legislation are currently before the Parliament. Reform highlights follow.

- New South Wales' Licence Reduction Program reviewed 250 licences between August 1995 and February 1997. Of the 85 licences identified for repeal, 72 have already been repealed. Proclamation of the remaining 13 repeals have been made contingent on the outcomes of other review processes including NCP reviews. New South Wales also made changes to reduce 'red tape' and provide for more certain and consistent decisions on development proposals.

- In-principle agreement has been reached to remove the Rice Marketing Board's current vesting arrangements subject to the acceptance of Commonwealth single desk export arrangements.

- Changes in the *Environmental Planning and Assessment (Amendment) Act 1997* are intended to simplify procedures for obtaining approvals to projects such as construction of new buildings or commencement of businesses through a one stop shop process.

- Repeal of the *Bread Act 1969* has removed the licensing requirements for bread manufacturers and also the restrictions on standard bread sizes, baking times and delivery times.

New South Wales are addressing ahead-of-time several reviews scheduled to be completed in 1999-2000. Two reviews have been completed and have resulted in repeal of the related legislation and one other Act has also been repealed. One 1999-2000 review is currently underway and three others are being considered through a national process.

Victoria

Victoria originally scheduled 146 reviews for completion by the time of the second tranche assessment. Subsequently, preliminary reviews found that 22 Acts did not significantly restrict competition and did not warrant detailed review. Victoria removed a further two pieces of legislation, which provide exclusive licences for casinos, from its review timetable on the basis that these formed contractual

arrangements with little scope for amendment. Victoria also removed the *Control of Weapons Act 1990* from its review timetable on the basis that it relates to public safety.

Of the remaining 121 reviews, 76 have been completed. There are 20 reviews currently underway, 13 of which are nearing completion. In addition, the Government has completed or commenced 23 third tranche reviews ahead of schedule. Of these, five pieces of legislation have been repealed and a further nine review reports are awaiting Government consideration. Victoria stated in its annual report that considerable progress has been made against its review schedule and that it is on track to complete its legislation review program by the December 2000 deadline.

Victoria has announced its response to 57 reviews, repealing 41 Acts and implementing reforms to a further 14 pieces of legislation. Some key reforms follow.

- Changes to the *Barley Marketing Act 1993* provide for the progressive opening of the market to competition. Restrictions on the domestic marketing of barley and the exporting of packaged barley will be removed completely by July 1999. Restrictions on the export of all other forms of barley will be removed after a transition period (to July 2001) to allow the Australian Barley Board (and its successor) to adjust to operating in an open, competitive market.

- Reform of the *Liquor Control Act 1987* has simplified licensing procedures and relaxed restrictions on the consumption of liquor on licensed premises. Victoria has retained some restrictions on packaged liquor licences. For example, it prevents an individual or single entity holding more than 8 per cent of the total number of packaged liquor licences, and it prevents outlets such as convenience stores, petrol stations and cinemas selling packaged liquor. Victoria's liquor licensing arrangements are discussed further in section B5.4.4.

- Reforms to the regulatory arrangements governing several health professions include the relaxation of advertising controls and the removal of restrictions to ownership of practices. The statutory registration of practitioners and the restrictions on the use of professional title are retained.

- The legislative preference towards State Trustees, under the *State Trustees (State Owned Company) Act 1994*, to administer several categories of estates and funds has been removed.

Queensland

Queensland had 68 reviews (of its entire program of 114 reviews) scheduled for completion for the second tranche assessment. Of these, 31 reviews have been completed and a further 24 are currently underway. Of those underway, six are nearing completion, one Act is expected to be repealed and three are to be addressed by national review. There are 13 reviews yet to be commenced.

After commencing its review program later than most other jurisdictions, Queensland had a relatively heavy program scheduled for 1998-99, with 52 reviews in this period. At the time of its annual report, eight of these reviews had been completed (seven pieces of legislation repealed) and a further 18 were underway. Nonetheless, the

Government stated that it is confident it will complete its review and reform program by December 2000. It indicated in its annual report that several larger reviews were commenced at the beginning of 1998, ahead of schedule, to alleviate the overall review workload. The Government stated that it would continue to look for opportunities to commence larger reviews earlier than scheduled and would devote additional resources towards reviewing legislation to ensure timely completion of its review program.

So far the Government has responded to the recommendations of 26 reviews and repealed 23 pieces of legislation. Reform highlights follow.

- Reforms to the *Chicken Meat Industry Committee Act 1976* provide for individual growers to negotiate directly with processors outside of legislative collective bargaining arrangements.

- The Brisbane Marketing Authority is proposed for corporatisation.

- Advertising controls have been reduced and commercial controls removed in regulations governing Health and Medical Practitioners (separate review for Pharmacy and Optometry pending).

Several reviews recommended retention of restrictions on competition in areas of agriculture, including dairy, barley and sugar. These are discussed in the following sections. The Casino Agreement Acts, which provide exclusive licences, were retained without reform as Queensland considered them to be contractual arrangements with the respective private enterprises and not able to be repealed without compensation.

Western Australia

Western Australia scheduled 166 pieces of legislation for review by the time of the second tranche including two Acts subsequently found to contain no competitive restrictions.

So far, recommendations from 92 reviews have been presented to the Government for consideration. At the time of Western Australia's annual report, the recommendations from 43 reviews had been implemented, with 15 Acts being repealed entirely and restrictions retained in 28 Acts. In addition, the Government had endorsed the recommendations from a further 45 reviews, and was drafting legislation for implementation by the year 2000.

Western Australia's review program has recommended several significant reforms. Some of the highlights of the program to date are set out below.

- Repeal of the *Bread Act 1982* has removed a number of onerous restrictions, including licensing requirements for bake-houses, restrictions on the time at which bread can be delivered and requirements for marking vehicles used for delivery.

- Removal of several restrictions, under the *Betting Control Act 1954,* enable bookmakers to compete with the Totalisator Agency Board on a more level footing.

- Exclusive licences to provide port services such as towage, piloting and stevedoring can be granted only by the responsible Minister who must consider whether public benefits from exclusivity exceed public costs.

- The review of the *Chicken Meat Industry Act 1977* and associated Regulations recommended that the legislation be amended to allow broiler growers to negotiate contracts with processors outside the existing compulsory collective contract system. The review found that a voluntary collective contract arrangement is in the public interest because it offers protection to broiler growers from the strong market position of the two large chicken meat processors in Western Australia.

- The review of the *Finance Brokers Control Act 1975* and associated Regulations has recommended that the Act be repealed on the grounds that a less restrictive code of conduct would be equally as effective in protecting consumers as the current arrangements and would reduce compliance costs for finance brokers. It was also noted that the Act duplicated provisions contained within the Commonwealth *Trade Practices Act 1974* and the *Fair Trading Act 1987*.

- The current system of mandatory licensing, under the *Painters Registration Act 1961*, has been found to be too restrictive. The review of the Act recommended that certification be supported by a system of negative licensing, allowing for the removal from the industry of persons who do not adhere to basic standards of commercial conduct. Western Australia stated that this would reduce business costs but still enable consumers to readily identify painters with particular skills.

Western Australia reported that it is taking steps to ensure that it completes its review and reform obligations by December 2000. The Government believes that, with the increasing experience of its reviewers, the efficiency of the State's review processes has been improved. The Cabinet has also recently approved a National Competition Policy Omnibus Bill to implement amendments and repeals resulting from reviews.

Some 20 reviews scheduled for the third tranche have been commenced ahead of schedule. Further, the need for many scheduled reviews is being obviated by the development of new legislation. For example, new legislation covering the health and medical professions will effectively remove the need for 30 reviews. The recent *Port Authorities Act 1999* (expected to be proclaimed in August 1999) and other Bills awaiting enactment, including the *Agricultural Industries Bill,* will repeal a further 24 pieces of legislation scheduled for review prior to December 2000.

South Australia

South Australia scheduled 121 reviews for completion by the time of the second tranche assessment. South Australia's tabulations in its annual report indicate that 46 reviews are complete, including five reviews that had been scheduled for 1999 or beyond.

The Government has announced its response to 27 reviews. In 21 cases, the Government has repealed legislation, or has identified legislation for repeal once it is no longer operational. Acts repealed to date include the *Bulk Handling of Grain Act 1955, Catchment Water Management Act 1995, Manufacturing Industries Protection Act 1937* and *The Carriers Act 1891*. Proclamation of the *Livestock Act 1997* will

streamline regulations affecting market entry and conduct relating to the keeping of bees, cattle, pigs and deer by repealing six separate Acts. The Government is currently drafting new legislation following the review of the *Local Government Act 1934*.

Some 73 of the reviews scheduled for completion in the second tranche period are still underway. South Australia's report indicated that 22 of these are expected to be complete by mid-1999, with a further two expected to become national reviews.

Of the 13 reviews scheduled for completion in the second tranche period but not yet commenced, three are now to be examined through a national process. Review of the *Occupational Health, Safety and Welfare Act 1986* has been deferred so that it can be examined in conjunction with related legislation in 1999. Advice from South Australia is that the remaining 1998 reviews, which are primarily within the portfolio of Primary Industries, Natural Resources and Regional Development, are now to be reviewed in 1999.

South Australia has also brought forward some reviews, recognising that it has over 30 reviews scheduled for 2000. Its annual report indicated that 20 reviews scheduled for 1999 and beyond have commenced early.

The Government has retained restrictions in several pieces of legislation. Restrictions in shop trading arrangements in the *Shop Trading Hours Act 1977* and the partial deregulation of liquor licensing arrangements provided by the *Liquor Licensing Act 1997* are discussed in the sections B5.4.3 and B5.4.4, respectively.

Tasmania

Tasmania scheduled 202 reviews of legislation for completion by the time of the second tranche assessment. In 16 cases, preliminary reviews found that legislation did not contain significant restrictions and further review was unnecessary. Some 113 of the remaining 186 reviews are now completed.

Tasmania's annual report indicated that, of the 73 scheduled reviews not yet completed or still to commence, 14 are nearing completion, 12 are being conducted in conjunction with a national approach and 25 have been deferred pending completion of related reviews or the expected repeal of the legislation. Four reviews have been commenced ahead of schedule, and two other Acts have been added to the review schedule for the third tranche.

The Government has announced its response to 95 reviews, proposing to repeal 86 pieces of legislation including the following Acts.

- The *Apple and Pear Industry (Crop Insurance) Act 1982* is to be repealed as no evidence was found to suggest that legislation to require growers to take out crop insurance is needed for the industry to operate efficiently and effectively.

- Part III of the *Traffic Act 1925*, regulating the carriage of goods or passengers, was found to have controls that stifled innovation and increased costs to consumers. New legislation is to be developed in line with the national road transport reforms.

- The *Weights and Measures Act 1934* is to be repealed and replaced with nationally uniform legislation.

The Government has retained restrictions following consideration of review recommendations in nine cases. Restrictions retained following the review of the *Motor Accident (Liability and Compensation) Act 1993* are discussed in the following section.

Tasmania has had to reschedule for State-based review a large number of Acts that it had originally listed for national or multi-jurisdictional review. This has had the effect of increasing the demands on the State in the latter part of the program. However, Tasmania stated that its Regulation Review Unit is working with other Tasmanian Government agencies to facilitate completion of the remaining reviews by the year 2000.

ACT

The ACT had scheduled some 181 reviews to be completed by the second tranche assessment. However, in 20 cases, review was deemed unnecessary, the legislation having been repealed or found to have no significant restrictions on competition. Of the remaining 161 reviews, 56 have been completed and 43 reviews are currently underway. Three third tranche reviews have commenced ahead of schedule.

The Government has announced its response to 36 reviews, repealing 35 pieces of legislation. Significant decisions follow.

- Repeal of the *Trading Hours Act 1962,* which removes restrictions to Monday to Sunday trading hours, and retains only minimal restrictions on shop trading.

- Amendments to legislation, following review of racing codes, ensure persons are not excluded from market entry or from accessing racing infrastructure.

- Reforms to the *Milk Authority Act 1971,* to be phased in over 2 years, eliminate subsidies and remove exclusive geographic distribution franchises.[19]

Currently, some 62 reviews originally scheduled by the ACT for completion by the second tranche are yet to be commenced. While some of these are to be considered as part of national or joint-jurisdictional reviews, or are awaiting the outcome of other reviews, it appears that as many as 48 reviews have been rescheduled for completion by the end of 1999. A significant number of these are in the Health and Community Care portfolio, which has rescheduled 26 reviews, including nine that are incorporated into the review of health practitioner legislation about to commence. The Department of Urban Services has rescheduled another 9 reviews.

[19] Although the review and the Government's decisions raise concerns in relation to structural separation between commercial and regulatory functions under clause 3 and the requirement to retain legislation only where it is demonstrated to be in the public interest under clause 5. These issues are discussed in sections B4.2 and B5.4.1, respectively.

The appearance of slippage in the ACT program is a consequence of the Territory having originally scheduled all of its reviews for completion by 1998. The Council raised the matter of progress against legislation review commitments with the ACT Government and received an assurance that the ACT is on track to complete its review program by the year 2000.

Northern Territory

The Northern Territory had scheduled 85 legislation reviews to be completed for the second tranche assessment. Some 26 reviews have been completed. Of these, nine are awaiting a Government response and five found no restrictions on competition.

Of the 59 reviews not yet complete, 12 are nearing completion and eight are in the final phase of planned 3 stage reviews (due for finalisation by 30 June 1999). Two of these are now part of national review processes and two Acts are expected to be repealed.

The Northern Territory has identified two reviews relating to the functions of the Territory Insurance Office (TIO) which it expects will be subject to further external review. Restrictions contained in mandatory insurance legislation, including legislation governing the role of the TIO, are discussed in the following section.

The Government has announced its response to 12 reviews, repealing 11 pieces of legislation. Reform highlights follow.

- Repeal of the *Grain Marketing Act* and the subsequent dissolution of the Grain Marketing Board will facilitate rationalisation in the Northern Territory grain industry.

- Reforms to the *Commercial Passenger (Road) Act* have removed the restrictions on the number of taxi licences.

- The *Building Societies Act and Regulations* has been repealed and building societies now registered under the *Financial Institutions (NT) Code* as part of a national scheme of legislation.

- Repeal of the *Stock (Artificial Breeding) Act and Regulations* has removed restrictions on insemination and siring.

The Government has also endorsed the review recommendations for partial reform of the *Financial Management Act*, which governs the investment of Government funds. The Government has agreed to broaden the types of financial institutions able to hold a Government account beyond banks to institutions with a suitable published credit rating.

Of the four reviews not yet commenced, the *Mining Act* has been deferred pending the outcome of Native Title amendments, while the others are to be included in national review processes.

Only two reviews were scheduled for the period of the third tranche in the Northern Territory's original review timetable. While the number of reviews still underway at

the time of the second tranche suggests that the original scheduling may have been overly optimistic, the progress demonstrated to date by the Northern Territory indicates that it should have little difficulty completing its review program by the CPA target date.

B5.4 Legislation review processes and reform outcomes: matters directly relevant to the assessment of second tranche progress

As part of its scrutiny of jurisdictions' legislation review and reform activity for the second tranche assessment, the Council identified a number of matters relevant to determining whether governments' progress has been sufficient to meet the obligations set out in the CPA. Upon investigation, some of these matters raised questions about governments' compliance with NCP legislation review obligations, and so are directly relevant to the assessment of progress by States and Territories for purposes of competition payments. Those matters are discussed in this section.

The Council's investigations also found that, for some categories of regulation, governments' review and reform activity met second tranche NCP obligations or that, because the review and reform process has not been completed, the matter is more appropriately assessed in the third tranche. These matters are discussed in section B5.5.

B5.4.1 Regulation of the dairy industry

Background

Dairy farming is Australia's fourth largest rural industry, producing 6-9 million litres per annum with a gross production value of approximately $3 billion. Approximately 45 per cent of Australian milk production is exported, which represents 10 per cent of world milk trade. Raw milk is used as either "market milk" (that is, fresh drinking milk) or 'manufacturing milk', which is used in the production of milk powder, cheese and butter.

Historically, the market milk sector has been tightly regulated through state-based dairy corporations, while the more export-focused manufacturing sector is relatively lightly regulated. This has resulted in the market milk prices paid to producers being approximately twice that of manufacturing milk (the price of which approximates the world price).

State-based dairy industry regulation typically includes:

- vesting of milk in a statutory body;
- farmgate price setting for market milk;[20]
- supply management arrangements:

[20] The average all-Australian price paid to producers for market milk is 52 cents per litre as compared to an average 24 cents per litre for manufacturing milk.

- via market milk production quotas in New South Wales, Western Australia and South-East and Central Queensland;[21] and
- via market milk pooling in Victoria, North Queensland, South Australia and Tasmania;

- food and safety standards; and
- compulsorily funded industry services.

The Commonwealth also regulates aspects of the dairy industry through marketing agencies, the imposition of a tariff quota system on some imported cheeses and through Domestic Market Support (DMS) paid to manufacturing milk producers' exports. The DMS Scheme will sunset in July 2000.

Farmgate price and supply management arrangements have a large impact on the market. In 1996-97, the state-based market milk regulations delivered transfers to producers of almost $370 million, while the Commonwealth's DMS delivered almost $120 million to manufacturing milk producers. Table B5.2 shows the state-by-state break down of these aggregate assistance figures.

States traditionally also regulated the "post-farmgate" arrangements in the dairy industry. This refers to the relationships, including price and margins, throughout the processing, vending and retail chain. Following an agreement in the early 1990s, all governments except the ACT have removed their post-farmgate arrangements.

Table B5.2 Estimates of dairy industry assistance for 1996-97, by State

	Market Milk Assistance	Manufacturing Milk Assistance	Total Assistance
		($ million)	
New South Wales	128	1	129
Victoria	70	103	173
Queensland	97	2	99
Western Australia	34	1	35
South Australia	28	6	34
Tasmania	12	6	18
Total Assistance	369	119	488

Source: ABARE (1999) and ADC (1998).

[21] In South-East Queensland the quotas are statutory mandated, while in Central Queensland they voluntary industry arrangements which have the same effect on the market.

The Significance of the Victorian Dairy Industry

Victoria is the largest milk producing State, accounting for more than 60 per cent of total Australian production. More than 90 per cent of Victoria's production is used in manufactured milk products, of which approximately 50 per cent is exported. The remaining amount (less than 10 per cent) is used as market milk for human consumption. Victoria is also the lowest cost producer of milk in Australia.

This compares with next largest producers, New South Wales and Queensland, which produce 13 per cent and 9 per cent of total Australian milk production, respectively. In both States, approximately 50 per cent of total milk produced is used as market milk.

The size and structure of the Victorian dairy industry has a significant influence on the rest of the Australian dairy industry. There is also a perception within the industry that, of all of the States, Victoria is the most likely to fully deregulate its dairy industry arrangements following its current review. If this occurs, it is likely to have ramifications for dairy regulation in other States, particularly on the Eastern Seaboard. Should Victoria deregulate, it would become increasingly difficult for other jurisdictions to sustain any remaining price and market restrictions, due to the competitiveness of Victorian producers, processors and manufacturers, the operation of the *Mutual Recognition Act* and the threat of inter-state trade.

Current status of review and reform program

All States have scheduled reviews of their dairy industry legislation under NCP. New South Wales, Queensland, Western Australia and the ACT have all completed their reviews.

New South Wales

The New South Wales review of the *Dairy Industry Act 1979* was completed in November 1997. The members of the Review Group – chaired by New South Wales Agriculture and comprising industry and government representatives – were unable to agree on whether farmgate prices and supply management arrangements for market milk should be deregulated.

The Review Group agreed that the market milk arrangements resulted in revenue transfers from consumers to producers, resource use efficiency costs and consequential impacts such as regional multipliers and income effects. But the Review Group could not agree on the net public benefit (cost) arising from the arrangements. Government representatives estimated the arrangements produced a net cost in the order of \$86-\$132 million per annum. Industry representatives estimated the arrangements produced a net benefit in the order of \$95-110 million per annum – relying heavily on (disputed) large multiplier effects.

The Chairman and industry members concluded the benefits arising from the current arrangements exceed the costs and recommended that the current farmgate pricing and supply management arrangements be retained and reviewed again by July 2003.

The government members (other than the Chairman) recommended that farmgate price control and supply management in New South Wales for market milk be

removed within 3-5 years if nationally co-ordinated reform was not achieved. They also recommended the New South Wales Government support an industry application to the Australian Competition and Consumer Commission for authorisation of collective arrangements as a transitional measure following the cessation of the current arrangements.

In May 1998, the New South Wales Government announced that it would extend the current farmgate arrangements for five years until the year 2003.

Queensland

The Queensland review of its *Dairy Industry Act 1993* was completed in July 1998. The Review Committee comprised industry and government representatives, supported by a producer and processor Working Group advising on supply management arrangements.

The Review Committee recommended farmgate price regulation be retained for five years to December 2003, but reviewed again before 1 January 2001. It also recommended the retention of supply management (quota) arrangements in South East Queensland, and their formal extension into Central and North Queensland for five years.

In accordance with Queensland guidelines, a public benefit test of the current arrangements was undertaken based on economic modelling by consultants. The estimates of economy-wide effects ranged from a loss of $28 million to a gain of $54 million.[22] The Review Committee concluded that farmgate deregulation would have little overall impact on the Queensland economy, but that the expected industry rationalisation resulting from deregulation would have large impacts in regional economies.

The Committee stated that it believed the reform of market milk arrangements is ultimately inevitable. However, it did not support an immediate move to deregulate as it considered "*the potential social, economic, environmental and regional impacts as unacceptable*" (Queensland Dairy Legislation Review Committee 1998, p. 4). In recognition of this, the Committee supported a national approach to industry rationalisation and a review of the Queensland arrangements prior to the year 2001 if necessitated by industry changes and market pressures.

The Queensland Cabinet endorsed the recommendations of the review, extending the coverage and duration of farmgate price and supply management arrangements until the year 2003.

Western Australia

The review of the Western Australian *Dairy Industry Act 1973* was completed in 1998. Agriculture Western Australia conducted the review, overseen by the Treasury. The review was supported by an industry working party consisting of representatives

[22] Net present values in 1996-97 dollars over a ten year period.

from the Western Australian Farmers Federation, the Dairy Industry Authority and the Dairy Program Partnership Group of Agriculture Western Australia.

The Review estimated that farmgate pricing results in a transfer from consumers to producers in the order of $26 million per annum. The collective value of market milk quotas which underpin the supply management arrangements in Western Australia, were estimated to have a discounted capitalised value of some $88 million.

The review recommended:

- the retention of farmgate prices for market milk – on the ground that it corrects an imbalance in market power which is accentuated in Western Australia by the lack of competition in processing and retailing;

- the continued vesting of all milk in the Dairy Industry Authority – on the grounds that it is a means for achieving regulation, provides a secure payment system and ensures that milk companies do not under-state the volumes used as market milk; and

- the continuation of the licensing powers of the Authority – to ensure that health and quality standards are maintained. (Western Australian Government 1999, p. 58).

The review also found that quotas, as a mechanism for ensuring year round supply of fresh milk, are unnecessary. However, it recommended that quotas be retained in a modified form so long as regulated farmgate pricing continues.

The Western Australian Cabinet endorsed the findings of the review.

ACT

There is only one dairy farmer in the ACT, and the Canberra Milk Authority purchases more than 95 per cent of the Territory's raw milk requirement from New South Wales and Victoria. Unlike all other jurisdictions, the ACT has not introduced post-farmgate reform.

The ACT reviewed its *Milk Authority Act 1971* during 1998. The review was conducted from within the ACT Government but independent of the Department of Urban Services, which has portfolio responsibility for the Act. The review recommended:

- the structural separation of the commercial and regulatory roles of the Milk Authority;[23]

- the extension of existing raw milk supply contracts until 30 June 2000;

- the retention of maximum retail price setting until mid-2000, but that price determinations be made by the IPARC;

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23 See section B4 for a discussion of the clause 4 issues.

- reform of processor and distributor margins on 31 December 1998 (when the then current TPA exemption expired);
- requiring the Milk Authority to continue to purchase raw milk from the only ACT dairy, Goldholm Dairy, so long as the Authority continues to acquire bulk raw milk;
- reform of licensing and zoning arrangements for the home vending sector; and
- the arrangements be notified as exempt from the TPA.

The Review argued that the ongoing price regulation was in the public interest due to the uncertainty associated with post-farmgate deregulation outcomes in New South Wales. Further, the Review observed that 'regulated states'[24] had the lowest retail prices by an average of 15 cents per litre. The Review estimated that this produced a public benefit for the ACT in the order of $5 million per annum. It also considered the regulation was necessary to countervail potential retail price impacts due to the market power of the major food retailers.

In support of the existing arrangements, the Review argued that the various ACT milk businesses were locally owned, they had invested large amounts of money in their businesses, they employed local people, and their profits stayed in Canberra. The review estimated that the industry contributed $30 million per annum to the local economy.

However, the Review suggested that existing arrangements should not be maintained in perpetuity in an environment which is subject to rapid change at all levels, and stated that the restrictions on competition could at best only be justified in the short term (ACT 1999, p. 15 and p. 25).

In recommending reform of the home vendor sector of the industry, the Review noted that the sector is confronting demand and financial difficulties despite being cross-subsidised by the retail sector by $850 000 per annum (or 2.5 cents per litre).

In mid-1998, prior to the Government responding to the review recommendations, National Foods entered the ACT retail milk market in competition with the incumbent operator using milk processed outside the ACT, thus effectively deregulating the ACT retail milk market. In its Annual Report, the ACT stated that:

> *Competition in the market has not impacted adversely on consumers, who are paying similar prices for retail milk. There is greater choice in products for consumers.* (ACT 1999 p. 8)

The ACT Government has endorsed the review recommendations. A Bill to give effect to the recommendations and to extend the exemption from the TPA was rejected by the ACT Legislative Assembly in late 1998. Consequently, the existing

[24] Being, New South Wales, Queensland and the ACT which, at the time of the review, still had post-farmgate regulation in place.

legislation lapsed on 1 January 1999, effectively deregulating dairy arrangements in the ACT. However, in March 1999, the Bill was passed by the ACT Assembly restoring (or re-regulating) the dairy arrangements.

Other jurisdictions

The Victorian dairy industry review is underway. An independent consultant has been engaged to conduct the review. An Issues Paper was released in March 1999 seeking submissions to the review from interested parties. The reviewer is expected to report to the Victorian Government in July this year.

The South Australian review is also in progress. An independent reviewer has been engaged who has initiated a public consultation process. The reviewer is expected to report to Government in October 1999.

The review of Tasmanian dairy arrangements is in progress. The Review Group initiated its consultative processes with the release of an Issues Paper in the second half of 1998. In April 1999, the Tasmanian Government advised that the process was close to completion.

The Commonwealth review of its remaining dairy industry regulations was scheduled for 1998-99. However, the review has been delayed and is now expected to start in the second half of 1999.

These reviews will be considered in the Council’s third tranche assessment.

National developments

The Australian Dairy Industry Council (ADIC) has proposed an Australia-wide dairy industry reform and adjustment package to the Commonwealth. The ADIC proposes the simultaneous repeal of all remaining State and Territory dairy regulation in mid-2000 and the payment of $1.25 billion to assist dairy producers to adjust to the open market. ADIC has proposed the imposition of a levy on all market milk to fund the package. The Commonwealth is considering its response.

All reviews to date have expressed support for a national approach to any reform.

The Council supports consideration of transitional arrangements and/or adjustment assistance as a complement to reform, particularly where an industry is traditionally highly regulated and important to regional economies (NCC 1999).

The Council agrees that a national approach to reform, incorporating appropriate adjustment arrangements, may be worthwhile. Recognising the continuing influence of domestic and international pressures that have driven productivity improvements over the past decade, the Council considers that any adjustment assistance package should include measures to encourage continued productivity improvement. Relevant considerations when considering an adjustment assistance package include the appropriate quantum and targeting of the assistance.

Assessment

Given the size and importance of the Australian dairy industry, the Council considers the review and, where appropriate, reform of restrictions on competition in the industry to be an important component of the NCP agenda. Accordingly, The New South Wales, Queensland, Western Australian and ACT dairy industry reviews are all relevant to the second tranche assessment.

The Council has various concerns about the reviews conducted to date. For example, the split along industry and government lines of recommendations from the New South Wales Review Group highlight the Council's concerns about the need for review panels, particularly in sensitive areas such as dairy, to be independent from industry. Industry should participate in reviews via submissions, and other consultative mechanisms, rather than direct representation on review panels. More generally, the Council is not satisfied that the reviews have clearly demonstrated a net community benefit in support of the retention of market milk arrangements.

Similarly, the Council is concerned about the robustness of the cost-benefit analysis undertaken in reviews. For example, many of the costs and benefits listed in the ACT review report appear to have been included directly from submissions without analysis of their merit. The Council's recognises that the ACT's analysis is predominantly qualitative: however, the review does not appear to weigh up the many costs and benefits listed and thereby provide an overall sense of where the balance of the public interest lies. Further, some of the identified 'benefits' presented in support of retaining marketing arrangements are doubtful – for example, that school children can see cows from a particular road.

However, in view of the proposed national dairy industry reform and adjustment package that is currently under consideration, and recognising the significance of the outcome of the Victorian review in determining the direction of reform Australia-wide, the Council consider the New South Wales, Queensland, Western Australia and ACT reviews through a supplementary assessment before July 2000.

A common difficulty encountered when considering legislative reform is balancing the concentrated nature of the benefits arising from restrictions with diffuse benefits, often spread across the economy, from reform. This is an issue facing governments when considering reform of dairy farming. However, it is not a reason to avoid reform.

For example, the Queensland Dairy Review Group determined that "*the overall impact on the economy is of less concern than the potentially important regional effects*" (Queensland Dairy Legislation Review Committee 1998, p. 163). This approach suggests that the review believed that the highly concentrated benefits to a few from the existing arrangements should be protected at the expense of the more diffuse costs to the majority. This approach is inconsistent with the principle underpinning the NCP legislation review, that arrangements should be reformed unless it can be shown that they deliver a net benefit to the community as a whole.

The Council takes this opportunity to make the following general comments relevant to reviewing the dairy industry under NCP.

Typically, four reasons are put forward by the dairy industry in support of market milk arrangements, specifically:

- ensuring year round milk supply at stable prices;
- countervailing the market power of dairy processors and retailers;
- support or provide protection for Australian producers against “corrupt” world markets; and
- supporting regional economies.

To varying degrees, each review presents these arguments and relies on them to support recommendations for the status quo.

Against this, the following points arising from these reviews should be noted.

- It is not clear why milk is significantly different from other basic foods, the price of which fluctuate throughout the year according to seasonal availability. It is likely that year round supply would be achieved in the absence of supply management arrangements, with higher prices paid to producers in lower production periods to ensure supply.
- It is not clear that there is undue concentration and/or abuse of market power by retailers. Any risk of this is reduced by large farmer co-operatives, that are a significant feature of the milk processing sector and that provide countervailing power to farmers. Further, if the retail sector is misusing a position of market power, there are remedies available under the TPA.
- it is true that world prices for dairy products are distorted by subsidies paid to producers (notably within the European Union). However, this has been the case for many years and is likely to be the case for some time further, recognising that assistance levels are gradually being reduced through world trade negotiations. Further, matching overseas assistance would impose significant costs on the Australia, not only through any direct payments to producers, but through domestic market distortions and a reduced incentive for the industry to innovate.
- While regional development is a legitimate and important policy objective of government, a tax on milk consumers to subsidise producers is a particularly blunt policy tool to achieve this objective (IC 1997, pp. 40-44).

Additionally, dairy has, and continues to, benefit from high levels of assistance compared to other Australian agricultural industries. No clear case has been presented in the reviews to date to demonstrate why the dairy industry is more deserving of this assistance.

All reviews have drawn attention to, and to various degrees relied upon, experiences of retail price rises between 10 and 20 cents per litre following post-farmgate deregulation, as evidence of the power of the retail sector and of little or no consumer benefit from further reform. These price increases are not surprising as:

- post-farmgate regulation held processor and retail margins below what are considered 'normal' commercial levels – partial deregulation has allowed them to adjust prices;
- the demand for fresh milk is relatively inelastic; and
- farmgate prices continue to be set by regulation: that is, the input cost to processors, and consequently retailers, remains fixed. Therefore, processor and retail margin adjustments have been accommodated at the retail level.

Each of the reviews expressed the view that deregulation is inevitable, with market arrangements becoming increasingly difficult to sustain due to domestic and external commercial pressures – the most immediate being the outcome of the Victorian review which is widely expected to recommend reform. Each review expressed concern that reform should be introduced in a manner sensitive to expected social and economic impacts on producers and rural communities.

Contrary to these sentiments, the reviews have largely recommended retention of existing market arrangements without incorporating transitional arrangements either in terms of staged reform implementation or structural assistance. The approach proposed by New South Wales and Queensland for their dairy industries, leaving existing arrangements in place for a further five years without a progressive introduction of transitional arrangements to open competition, has the potential to exacerbate any industry dislocation. Such an approach provides no impetus or incentive for the dairy industry to prepare for, and respond to, expected change.

B5.4.2 Domestic marketing arrangements for rice

Background

In 1995, the New South Wales Rice Review Group (the Review Group) recommended that the domestic rice marketing monopoly held by the New South Wales Rice Marketing Board (the Board) be deregulated, finding that this would deliver a net community benefit. The Review Group found a case for retaining the Board's export monopoly.

The Review Group proposed that domestic deregulation be implemented by allowing the Board's vesting power over the New South Wales rice crop to expire after 31 January 1999. However, contrary to this recommendation, the New South Wales Government retained the existing vesting arrangements until 31 January 2004, with a further review in the year 2002.

In its first tranche assessment in June 1997, the Council identified the decision by New South Wales not to reform its domestic rice marketing arrangements, consistent with the review finding, as a compliance failure under clause 5 of the CPA. The Council's decision did not extend to the single desk export monopoly. The Council agreed to reassess New South Wales' progress with implementing domestic deregulation prior to July 1998 following an undertaking by the New South Wales Government to work with the Council towards resolving the matter consistent with the recommendations of the 1995 Review.

Despite extensive discussions, the following twelve months saw no progress toward deregulating domestic rice market arrangements. As a result, in June 1998, the Council recommended that the Commonwealth Treasurer deduct $10 million from the 1998-99 component of the New South Wales first tranche NCP payments. The deduction was to apply from 31 January 1999, being the date for reform of domestic rice marketing recommended by the 1995 Review Group. The Council based its penalty broadly on the costs that the Review Group estimated fall on the Australian community as a result of the current domestic arrangements.

Subsequently, the Commonwealth Treasurer established a working group to examine Commonwealth options for ensuring a single desk for rice export under Commonwealth jurisdiction, if necessary, while allowing for domestic market deregulation. The Working Group was chaired by the Commonwealth Department of Agriculture, Fisheries and Forestry Australia, with participation from the Council Secretariat, Commonwealth Treasury, the Ricegrowers' Association of Australia, the NSW Rice Marketing Board and the Ricegrowers' Co-operative Limited (RCL).

On 22 January 1999, the Working Group delivered its report to the Commonwealth Treasurer. The key features of its preferred model were:

- the establishment under Commonwealth jurisdiction of a Rice Export Authority (REA) to manage a Commonwealth export monopoly for rice;
- sole export rights to reside with the RCL for an initial 3-5 years;
- during this period the REA may approve third parties to export rice where such action would not diminish benefits arising from the single desk;
- the regular review of the single desk to ensure it delivers a net benefit to the community;
- the REA to report regularly to the Commonwealth Parliament on the use of the export monopoly; and
- the cost of managing the single desk to be recovered from exporters.

Developments

In April 1999, the Commonwealth Treasurer sought in-principle agreement from the New South Wales Premier to deregulate domestic rice marketing arrangements in line with the Working Group's preferred model. The Premier gave his in-principle agreement, thereby ensuring receipt by New South Wales of all first tranche competition payments.

The Premier put three qualifications on his State's continuing involvement in the rice marketing reform process. Specifically, that:

> - *the proposed Commonwealth single desk arrangements are feasible and practical, and do not put the export premiums under any risk;*

- *account is taken of the industry argument on the need for a transitional period to the commencement of the arrangements, and on the length of the initial period for which the [RCL] would be given an exclusive export licence; and*

- *all other States are in agreement with the proposal.*

The Treasurer asked the Council for its views on the New South Wales' in-principle commitment. The Council stated that it was satisfied with the commitment but made several comments on the Premier's qualifications.

First, the feasibility and practicability of a single export desk was addressed in the New South Wales 1995 rice industry review which found that it was feasible. This position was endorsed by the RCL both at the time and subsequently. As to the security of export premiums, a single export desk under Commonwealth jurisdiction will be at least as secure as the current New South Wales rice export arrangements, given the Commonwealth's constitutional power to legislate with respect to exports.

Second, the rice industry should be put on notice that the transition period prior to the new arrangements begins immediately and concludes with the passage of Commonwealth and New South Wales legislation, which will establish the single desk and repeal the domestic market arrangements respectively. Genuine reform requires near-simultaneous legislative action by the Commonwealth and New South Wales Governments

The Council sees no reason to extend the transition period or delay the reform of New South Wales' domestic rice marketing arrangements as:

- it is now four years since the rice review recommended domestic market reform, and the review suggested the industry was then already well placed to meet the challenge of more competitive domestic arrangements;

- export premiums arising from New South Wales rice exports will be protected under the Commonwealth single desk and by the initial exclusive licence period;

- only the small proportion (approximately 15 per cent) of New South Wales rice production which is marketed on the domestic market will be affected by the reform of the New South Wales marketing arrangements; and

- the policy refinement, legislative drafting and legislative action required to achieve this will take several months.

Parties have agreed that the duration of the initial exclusive licence period to be conferred on the RCL will be between three and five years. This will be the subject of negotiations prior to the introduction of the Commonwealth arrangements.

Assessment

The Council is satisfied that the in-principle agreement by New South Wales to domestic rice market reform meets the second tranche NCP obligations.

However, the Council is concerned to ensure that the policy development and implementation of the Working Group's preferred model is not unduly delayed, particularly in light of the Premier's qualifications on his Government's continuing involvement.

The Council will continue to monitor developments to ensure progress remains on track and will consider the outcome in its third tranche assessment of progress. Notwithstanding this, if prior to the third tranche assessment, evidence emerges that progress is unduly delayed, the Council will consider making a supplementary second tranche assessment and recommendation to the Commonwealth Treasurer on competition payments to New South Wales.

B5.4.3 Shop trading regulation

Background

Legislation controlling the trading hours of shops was common place across Australia ten years ago. Prohibitions on Sunday trading date back to pre-Norman England and the first restrictions on trading hours in Victoria were introduced in 1885. These restrictions were intended to achieve a number of objectives, including observance of the Sabbath, protection of shop employees and to minimise the risk of market dominance by larger retailers. The legislation normally allowed for exemptions for a range of premises based on size, location and product sold – mainly small local shops selling newspapers, milk and tobacco. The impact of such legislation was clearly anti-competitive, with significant adverse effects on consumer convenience and choice.

The position across the different jurisdictions now differs widely. A generally deregulated environment is already established in New South Wales, Victoria, ACT and Northern Territory. Significant restrictions are still in place in Queensland, Western Australia, South Australia and Tasmania.

Current status of review and reform program

All jurisdictions, except the Northern Territory, have reviewed or will review trading hours legislation over the period of NCP. The Northern Territory has no specific trading hours legislation and has minimal regulation of shop trading. Table B5.3 below sets out the current position in each jurisdiction.

Shopping regulation was reviewed in Victoria in 1996 and in the ACT in 1998. Trading hours and other shopping arrangements are now largely deregulated in both jurisdictions.

Trading hours in New South Wales are also largely deregulated. Residual controls are through the *Factories, Shops and Industries Act 1962*, which was scheduled for review from 1996-97. The Act regulates a range of matters, including hairdressers and occupational health, in addition to trading hours. A series of staged reviews of the Act have commenced, although the trading hours component is still to be examined.

Queensland's review of the *Trading (Allowable Hours) Act 1990* and the *Trading (Allowable Hours) Regulation 1994*, which was scheduled for early 1999, has been deferred until the determination of a relevant appeal in the Industrial Court against a decision on Sunday trading hours by the Industrial Relations Commission.

In Western Australia, the original timetable for the review of the *Retail Trading Hours Act and Regulations* was extended due to the substantial number of submissions received. Completion of the review is now due by the end of June 1999. A Community Reference Group has been convened to consider issues presented by the review team.

The Tasmanian review of the *Shop Trading Hours Act 1984* is scheduled to commence later in 1999.

South Australia reviewed its *Shop Trading Hours Act 1977* in 1998. The SA Government announced new trading hours arrangements on 21 October 1998, to come into effect on 8 June 1999. While there has been some liberalisation, the new arrangements maintain significant restrictions in several areas.

The second tranche assessment, therefore, concentrates on the South Australian *Shop Trading Hours Act 1977* – Victoria and ACT have already implemented deregulated arrangements; Northern Territory has limited restrictions; and the review and reform performance of the other jurisdictions will be assessed in the third tranche of NCP.

Table B5.3 Progress with reviews of shop trading legislation by jurisdiction, at 30 June 1999

	Legislation	Review Status	Current Restrictions
New South Wales	*Factories, Shops and Industries Act 1962*	Review has not commenced	Minimal restrictions – Monday to Saturday trading hours not regulated but some restrictions on Sunday trading
Victoria	*Shop Trading Act 1987* and *Capital City (Shop Trading) Act 1992*	Review completed 1997	Minimal restrictions – Monday to Sunday trading hours not regulated
Queensland	*Trading (Allowable Hours) Act 1990 (and regulations)*	Review to commence in July 1999	Significant restrictions – Monday to Saturday trading hours regulated, and Sunday trading prohibited outside major towns where it is restricted
Western Australia	*Retail Trading Hours Act 1987 (and regulations)*	Review underway and due to report in June 1999	Significant restrictions – Monday to Saturday trading hours regulated, and Sunday trading prohibited outside tourism precincts where it is restricted

	Legislation	Review Status	Current Restrictions
South Australia	*Shop Trading Hours Act 1977*	Review completed 1998 and limited changes announced on 21 October 1998 with effect 8 June 1999	Significant restrictions remain – Monday to Saturday trading hours regulated, and Sunday trading prohibited outside Adelaide CBD where it is restricted – recent changes had limited impact
Tasmania	*Shop Trading Hours Act 1984*	Review scheduled to commence later in 1999	Significant restrictions – Monday to Saturday trading hours regulated, and Sunday trading prohibited for shops employing more than 250 people
ACT	*Trading Hours Act 1962*	Trading Hours Act repealed in 1997 due to lack of community support for trading hours restrictions	Very minimal restrictions – Monday to Sunday trading hours not regulated
Northern Territory	No specific 'shop trading hours' legislation	No review scheduled	Very minimal restrictions – Monday to Sunday trading hours not regulated

Source: Jurisdictions' Annual Reports (1999)

Shop Trading Hours Act 1977 (South Australia)

South Australia reviewed its *Shop Trading Hours Act 1977* in 1998. This legislation imposed considerable restrictions on trading hours. Arising from the review, the South Australian Government announced new trading hours arrangements on 21 October 1998, which came into effect on 8 June 1999.

South Australia's legislation exempts certain shops from the controls on hours of trade. Exemption is based on size and type of shop. This second exemption category includes a variety of activities and products, such as antiques (other than coins or stamps), live fish, wood carvings, greeting cards, surgical appliances, fresh flowers, ice-cream, household pets, garden supplies, hairdressing, souvenirs, cigars, motor vehicles and boats. The only change to this list, following the review, was to extend the exemption to include the sale of caravans and trailers.

The South Australian Government's response to the review provides for:

- trading by non-exempt shops, in the city, to be allowed until 9 pm, Monday-Friday, but only until 7 pm, in the suburbs (except for Thursday when trading is allowed until 9 pm), although the extended hours do not apply to (exempt) traders of motor vehicles or boats;
- trading by non-exempt shops will be allowed on Easter Sunday in the city only from the year 2000; and
- trading on Sundays allowed in the suburbs on six Sundays a year – four before Christmas with the two others prescribed following consultation.

While the new legislation provides for some extension to allowable trading hours for shops that are not exempt from controls on hours of trade, the new arrangements still contain significant restrictions, including:

- controls on the hours during which shops may open;
- variation in allowed hours, based on the day of the week; and
- discrimination in controls between different shops dependent on location, size and products sold.

Assessment

As well as restrictions on trading hours, the discriminatory treatment of different retailers with little apparent justification is a concern for competition policy. There is no clear net benefit from restricting the right of a shop to sell coins or stamps on a Wednesday evening when its neighbour, which sells antiques, is allowed to trade. The exemption on small shops, whatever their sales, is clearly discriminatory to the detriment of larger businesses.

There may also be adverse consequences for consumers from unjustified restrictions on competition. For example, an evaluation of the impact of deregulated shopping hours in Victoria indicates that longer trading hours increases consumer welfare. The work found a net benefit to consumers, in terms of increased convenience nationally, valued at $1.2 billion or $65 per capita in 1995-96 prices (Brooker and King 1997).

The annual report from South Australia confirms that the trading hours review identified many of these issues.

> *The review found that the Shop Trading Hours Act 1977 and its regulations provide for a very complicated web of principles, licences, exemptions and exceptions…There is no consistent, coherent theme to the Act….The objectives of the Act are unclear….Any residual necessity for the Act on industrial grounds is arguable given the existence of industrial tribunals and the award system…. The Act is discriminatory in its application.* (Government of South Australia 1999)

However, there appears to be a disparity between this analysis, which is reported from the NCP review, and the suite of measures that have been adopted by the Government. The annual report material provided by South Australia does not make clear the extent to which those measures followed or were in contradiction to the recommendations of the NCP review of the State's trading hours. South Australia's annual report also provides little, if any, public interest justification for the restrictions now in place, stating only that the changes to trading arrangements "*represent a workable solution to balancing the interests of large and small retailers, of city and suburban traders and employees, employers and consumers*" (Government of South Australia 1999, p. 17).

Despite a request by the Council, South Australia did not provide the Council with a copy of the trading hours review report or a detailed comparison of the review's recommendations and the Government's decisions. South Australia offered to brief the Council on the key findings on a confidential basis and indicated that it would report in full in the year 2000, consistent with its view that the obligation in the CPA is the review and removal of unjustified restrictions by the end of 2000.

The Council does not support the interpretation placed by South Australia on the CPA obligation. The agreement contains a clear commitment on governments to report annually on their progress with reviewing and reforming legislation. The Council does not consider that a briefing on a confidential basis provides a sufficiently transparent approach to progress reporting.

Given the limited analysis of the net community benefit from the restrictions now in place provided by South Australia, the Council was not able to assess the adequacy of the review process, or the extent to which the recommendations were implemented. In particular, the Council cannot be certain that the South Australian Government has met the key tests in the CPA that existing restrictions on trading arrangements provide a net community benefit and that the restrictions are needed to achieve the objectives of the legislation. The Council will consider an annual deduction from South Australia's NCP payments if South Australia does not remove unjustified restrictions on shop trading arrangements by 31 December 2000 or demonstrate that the restrictions retained beyond 31 December 2000 provide a net community benefit.

B5.4.4 Liquor licensing

Background

The primary objective of liquor laws, across jurisdictions, is the minimisation of harm associated with the abuse of alcohol, and the consequential provision of adequate controls over its sale and consumption. Some jurisdictions' laws also have the objectives of promoting proper development of the liquor industry and diversity in response to consumer needs. These objectives are said to be in recognition of consumers' expectations about the availability of liquor and the commercial expectations of the various participants in the liquor retailing industry.

As a result, licensing laws in most States contain 'public interest' requirements that restrict competition among businesses in the supply of liquor. This covers both supplies for consumption 'on-site', as in a hotel or restaurant, and 'off-site' as from a bottle-shop. The restrictions may include, for example, the requirement to be licensed, controls on the type of premises which can supply liquor, limitations on trading hours and a need for the licence holder to demonstrate that they are a suitable person. There are also a range of site controls, including the segregation of liquor sales from other activities and prohibition on access by minors.

Traditionally, the consumption of liquor has been based around hotels, both for on-site consumption and, as in some jurisdictions, for off-licence sales. The past ten years have seen a general movement to a more liberal, deregulated marketplace, in line with the growth in the number and range of venues for eating and gaming. For example, in Victoria, the number of premises licensed for consumption of liquor on the premises (mainly restaurants) rose from 731 in 1987-88 to 2 340 in 1995-96.

For off-licence sales of packaged liquor, the main restriction is on the type of businesses that can be licensed. Victoria, Queensland, South Australia and Tasmania all prohibit the sale of liquor by convenience stores. In New South Wales, Western Australia and the Northern Territory, licence applications for convenience stores are at the discretion of licensing agencies, but are rarely permitted. The ACT allows the sale of packaged liquor by convenience stores, except where such stores also sell petrol.

This prohibition on the sale of liquor from petrol stations is also in place in Victoria, Queensland, South Australia and Tasmania. Only the Northern Territory allows petrol stations to sell packaged liquor, most commonly from combined road-house/ restaurant/petrol stations in remote areas. Licensing of petrol stations in New South Wales and Western Australia is at the discretion of licensing agencies, although approval appears to be rarely granted.

In Victoria, there is an additional restriction that a single person or corporation may not hold more than 8 per cent of the total number of packaged liquor (off-premises) licences (the 8 per cent limit).

Current status of reviews of liquor licensing

All States and Territory Governments are reviewing their licensing laws over the period of NCP. However, to date, only South Australia and Victoria have completed reviews and implemented reforms.

In Victoria, the Government adopted a progressive, broad-based reform program. This has simplified licensing arrangements so alleviating compliance burdens, removed the ‘needs’ criterion and restored broader planning controls to local government. However, Victoria also retained some of the previous restrictions, including the prohibition on sales of packaged liquor by convenience stores and the 8 per cent limit for packaged liquor licences (although the 8 per cent limit was removed for licensed premises).

In South Australia, the outcome of the review and reform process was partial deregulation, with some of the existing restrictions retained. However, the review also recommended a further review after three or four years, once evidence is available on the effects of the reforms and of the experience of deregulation in other jurisdictions.

The Northern Territory intends to pass new licensing legislation later in 1999, as part of a broader review of licensing including liquor and gaming. The Western Australian Parliament is currently considering a Bill to limit the number of licences that could be held by an individual or business. As new legislation, both proposals will need to meet the provisions of clause 5(5) of the CPA. The Northern Territory confirmed its intention to conduct an NCP review prior to developing its legislation.

The current status of licensing reviews is set out in Table B5.4 below. Victoria and South Australia are relevant jurisdictions for the second tranche assessment as both have conducted reviews and implemented reforms. All other jurisdictions will be assessed as part of the third tranche, because of the timing of their review and reform programs. Thus, the Council’s primary focus in this assessment is on:

- Victoria's *Liquor Control Reform Act 1998*, which retains certain controls in the earlier *Liquor Control Act 1987*, especially where the review recommended deregulation; and

- South Australia's *Liquor Licensing Act 1997*, which retained restrictions in the earlier *Liquor Licensing Act 1985*.

Table B5.4 Progress with reviews of liquor licensing arrangements by jurisdiction, at 30 June 1999

	Review and Reform Status
New South Wales	Review underway and scheduled for completion in late 1999
Victoria	Review completed 1998 and changes implemented 1998 and 1999
Queensland	Review underway and scheduled for completion in July 1999
Western Australia	Review underway and scheduled for completion in June 1999 (Private Member's Amendment Bill also currently under consideration)
South Australia	Review completed 1996 and changes implemented in 1997
Tasmania	Review scheduled to commence in the second half of 1999
ACT	Review underway and scheduled for completion mid 1999
Northern Territory	Review underway and scheduled for completion in September 1999; new legislation on licensing of liquor controls and gaming to follow

Source: Jurisdictions' Annual Reports (1999)

Liquor Control Act 1987 and Liquor Control Reform Act 1998 (Victoria)

Victoria's Review of the *Liquor Control Act 1987* commenced in September 1997. The review followed a semi-public process, involving an Issues Paper, Discussion Paper and a final Review Report provided to the Government in April 1998. The review panel received 47 submissions, met with 20 interested parties and commissioned an independent analysis of the effects of the restrictions on competition in the liquor industry.

The Review recommended significant pro-competitive reform of Victoria's liquor laws, particularly in regard to licensed premises. Victoria has now implemented substantial pro-competitive reform, including simplification of the licensing arrangements, abolition of the needs criterion, and relaxation of the controls on the presence of non-drinking minors on licensed premises under adult supervision. These changes were implemented through the *Liquor Control Reform Act 1998*. As a consequence, liquor retailing in Victoria is now less restricted than in any other jurisdiction.

However, Victoria also retained certain restrictions on licensing in the *Liquor Control Reform Act 1998*. For example, it retained the restriction on the number of packaged-liquor licences that can be held by the same or related persons (to 8 per cent of the

total available licences), contrary to the Review recommendation for its removal. Victoria also retained the restriction on sales through outlets such as convenience stores, cinemas and petrol stations in line with the Review recommendation. Victoria's basis for retaining this restriction was concern about problems that may occur from potentially easier access to liquor for minors and proximity of liquor to drivers.

Analysis of competition issues

The two relevant matters for the assessment of Victoria's performance against the NCP legislation review and reform principles are Victoria's decisions to:

- retain the 8 per cent limit; and
- retain the restriction on sales through outlets such as convenience stores and petrol stations.

Victoria's arguments

Victoria argued in its annual report that the 8 per cent limit is consistent with the objective of minimising underage drinking. Victoria indicated that it would also have the effect of protecting smaller retail bottle-shops, particularly in the regions, from competitive pressures and would also guard against market dominance reducing competition. Victoria's annual report stated that "it is not unreasonable to expect that in an entirely unregulated market a duopoly may emerge."

Victoria retained the ban on licensing certain premises (such as convenience stores in metropolitan Melbourne and provincial cities, milk bars, petrol stations and drive in cinemas). The Government indicated that the potential for alcohol abuse by young drinkers was the basis for its concerns about the licensing of convenience stores (generally seen as premises of not more than 240 square metres selling food and other convenience products, being different from small supermarkets). Victoria's annual report also stated that it is agreed by the Victoria Police and alcohol and drug agencies that access to packaged liquor through supermarkets is a significant contributor to the problem of underage drinking in public places.

Furthermore, the Government is concerned about the proximity of liquor to drivers. It considers that licensing petrol stations would have implications for drink driving because, unlike purchases from drive-in bottle shops where the intention to purchase alcohol is clear, the availability of packaged alcohol at petrol stations may encourage impulse purchases.

The Government therefore stated that it is not in the community interest for premises such as drive-in cinemas, petrol stations and convenience stores to be licensed.

Victoria's NCP review

Victoria's NCP Review had assessed these issues and recommended abolition of the 8 per cent limit. In support of this recommendation, the Review concluded that:

- the 8 per cent limit is not necessary to achieve diversity in retailing;

- liquor retailing overall is likely to be more competitive in Victoria in the absence of the rule;
- no other State or Territory has an explicit restriction on the number of liquor licences that may be held by a person or corporation;
- the Victoria Police acknowledged that the two major supermarket chains are 'responsible sellers of liquor';
- several wholesale buying-groups supply multiple licensed retail outlets at a level well in excess of the 8 per cent limit; and
- an increase in the general availability of liquor, brought about by the removing the 8 per cent limit, would be unlikely to have a significant impact on total consumption.

The report commented that issues concerning threats of monopoly are better dealt with through the *Trade Practices Act* than through industry specific legislation.

The Council's considerations: the 8 per cent limit

There is no doubt that, as the Victorian Government argues, underage drinking is a significant issue for the community. However, there is little conclusive evidence provided to support the view that restricting the number of off-licences held by one organisation to 8 per cent of the total, which affects in practice only the two major supermarket chains, will achieve the objective of reducing alcohol abuse by underage drinkers.

The data on juvenile prosecutions in Victoria relating to alcohol abuse, referred to in the Government's annual report, do not provide any evidence on location of offence or the source of the liquor consumed. They do not necessarily support that contention that supermarkets are a major contributor to juvenile alcohol abuse.

The Victoria Police argued that the potential for binge drinking provides a case for closer supervision of alcohol sales by off-licence venues relative to licensed premises, given that binge drinking cannot occur lawfully on licensed premises (Victoria Police 1998, p. 5). The Council fully accepts this argument. However, any link between alcohol sales by supermarkets and underage drinking and binge drinking appears to have little, if any, relevance to the 8 per cent rule. Consideration of the evidence before the Review suggests that the 8 per cent rule does not achieve the objective of minimising underage consumption for the following reasons.

- Only the two large supermarket chains, Liquorland and Safeway, are affected by the 8 per cent rule. The rule does not apply in practice to smaller chains and independent liquor stores (because they do not have sufficient market share) or to buying groups, some of which hold in excess of 8 per cent of licences. Neither does it apply to hotels, having been removed for General Licences on the ground that it has no effect in practice.
- Both the large chains are acknowledged to be responsible sellers of alcohol. For example, Victoria's Review stated that Liquorland and Safeway "are

acknowledged by the Victoria Police as being amongst the overwhelming majority of packaged liquor licensees who are responsible sellers of alcohol." (*Liquor Control Act 1987* Review 1998, p. 76)

- The Review found that an increase in the general availability of liquor, brought about by the removing the 8 per cent rule, would be unlikely to have a significant impact on total consumption. It cited, among other things, evidence from New Zealand, where aggregate alcohol consumption levels have steadily declined (by nearly 18 per cent over 10 years) despite an increase in the number of liquor licences from 6 247 in 1988 to 11 048 in 1996 (*Liquor Control Act 1987* Review 1998, p. 120).

- The logical interpretation of comments that availability of liquor through various off-licence outlets is a contributory factor to underage drinking would suggest that the key public policy objective ought to be to limit the total number of off-licences (in contrast to the generally deregulatory action taken by the Victorian Government). However, retaining the 8 per cent limit on off-licences does not limit the total number of outlets, at most it limits the number which can be owned by one organisation.

- Removing the 8 per cent rule may even help to minimise problems due to underage consumption, given the large supermarket chains' established records for responsible selling of alcohol, if it results in liquor stores operated by the large chains replacing smaller independent sellers, as controls on sales would be tightened.

Thus, it appears that the primary objective for the retention of the 8 per cent limit is to shield existing holders of packaged-liquor licences from competitive pressures that would arise if the two major supermarket retailers were allowed to expand. This is emphasised by the then Minister's statement in May 1983, when the rule first became law. The Minister commented that the limit was a safeguard "*... to prevent domination of the liquor industry in the long term by hotel chains and supermarket chains*." Victoria's 1998 Review confirms that:

> *the price of packaged liquor in the industry with the 8% rule would be higher relative to the price of packaged liquor without the 8% rule.*

Available evidence casts doubt on whether removal of the limit would lead to unacceptable retail concentration as alleged by Victoria. In New South Wales, where there are no restrictions on the number of licences which can be held, the two supermarket chains between them hold only 22.6 per cent of all packaged liquor licences, in comparison with 15.5 per cent in Victoria where the limit applies. Moreover, holders of General Licences such as hotels sell considerable volumes of packaged liquor. Thus, the percentage of packaged liquor licences held by the two supermarket chains overstates their relative share of the total packaged liquor market. In any case, as recognised by Victoria's Review, the TPA is a better mechanism for dealing with any unacceptable concentration in packaged liquor retailing.

As also recognised by the Review, removal of the 8 per cent rule is likely to lead to a reduction in prices, as cost savings from greater competition are passed onto

consumers. The Council considers that the potential increase in competitive pressure could be significant as evidenced by Liquorland's recent application to increase the number of its licences for packaged liquor by 69, from 89 to 158.[25] Apart from reduced prices, there are also intangible benefits which could also be expected to flow from abolition of the 8 per cent limit including, for example, greater availability of outlets, a broader range of products and improvements in customer service.

Conclusion and recommendation

The Council acknowledges that there have been substantial reforms to liquor licensing arrangements in Victoria, and that arrangements in general are now less restricted than in other jurisdictions. However, the Council is not convinced that the Government has demonstrated a sufficient public benefit case to support retention of the 8 per cent rule, particularly given the Review recommendation advocating removal of the restriction. Evidence provided by Victoria, while addressing relevant NCP public interest factors, does little to support an argument that the rule is necessary to limit underage drinking or that there is a net community benefit in shielding existing holders of packaged liquor licences from greater competition.

The Council concludes that, for Victoria to be considered as complying with its NCP obligations, the Government will need to remove the 8 per cent limit from its liquor licensing legislation in line with the recommendation of its Review. Given that the Review provides no specific date for removal, the Council considers the provisions of the CPA, which require the removal of unjustified restrictions by the end of the year 2000, should apply. The Council will consider an annual deduction from Victoria's NCP payments if Victoria does not remove the 8 per cent rule by 31 December 2000.

The Council's considerations: liquor sales by convenience stores and other venues:

Victoria's Review recommended that the prohibition on licensing cinemas, petrol stations, milk bars, convenience stores and mixed businesses remain. It was unable to identify a reasonable alternative non-regulatory means of achieving the "adequate controls" objective of the legislation that the prohibition seeks to address.

The evidence to support retention of the prohibition is not clear cut. For example, the Review found the primary objection to licensing convenience stores and other businesses to be that they are places frequently visited by families and, in particular, unaccompanied minors, but stated that no evidence was presented to suggest that well-run convenience stores are more likely to sell alcohol to minors than are other licensees. The Review also considered that licensing petrol stations may send the wrong message to the community concerning drink driving, but was not fully convinced that licensing petrol stations, subject to appropriate conditions, would in fact lead to a significant increase in drink driving (*Liquor Control Act 1987* Review 1998, pp. 70-74). The Victorian Government stressed that social objectives – especially reducing drug abuse by youth and reducing drink driving – support its decision to retain the licensing prohibition on convenience stores and other venues.

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[25] Liquorland applied for the additional licences on the basis that its share at the time its application was made was less than 8 per cent, in line with what appears to be the approach taken until recently by the Liquor Licensing Commission.

While the evidence may be equivocal, the Council does not believe that the Review's recommendations, or the Victorian Government's policy response, is unreasonable. As this was a bona fide review, the Council accepts the balance of the arguments regarding the overall benefits to the community from retaining some restrictions on the premises that can supply packaged liquor. The Council considers that Victoria has complied with its NCP obligations in retaining the restriction on liquor licensing in respect of premises such as cinemas, petrol stations, convenience stores and milk bars.

Liquor Licensing Act 1985 (South Australia)

Following an NCP Review in 1996, South Australia removed several restrictions on the sale of alcohol. For example, the licensing authority no longer may take account of the impact of a new licensee on existing licence holders. These changes were incorporated in the new *Liquor Licensing Act 1997*, which came into operation on 1 October 1997.

However, consistent with the Review recommendations, the new Act also retained a number of restrictions, including:

- restrictions on the types of outlets that can retail liquor, that is, only hotels and retail liquor stores devoted entirely to selling alcohol are able to sell packaged liquor; and

- a 'proof-of-need' requirement for hotels and bottle shops – applicants for licences must demonstrate that the licence is necessary to meet the needs of consumers in the locality.

The justification for these restrictions, given by the Review, is that they are necessary to prevent a proliferation of liquor outlets. Indeed, in considering the recommendations of the Review, the South Australian Government stated that it saw retention of the needs test as an appropriate balance of the competing demands of all the community.

Nonetheless, the Government noted that the Review qualified its recommendations by proposing a further examination of liquor licensing arrangements in three to four years. In accordance with this, the Government proposes to review the desirability of retaining the 'proof-of-need' criterion at the end of the year 2000 or early 2001, although this would not be a full review of the 1997 legislation.

Assessment

The Council is not convinced that restricting licences for the sale of packaged liquor to hotels and bottle shops, for example, preventing establishments such as supermarkets from selling packaged liquor, is necessarily the best way to minimise harm from misuse of alcohol. As shown by Victoria's review, many operators other than hotels and liquor stores selling alcohol only, are likely to be capable of managing the sale of packaged alcohol in a way which meets community objectives about its use. Similarly, the 'proof-of-need' criterion inevitably impacts on the commercial interests of existing and potential licensees, restricting competition and reducing convenience for consumers especially in relation to packaged liquor sales.

However, the net public benefit of allowing liquor sales by outlets such as convenience stores and petrol stations is not clearly established. As discussed in the section above relating to Victoria's liquor licensing changes, evidence from the police and alcohol and drugs agencies suggests that preventing outlets such as convenience stores and petrol stations from selling alcohol may be in the community interest. On the other hand, the Victorian review found little evidence of harm arising in the ACT, where supermarkets can sell packaged liquor. Overall, the Council's view is that the evidence may support the approach being taken by both South Australia and Victoria, following their reviews, in retaining restrictions on these types of outlets.

The case in favour of 'proof-of-need' as a licensing criterion is less clear. South Australia's Review opted for retention with further review when the community impacts of less regulated approaches in other jurisdictions are clearer. Victoria has already removed the requirement to prove need following the finding by its Review that removal would primarily change the pattern of sales, reflecting customer demand and convenience, rather than impact significantly on alcohol consumption and problems from misuse.

In assessing NCP compliance, it is relevant to take into account that the South Australian Government has agreed to reconsider the case for retaining the needs criterion in late 2000 or early 2001. This is within four years of the date that the current Act became operational and thus is broadly in line with the timeframe recommended by South Australia's NCP Review for reconsideration of restrictions. In these circumstances, the Council assesses South Australia as meeting its second tranche NCP obligations on liquor licensing. The Council will take into account progress towards establishing the further review of the 'proof-of-need' criterion achieved by South Australia in its third tranche assessment.

B5.4.5 Third party motor vehicle insurance

Background

Each jurisdiction operates its own legislated compulsory scheme to cover costs associated with personal injuries resulting from motor vehicle accidents.

The regulatory environment governing delivery of compulsory third party (CTP) insurance varies significantly across jurisdictions. In two states, New South Wales and Queensland, private sector providers compete to provide CTP cover. In the other jurisdictions CTP insurance is provided by monopolies. In all but the ACT these are government-owned statutory monopolies. The ACT legislation provides for any qualified insurer to seek ministerial approval to provide CTP services. However, in practice, a single company provides cover.

Premium setting in all jurisdictions is subject to some form of regulation or oversight. In New South Wales, insurers propose the premium they intend to charge and file the premium with the Motor Accidents Authority (MAA). The MAA can reject the premium if it considers it excessive or inadequate to fully fund liabilities or if the premium does not comply with certain conditions. The Motor Accidents Insurance Commission in Queensland recommends premiums to the Government following actuarial advice and submissions from insurers. In all other jurisdictions, except Tasmania, the monopoly provider recommends premiums to the Government for

approval. In Tasmania, the Government Prices Oversight Commission (GPOC) recommends maximum premiums to the Government, following a review process involving public consultation.

Legislation also determines the nature of the product – that is, the terms of cover, the basis for determining compensation and eligibility for compensation. Supplementary activities often associated with CTP, such as accident prevention schemes, are either performed by the monopoly or, where there is competitive delivery, by an independent oversight authority, with funding from all CTP insurance providers.

Current status of reviews of CTP legislation

All governments, except the ACT, have scheduled relevant legislation for review. The ACT is not reviewing its legislation, on the grounds that it already provides for competitive delivery of CTP services.

Reviews have been completed in New South Wales, Victoria, Tasmania and the Northern Territory. In Western Australia, the review was close to finalisation at the end of June 1999. The Northern Territory is proposing an additional review to extend the coverage and independence of the earlier process. Therefore, at this stage, only New South Wales, Victoria and Tasmania are subject to assessment under the second tranche for CTP. Table B5.5 below outlines the current position.

New South Wales has recently announced a suite of new measures to amend aspects of its current legislation. The headline announcement is for a $100 reduction in the cost of green slips. This will be funded largely by reducing the costs of the scheme through greater controls over legal and medical costs. Claimants will have to refer disputes over medical issues to a single panel and general disputes to a Claims Assessment and Resolution Service. In addition premiums will be more risk related.

The actions being taken by New South Wales are consistent with its second tranche NCP obligations on this matter, given the existing deregulated arrangements and the recently introduced changes, which should simplify claims processing. The second tranche assessment, therefore, concentrates on the Victorian Transport Accident Compensation Legislation, the Tasmanian *Motor Accidents (Liabilities & Compensation) Act 1973* and the Northern Territory's *Motor Accidents (Compensation) Act* and *Territory Insurance Office Act*.

Transport Accident Compensation Legislation (Victoria)

Victoria's Review of its transport accident compensation legislation identified three main restrictions on competition:

- the scheme is compulsory for all registered vehicles;
- the Transport Accident Commission (TAC) has a statutory monopoly over the provision and administration of no–fault transport accident compensation in Victoria; and
- premiums are set by regulation.

The Review found there is a net community benefit from the compulsory nature of the scheme, although it did not investigate whether there is a viable alternative. It recommended no change to this aspect of the scheme.

Table B5.5 Progress with reviews of compulsory third party insurance legislation by jurisdiction, at 30 June 1999

	Legislation	Review and Reform Status
New South Wales	*Motor Accidents Act 1988 & Motor Vehicles (Third Party Insurance) Act 1942*	Review completed in 1998. Recent announcement provides for $100 reduction in premiums, risk based premiums and claims resolution mechanisms.
Victoria	*Transport Accident Compensation Legislation*	Review of Transport Accident Compensation legislation by Department of Treasury and Finance in 1997-98. Review found a found net benefit from compulsory scheme but significant costs associated with monopoly provision. The review recommended removal of statutory price setting provisions, introduction of risk reflective premiums and the separation of commercial, regulatory and other non-commercial functions. The Government announced in October 1998 that it would retain the main features of the existing scheme.
Queensland	*Motor Accident Insurance Act 1994*	A major review has commenced, including NCP issues.
Western Australia	*Motor Vehicle (Third Party Insurance) Act 1943* and regulations	Review is expected to be completed in June 1999. Completion date deferred from July 1998 to enable additional consultation and to address issues raised by NCC.
South Australia	*Motor Accidents Commission Act*	Review underway.
Tasmania	*Motor Accidents (Liabilities & Compensation) Act 1973*	Review completed October 1997. Recommended that the Motor Accidents Insurance Board should continue to operate as a monopoly provider and that the power of the Board to enter arrangements with other insurers be replaced with a power only to reinsure. Recommendations accepted by the Tasmanian Government in December 1998.
ACT		No review scheduled as legislation provides for competitive arrangements.
Northern Territory	*Motor Accidents (Compensation) Act & Territory Insurance Office Act.*	Internal review completed by Territory Insurance Office. The Northern Territory is finalising the terms for a wider external review.

Source: Jurisdictions' Annual Reports (1999)

The Review concluded that, on balance, there are significant costs associated with the monopoly. These costs include reduced incentive for suppliers to innovate and improve performance, or to reduce costs and prices, and constraints on consumer sovereignty. The Review recommended that statutory price setting be discontinued and risk reflective premiums be introduced, and that the TAC's commercial activities be separated from its regulatory and non-commercial functions.

The Government did not accept the majority of the Review's recommendations. The Government believes that a competitive model with compulsory coverage, lifetime care and community ratings would involve substantial on-going regulatory costs. Furthermore, while it agreed that the TAC premiums do not reflect risk (and therefore offer little incentive for those at risk to modify their driving behaviour), it was not persuaded that a strictly risk-reflective premium structure is required by the objectives of the scheme.

The Government stated that it did not release the review for public comment prior to making its decision, as it had already reviewed the scheme in its first term in office (1992 to 1996), although it acknowledged that the earlier review did not consider NCP matters.

Assessment

The Council questions whether Victoria has fully met its NCP obligations in relation to traffic accident compensation arrangements. The Council's concern arises from the disparity between the recommendations of Victoria's Review and the program implemented by the Government. Victoria's annual NCP report does not provide convincing evidence to rebut the Review's recommendations and justify the disparity.

The Council considers that Victoria should review its current position regarding arrangements for the delivery of CTP insurance. In view of this, and emerging questions about CTP review processes and outcomes in other jurisdictions, the Council considers the best way forward would be by way of a national review of CTP, conducted by an independent body with recognised expertise.

Victoria has indicated that it is willing to co-operate with a review by the Productivity Commission, possibly commissioned by the Council, of the different regimes provision of CTP for motor vehicles in Australia. This review would examine the approaches to, and performance of, regulation of transport accident insurance in the States and Territories, and provide recommendations on the appropriate level of competition in the provision of these services. The review might also consider any national issues which State and Territory reviews have not, or could not, address.

Victoria's agreement to such a review constitutes satisfactory compliance with its second tranche NCP obligations on this matter.

Motor Accidents (Liabilities and Compensation) Act 1973 (Tasmania)

A review of the *Motor Accidents (Liabilities and Compensation) Act 1973* was undertaken during 1997. The Review focussed on the statutory monopoly and the power of the Motor Accidents Insurance Board (MAIB) to enter arrangements with other insurers. A three-person team, including the Executive Officer of the MAIB, conducted the review.

The Review found that the statutory monopoly was justified and recommended its retention, noting that:

- premiums would be higher under a competitive model, because of additional costs faced by new entrants, and the need to fund an industry regulator and a scheme to cater for uninsured or unidentified vehicles;
- comparisons of cost of claims processed by MAIB and by New South Wales insurers did not support suggestions that competition would reduce premiums;
- while higher premiums might be acceptable if there is product innovation, the product in this case is defined by statute preventing innovation; and
- the size of the Tasmanian market precludes more than two providers, leading to potential oligopoly.

The Tasmanian Government accepted the review recommendations in December 1998.

Assessment

The Council considers that the close links between the Review Group and the MAIB, the provider of CTP in Tasmania, cast doubt on the weight of the Review Group's argument to support retention of the MAIB monopoly.

The Council raised the matter of the lack of independence of the Review Group with Tasmania during the assessment process. Tasmania argued that, at the time the Review was established, the Council's views of the importance of independent panels had not been expressed publicly. Tasmania also considered its review process had strong compensatory elements. For example, the Government indicated there had been considerable public consultation, including with industry participants. Thus, Tasmania argued that it met the provisions of the CPA on this matter.

While acknowledging that the Council's views on the importance of independent processes were not made available until after the establishment of Tasmania's Review, the Council considers that the matter of independence is relevant in this case. The Council understands, for example, that the MAIB, which was represented on the Review Group, made a submission prior to the commencement of the Review, which argued that the current arrangement should not be changed. Similarly, the Council understands that the Tasmanian Law Society, to which the barrister/solicitor on the Review Group has a close connection, provided a paper to the review arguing that there is no basis for any change to current arrangements.

In the light of the process adopted for this review, the Council believes that the finding that premiums would be higher under a competitive model warrants further examination. For example, premiums in a competitive market might in fact be much lower than estimated by the Review Group for several reasons.

- New entrant costs might, in practice, be quite low, as private insurers are likely to enter the CTP market on the basis of their existing infrastructure and advertising arrangements. That is, many potential participants would face a marginal cost of entry rather than full start-up costs.

- It is true that in New South Wales and Queensland, where there is competitive provision of CTP services, an industry regulator oversees pricing, monitors scheme arrangements and acts as conduit to the Government. However, these would not be entirely new functions or costs for Tasmania in the event of change. Government resources are already devoted to determination of premiums (including price regulation by the Government Prices Oversight Commission), prudential oversight, management of the MAIB, and payment of Commonwealth and State taxes and charges. To suggest that significantly higher costs would be associated with an industry regulator would imply that these functions are currently not being undertaken in Tasmania.

- In competitive markets in other jurisdictions, claims made in respect of uninsured or unidentified vehicles are allocated across all insurers according to market share. This is unlikely to impact greatly on premiums.

- Premiums can be readily collected and distributed through the motor vehicle registration system. For example, in Queensland, the registration system collects the insurance premiums and remits to the relevant insurer. This is a relatively simple computer-based operation.

- Evidence from Queensland and New South Wales suggests that the small market size and potential oligopoly argument raised by the Tasmanian Review Group is also doubtful. In both New South Wales and Queensland, there are operators with smaller market share than the Tasmanian market. In any case, problems relating to oligopolistic pricing may be better addressed through scheme design/regulation than by requiring monopoly supply.

- There is evidence from relevant bodies such as the Insurance Council of Australia which casts doubt on the administration cost comparisons for the six major CTP jurisdictions in Australia used by Tasmania’s Review Group to support its claims about likely premiums under a competitive arrangement.

Given the questions about the independence of the review process and the recommendations of the Review Group, the Council does not consider that Tasmania’s review and reform action relating to CTP arrangements for motor vehicles sufficiently addresses the State’s NCP obligations. In line with the recommendation regarding the position in Victoria, the Council considers that an appropriate way forward would be through a national review by the PC of arrangements for CTP for motor vehicles.

The Tasmanian Government has indicated support for an independent review by the PC of national CTP arrangements but stated that it will not necessarily be bound by the outcome of such a review. On the basis of the Government's support for further consideration, the Council assesses Tasmania as complying with its second tranche NCP obligations on this matter.

Motor Accidents (Compensation) Act and Territory Insurance Office Act (Northern Territory)

The *Motor Accidents (Compensation) Act* establishes a no-fault third party compensation scheme, prescribes rates of benefit and abolishes certain common law rights. The *Territory Insurance Office Act* establishes the Territory Insurance Office (TIO) to provide certain insurance, financial and related services. The Act confers a monopoly on the TIO as provider of motor vehicle accident CTP insurance. The TIO also acts as the insurer of Territory assets and liabilities.

The Northern Territory has undertaken an internal review (involving the TIO) of legislation governing the operation of the TIO. The recommendations of this review, and the Northern Territory Government's decision in response, have not been reported in detail. However, following criticisms by the insurance industry of similar reviews in other jurisdictions, the Northern Territory Government agreed to reconsider its position. The Government has now decided to hold a further review, which will have a more extensive brief, covering a range of activities for which the TIO is responsible and involving an appropriately independent process. The Territory is also considering the possible coordination of this exercise and any national review of CTP as proposed above.

The Council considers that the program for further review of the role of the TIO proposed by the Northern Territory Government complies with second tranche obligations.

B5.4.6 Workers' compensation arrangements

Background

Workers' compensation insurance is a compulsory arrangement, whereby employers purchase insurance policies from authorised insurers on behalf of employees. In each State/Territory, a public monopoly provider administers the workers' compensation scheme.

There are significant restrictions on competition where the entire process is provided through a single state-based monopoly supplier covering all aspects of the scheme.

Current status of reviews of workers' compensation legislation

Legislation review and reform performance for the second tranche of NCP is relevant only for New South Wales and Victoria. In all other jurisdictions, workers' compensation legislation is scheduled for review during the period of the third tranche. Table B5.6 below summarises review status across all jurisdictions.

In New South Wales, a major inquiry into the workers' compensation system was launched in April 1997, prompted by an accumulating deficit in the workers

compensation scheme. The report of that inquiry, by Richard Grellman, was issued in September 1997. This led to the passing of the *Workplace Injury Management and Workers Compensation Act 1998* and the cognate *Workers Compensation Legislation Amendment Act 1998,* the majority of which came into effect in August and September 1998.

As a result, as from October 1999, the workers' compensation system in New South Wales will be privately underwritten. There will be a Rating Bureau, which will develop a methodology for the setting of premiums and a process for review of that methodology by WorkCover. The premium payable by employers is to be set on the basis that fully funds claim liabilities. There is provision to keep the average premium rate of 2.8 per cent for a period of up to 12 months after private underwriting is introduced. WorkCover will, therefore, license insurance companies to offer services and run schemes that are compliant with minimum criteria. Processes will be in place to limit the costs of disputes through formal mediation reviews and medical panels.

In Victoria, a review by the Department of Treasury and Finance recommended that the Victorian WorkCover Authority (VWA) monopoly should cease and a competitive scheme be introduced. The Review did not outline a proposal for a competitive scheme. However, the Victorian Government decided to retain monopoly delivery through the VWA.

Table B5.6 Progress with reviews of workers' compensation legislation by jurisdiction, at 30 June 1999

	Review and Reform Status
New South Wales	Review completed. Review recommended that a private sector, competitive scheme be introduced. Government has adopted this approach in legislation that is currently being implemented.
Victoria	Review by Department of Treasury and Finance recommended that the Victorian WorkCover Authority monopoly should cease and a competitive scheme be introduced. The review did not outline a proposal for a competitive scheme. The Victorian Government decided to retain monopoly delivery through the VWA.
Queensland	Review of the *Workcover (Queensland) Act 1996* scheduled for 2000.
Western Australia	Review of *Worker's Compensation and Rehabilitation Act 1983* expected to be completed in June 1999.
South Australia	Review of *Workers Rehabilitation and Compensation Act 1986* is scheduled for 1999.
Tasmania	Joint Select Committee review of the *Workers' Rehabilitation and Compensation Act 1988* reported in May 1998. Government considering response.
ACT	Review of the *Workers Compensation Act 1951* and the *Workers Compensation Fund Supplementation Act 1980* currently underway.

	Review and Reform Status
Northern Territory	Review of the *Work Health Act* and the Occupational Health and Safety Regulations is underway.

Source: Jurisdictions' Annual Reports (1999)

Assessment

New South Wales

The Council considers that review and reform action taken by New South Wales complies with CPA obligations, as it provides for competitive, market choice of insurer for employers, within a compulsory statutory framework.

Victoria

The Department of Treasury and Finance Review of Victoria's workers' compensation arrangements made eight recommendations, including the primary recommendation that the Victorian WorkCover Authority (VWA) cease to provide insurance and that all underwriting risks be borne by private insurers. The Review also recommended introduction of decentralised competitive premium setting and that insurers be subject to independent regulation and prudential requirements.

The Victorian Government rejected most of the Review's recommendations, including the primary recommendation for private delivery of workers' compensation insurance through a competitive model. Victoria referred to the substantial benefits which have flowed from reforms to workplace accident arrangements in the existing Workcover scheme, and to the success of integrated schemes overseas, to support its case. Victoria stated that these benefits include low and stable premiums and a greater ability to capture the benefits of investment in accident prevention and long term rehabilitation.

Victoria also believes that, in a competitive market, the objective of affordable universal coverage could not be achieved without significant regulation to enforce and subsidise universal coverage, either directly or through an insurer of last resort. The Government argued that investor pressure on private insurers means they are less able to manage the benefit structure, which focuses on long term rehabilitation and return to work and as a result has a significantly increased liability tail (due to restrictions on common law actions). The Government considered that heavy-handed regulation, involving potentially high compliance costs, would be necessary to deliver the objectives of its workers' compensation legislation through a system of competing private insurers.

Victoria did acknowledge the benefits associated with premiums that are more risk reflective. It noted there may be (limited) means of ensuring premiums are more reflective of risk and stated that it intended to introduce greater flexibility to enable insurers to compete on administrative costs. However, the Government's acceptance of this recommendation was tempered by concerns about premium volatility.

The recommendation by Victoria's Review supporting a competitive approach to the delivery of worker's compensation, and the recent pro-competitive developments in New South Wales, raise a question for the Council as to whether Victoria's decision to retain the VWA monopoly fully addresses NCP obligations. Given the disparity in the two States' approaches, and that all other jurisdictions will confront similar questions, the Council considers the best way forward would be through a national review conducted by an independent body with recognised expertise.

As it has for its CTP arrangements, Victoria indicated that it is willing to co-operate with a review by the PC, possibly commissioned by the Council, of the different regimes for regulating workers' compensation. Victoria's agreement to such a review constitutes satisfactory compliance with its second tranche NCP obligations on this matter.

B5.4.7 Professional indemnity insurance for legal practitioners

Background

Professional indemnity (PI) insurance is compulsory for all solicitors throughout Australia, because of the perceived risks to consumers of legal services of allowing lawyers to practice without insurance. This insurance provides a means of funding claims from clients of solicitors who allege loss as a result of negligence in how their legal affairs are handled. Losses from fraud or mismanagement of funds held on behalf of clients are normally dealt with through separate (fidelity) arrangements.

Historically, compulsory PI insurance for solicitors has been delivered by a monopoly provider, either through:

- a single Master Plan negotiated with a commercial insurer, which provides a policy under which all solicitors are covered; or
- an independent mutual fund, with a levy on all solicitors within the relevant region.

Both approaches are recognised to have strengths and weaknesses for the profession itself and neither is without risk. For example, Master Plans have demonstrated dramatic increases in their premmie, whilst mutual funds can find themselves without the resources required to cover outstanding claims, as happened in the United Kingdom in 1997.

More recently, some jurisdictions are allowing individual lawyers to choose their own insurer on the open market – normally with the proviso that the policy has to meet certain minimum criteria. This is the approach adopted for the insurance of barristers in New South Wales and lawyers more generally in New Zealand. Although PI insurance is not compulsory for lawyers practising in New Zealand, around 95 per cent of lawyers do hold such cover.

State and Territory reviews of professional indemnity insurance legislation

Apart from the ACT, which has deregulated its market to allow two approved insurers, all other jurisdictions require legal practitioners to take out PI insurance through a single provider of professional indemnity insurance cover.[26]

New South Wales has completed an NCP review of its *Legal Profession Act 1987*. This review included an assessment of PI insurance arrangements for solicitors and recommended deregulation, subject to certain constraints. The report was tabled in the New South Wales Parliament in November 1998 but is still to be formally considered by Cabinet.

Victoria has taken a number of actions on PI insurance. Following an NCP-based review in 1996, Victoria legislated to allow lawyers a choice, after a transition period, as to whether to insure with the Legal Practitioners Liability Committee (LPLC) or through other commercial insurers. Subsequently, however, following a review undertaken by the Legal Practice Board (LPB), Victoria reversed this decision and amended its legislation to confirm the existing statutory monopoly.

Apart from the ACT, which has completed its review and partially deregulated its market, the Council's primary focus for this assessment is on Victoria's *Legal Practice (Amendment) Act 1998*, which retains the statutory monopoly. Because of the timing of their review and reform activity, all other jurisdictions will be assessed as part of the third tranche. Table B5.7 summarises the status of jurisdictions' reviews at 30 June 1999.

Table B5.7 Progress with legislation providing for professional indemnity insurance for legal practitioners by jurisdiction, at 30 June 1999

	Review and Reform Status
New South Wales	Review completed. Report tabled in Parliament in November 1998. It is unlikely that Cabinet will consider the report before the end of June 1999.
Victoria	Review, following NCP principles, recommended the introduction of competitive arrangements. The *Legal Practice Act 1996* provided for competitive arrangements for legal indemnity insurance, with a sunset date, for the previous monopoly, of 1 January 1999. A further review by the Legal Practice Board (June 1998) recommended that the monopoly continue and that the reforms in the *Legal Practice Act 1996* not proceed. The Government passed the *Legal Practice (Amendment) Act 1998* that continues the monopoly.
Queensland	Review of the *Queensland Law Society Act 1952* and the *Queensland Law Society (Indemnity) Rule 1987* is pending.
Western Australia	Review of *Legal Practitioners Act 1893* and Rules rescheduled to March 2000.

[26] PI insurance for barristers in New South Wales is open to the market.

	Review and Reform Status
South Australia	Review of the *Legal Practitioners Act 1981* is currently underway.
Tasmania	Review of the *Legal Profession Act 1993* is to commence later in 1999.
ACT	Review completed. The ACT has a partially deregulated market with two insurers approved.
Northern Territory	*Legal Practitioners Act* to be reviewed as part of development of a national market for legal services. However, PI issues will be reviewed separately by the end of 2000.

Source: Jurisdictions' Annual Reports (1999)

Victoria's Legal Practice Act 1996 and Legal Practice (Amendment) Act 1998

Victoria's *Legal Practice Act 1996* provided for, among other things, competitive delivery of legal PI insurance by allowing legal practitioners the right to insure either with the Legal Practitioners Liability Committee (LPLC) or another insurer of their choice. The LPB would set the minimum conditions for all insurance policies. Under the Act, the monopoly was to sunset on 1 January 1999. In the interim, the LPLC was to continue as the monopoly provider of PI cover and the LPB was to review its future operation.

The LPB's report to the Victorian Government, in June 1998, disagreed with this position and recommended that the LPLC's statutory monopoly on supply of compulsory PI insurance continue, and that the reforms envisaged under the *Legal Practice Act 1996* not proceed. As a result of this advice, Victoria passed the *Legal Practice (Amendment) Act 1998* to confirm and extend the statutory monopoly indefinitely.

Analysis of Competition Issues

The NCP tests for assessing such restrictions under clause 5 of the CPA cover two elements:

- that the benefits of the restrictions to the community as a whole outweigh the costs (the net benefit test); and
- that the objectives of the legislation can only be achieved by restricting competition (the alternative means test).

The LPB's Review found that the monopoly provides a net benefit to the community. It noted reports from external consultants to the LPB, which advised that:

- premiums under a statutory monopoly would be cheaper than those under a commercial arrangement, in the long term;
- the monopoly could provide greater premium stability than the commercial market, over the long term; and

- a monopoly fund would cover elements of the legal services market, such as smaller operators, retired solicitors who are insolvent, deceased practitioners, disbanded partnerships or disgraced solicitors who are struck off, which the commercial market would not cover.

As required under the CPA, the LPB Review also considered alternative means for achieving the objectives of the legislation. It considered that the objectives are to ensure protection for all consumers of legal services, to ensure consumer access to economic and convenient services including sole practitioners, and to ensure that competition within the legal services market is not reduced by the inability of a practitioner to obtain insurance coverage. The review found all alternatives to the monopoly to be deficient and concluded that an open market would not achieve the objectives of the legislation.

There is considerable evidence that supports an alternative approach to that recommended by the LPB Review. For example, in relation to the net benefit associated with restrictions on competition in this area, the New South Wales' NCP Review of the State's *Legal Profession Act 1987* took the following evidence.

- Willis Corroon Professional Services Limited indicated that its experience, as the agent of insurers entering the market in the ACT, was that competition led to broader cover, cheaper premiums and a higher level of service.

- PI insurance for barristers in New South Wales is open to the market. The Bar Association of New South Wales indicated that the threat to clients posed by an insurer ceasing to operate was more apparent than real. The Bar Association also stated that, to its knowledge, no barrister had been refused cover as a bad risk and believed that any such barrister would probably obtain cover, albeit at a higher premium.

- The ACCC argued that the insurance market is large enough to accommodate any practitioner and that in any case, the threat of losing insurance would provide an incentive to solicitors to provide better customer service. Similarly, the New South Wales Council on Social Service considered that it is in the best interests of the profession and the public for the market to be deregulated.

The New South Wales NCP Review concluded that:

> *The provision of a choice of insurers for solicitors would be likely to engender competition in the market for PI insurance, reducing the costs of legal practice.*

It recommended that:

> *deregulation of the market for professional indemnity insurance for solicitors should take place, subject to appropriate protection for clients being addressed, through minimum standards for policies, run-off and indemnity.* (New South Wales Attorney General's Department 1998)

Available evidence in other jurisdictions also raises doubt about the conclusion reached by the LPB. The ACT has partially deregulated its arrangements and there are now two approved insurers. Within Victoria itself, there is a competitive market delivering top-up indemnity insurance above the compulsory minimum. Under the fully competitive arrangements in New Zealand, premiums for sole practitioners and new entrants are set on the basis that they are good risks (until experience shows otherwise). Run-off cover is purchased on a diminishing scale from 100 per cent of fees to 50 per cent, diminishing at 15 per cent a year. There are minimum criteria for insurance that were developed following a review in 1993, which have been adopted as a voluntary industry standard.

Similarly, the available evidence suggests that potential (competitive) alternatives to the statutory monopoly are available, including:

- an open market for legal PI insurance as exists in New Zealand and Ireland (where a mutual fund also operates), potentially supplemented by external minimum standards;

- a single insurer selected for a defined period through a competitive tender process;

- a regime whereby practitioners can limit liability where they have sufficient assets to meet compensation at a required level; and

- a risk weighting scheme whereby insurers are required to accept all proposals, with a limit set on the maximum and minimum premia, such as the model for CTP insurance in New South Wales.

Moreover, the market-based approach appears to have general support within the profession. For example:

- in New Zealand, where lawyers rejected a proposal in 1993 to move from the competitive model to a master policy scheme;[27] and

- in the United Kingdom, where a recent ballot of the Law Society indicated a large majority of solicitors in favour of the right to choose their insurer on the open market (Law Society of England and Wales 1999). The outcome of this ballot contrasts with the recent decision of the United Kingdom Law Society to retain the statutory monopoly fund.

One important consideration in assessing the net benefit of the different arrangements for the delivery of PI insurance is the potential cost to the community of high risk behaviour, given that the statutory scheme is ultimately underwritten by its members. The ballot of solicitors in the United Kingdom was taken following the failure of its Mutual Fund in 1997, due to "*the very substantial shortfall between the contributions so far collected and the likely costs of claims*." The United Kingdom Law Society blamed the failure on the situation where "*the comfort factor is too great – leading a*

[27] Personal Communication, Austin Forbes QC, Christchurch, New Zealand, President of the New Zealand Law Society 1994.

small number of firms to fail to adopt proper risk management systems, relying on the rest of the profession to bail them out" (Law Society of England and Wales 1998, para. 1.5).

Premium setting which is more reflective of risk than the current arrangement would reduce the potential financial demand on the community. Indeed, the LPLC has adopted more risk-related premiums since 1996. It also fully employs opportunities for re-insurance in order to spread that risk. Studies have identified further options to address this issue, including the establishment of an assigned risk pool funded by the market, which would enable higher risk lawyers to obtain cover although at a higher premium. The Insurance Council of Australia has indicated to the Council that, in anticipation of the introduction of competition, several insurers are preparing schemes that do not envisage premium increases, except for firms with poor claims histories.

Finally, the concept of the legal profession as a single distinct discipline, which ought to share risk solely within itself, is becoming less relevant with the growth of multi-service consultancy companies providing a coordinated suite of business services covering law, accounting, finance, economics, management and strategic development etc. The legal element within any consultancy advice is unlikely to readily distinguishable, and it is not always clear that legal issues are necessarily more complex or risky than those relating to, say, financial or strategic advice.

Assessment

There is evidence to suggest that the argument contained in the LPB Review and in Victoria's annual report may not fully address the legislation review competition tests within the CPA. The experience in other countries and conclusions reached by other Australian reviews tends to suggest that competitive delivery presents a workable alternative to the monopoly and that there are likely to be benefits from introducing competition. Indeed, Victoria's own earlier NCP Review, which led to the *Legal Practice Act 1996,* supported a more competitive arrangement.

The decision to retain the monopoly was taken on the basis of recommendations by the LPB, a body with representation from a number of bodies including lawyers. While making no comment on objectivity in this case, the Council notes that the earlier pro-competitive reforms encompassed within Victoria's *Legal Practice Act 1996* followed a review process which was to a large extent independent of (but working in consultation with) legal industry representatives. The equivalent New South Wales Review which supported competitive delivery, although undertaken by the Attorney General's Department, appears to have considered submissions from a much wider range of stakeholders than did the LPB.

Victoria has now committed to revisit its policy approach to the delivery of PI insurance for solicitors. The Victorian Government has advised the Council that it will conduct a further independent review to test whether a change to existing restrictions would be appropriate. The Council acknowledges that determining the best way of delivering PI insurance involves some complexities, and considers that Victoria's undertaking to conduct a further review is the most appropriate way to proceed.

B5.4.8 Australian Postal Corporation Act

Background

On 19 May 1997, arising from its NCP legislation review commitments, the Commonwealth Government requested the National Competition Council to review the *Australian Postal Corporation Act 1989*.

The Act restricts competition in several ways. The main restrictions arise from those sections of the Act that reserve certain postal services to Australia Post. With a few exceptions, only Australia Post can carry a letter for less than $1.80 if it weighs less than 250g. In addition, only Australia Post can deliver international mail in Australia.

The Act also requires Australia Post to provide reasonable access to postal services for all Australians – a universal service obligation (USO). In addition, it stipulates that Australia Post must provide a letter service at a uniform rate across the whole country; so whether a letter is sent from Bourke to Mount Isa or around the corner in a capital city, the cost to the sender is the same.

Council recommendations

The essential elements of the Council's package for the reform of postal services in Australia included:

- retention of the obligation on Australia Post to provide an Australia-wide letter service, with unprofitable parts of the USO subjected to community service obligation (CSO) funding from a mix of sources;
- that household letter services remain reserved to Australia Post, with a mandated uniform rate of postage;
- open competition in business letter services, with Australia Post free to discount against a maximum charge set at the same level as the uniform rate for household letters;
- open competition in all international mail services;
- the application of general pro-competitive regulation plus limited special arrangements to restrict monopolistic behaviour by Australia Post in the transition to fully competitive business letter services and to ensure access on reasonable terms to Australia Post's CSO-funded services and post office boxes;
- licensing of all letter service providers to maintain minimum standards and ensure that Australia Post's competitors do not free-ride on its obligation to provide comprehensive services;
- accounting separation for Australia Post's retail operations, reserved services and CSO–funded services;
- services standards for the universal service obligation be established in the legislation that will be monitored and enforced by the Australian Communications

Authority, and a service charter be used to explain these minimum standards to customers; and

- an effective competitive neutrality complaints mechanism.

The Council considered that opening up the market for business mail would generate significant competition. Indications of this potential competition came from both competitors and postal service users. On the other hand, it was not obvious where or how such competition would arise for household mail. Because the information necessary to judge the impact of extending the package to the household sector was not available, the Council considered it best to deregulate business mail and to assess the need for further reform later.

The Council noted the strong community support for the two social obligations of Australia Post, namely the universal service and the uniform rate. The Council recommended that these obligations be strengthened through guarantees to the community on minimum performance standards. The package of recommendations put forward by the Council would enable these two obligations to be met, while encouraging competition in markets where it is most likely to arise and be of greatest benefit.

Commonwealth Government's response

On 16 July 1998, the Government announced its response to the Council's review.

The Government's reforms are to apply from 1 July 2000. The key features are:

- Australia Posts' monopoly on domestic mail will be reduced from 250g and four times the standard letter rate to 50g and one times the standard letter rate;
- an access regime;
- incoming international mail to be open to competition;
- a further review in 2002-03 to assess the effects of these changes and the need for further reform; and
- a Service Charter, approved by the Government, to be underpinned by regulations which require Australia Post to meet specified performance standards, including delivery times and a minimum number of postal outlets.

Australia Post will continue to fund its CSOs from cross-subsidies and the uniform rate will remain at 45 cents until at least 2003.

Bulk mail customers will benefit from:

- a reduction in the volume threshold;
- aggregation, which will allow smaller volume mailings to be combined to generate volumes sufficient to attract larger discounts;
- the development of a performance monitoring system for bulk mail; and

- Australia Post and its major customers will develop a Code of Practice to improve the commercial relationship.

In addition, arrangements are to be made to assure competitors that Australia Post is not cross-subsidising from its protected monopoly services to its services that are in competitive markets.

Analysis of response

The reduction in the monopoly threshold will still retain the uniform rate. The Government believes the reduced threshold will provide sufficient protection for Australia Post to continue to cross subsidise its loss making services and so continue to provide a universal service. There may be enforcement problems in having the standard letter rate monopoly protected at 45 cents. There will be an incentive to bundle mailing services with postage (so that, while the cost of the bundled mail service is more than 45 cents, the effective ‘cost’ of the postage element is less than 45 cents) and so undermine the postal monopoly. While the reduction in the monopoly will encourage competition, by itself it will offer less incentive than the Council’s recommendations.

Instead of opening up business mail to competitors, the Government has chosen to direct Australia Post to make the bulk mail system more accessible, to improve relations with its largest customers and to put in place an access regime. It has also removed larger letters from the Australia Post monopoly.

The greatest scope for increased competition will arise from an effective access regime. The Government is still to release the details of the regime it proposes and so it is not yet possible to estimate its effect. After the previous Australia Post review (IC 1992), the Government instituted an interconnection scheme for bulk mail which was meant to offer more choice for bulk mailers and allow them to access the Australia Post network at various stages. The scheme has not been a success. It is therefore important to know the detail of the proposed regime in order to assess the effect on competition.

Both the Government’s reforms and the Council’s recommendations call for the opening of inwards international mail to competition. Because the Government has chosen a more regulated response, it will need to put in place arrangements to protect the Australia Post monopoly on domestic mail to address the potential for domestic mail to be posted overseas for delivery in Australia, bypassing Australia Post.

The Government recognises the need for further review, when an assessment of the new reforms would be undertaken. This is in line with the Council’s recommendations.

The Government put in place regulations on performance of Australia Post in May 1998. Australia Post's performance is audited against these and a report tabled in Parliament. Australia Post is then required to submit a plan for overcoming any shortfalls in performance. While this is not as strict an arrangement as that envisaged by the Council, the effect may be similar, as Australia Post is keen to protect its reputation.

The Government's reforms are in many ways similar or the same as the Council's recommendations. However, there is a difference in approach to one major issue – how to inject more competition into the postal services industry. The success of the Government's approach will depend on the effectiveness of the access regime. Until there is more detail available about the access regime, it is not possible to fully assess its likely effects. To date, the Commonwealth has not elaborated on the July 1998 press release that sketched-out its postal reforms.

Assessment

The Council considers that the package proposed by the Commonwealth can fulfil its NCP obligations for legislation review. However, crucial to this is the nature and form of the access regime. Previous attempts to allow access to Australia Post's network have not been successful. Subject to the Government implementing an effective access regime, the Council considers the Commonwealth to have fulfilled its NCP obligations with respect to Australia Post.

B5.5 Other review and reform matters investigated as part of the second tranche

This section deals with a range of legislation review and reform activity that falls into one of four categories. Specifically:

- review and reform activity which satisfies a government's second tranche legislation review commitments; or
- reviews and/or reforms which demonstrate evidence of progress achieved through NCP processes; or
- matters which have arisen during the second tranche assessment but will be assessed in the third tranche assessment; or
- issues which are on-going from the Council's first assessment of the Commonwealth Government's progress.

B5.5.1 Agricultural statutory marketing arrangements

Agricultural statutory marketing arrangements (SMAs) are prima facie anti-competitive. Typically, they incorporate a centralised marketing board with powers to compulsorily acquire or vest an entire crop, set quality grades and prices, and act as the single seller of the acquired product on either or both the domestic and export markets. They are anti-competitive because they impose legislative restrictions on producers to sell their product to the marketing body and on customers to buy the product from the marketing body.

All governments are reviewing legislation governing SMAs over the period of NCP. Legislation relating to the dairy industry and to the domestic marketing of rice in New South Wales raise matters directly relevant to the Council's assessment of progress for second tranche competition payments and was discussed in section B5.4.2. This section discusses review and reform activity relating to regulations in other agricultural industries, where a government's review and reform activity either

complies in full with second tranche obligations or will be assessed under the third tranche.

Barley marketing arrangements (Victoria, South Australia and Queensland)

Background

The barley industry is dominated for many years by statutory "single-desk" authorities. Each significant barley-growing State[28] has had its own marketing authority with an exclusive right to acquire barley (and often other coarse grains) and to sell it on the domestic and international markets.

Developments

The review and, in some instances, reform of the statutory barley marketing arrangements in relevant States is well progressed.

Queensland reviewed its *Grain Industry (Restructuring) Act 1993* in mid-1997. The Review Panel comprised government and industry representatives, including from Grainco, the SMA under review. In practice, the domestic market monopoly arrangement is no longer operating in Queensland, as recommended by the Review, with legislation to codify the changed arrangements before the Queensland Parliament (the *Primary Industries Legislation Amendment Bill 1999*). However, the Government has retained the export marketing monopoly until at least June 2002, albeit subject to earlier review if there is a change either to arrangements in other States or to the policy of the Japan Food Agency (JFA).

In 1997, Victoria and South Australia jointly reviewed their respective *Barley Marketing Act 1993*. The two Governments accepted the review recommendations to remove the domestic marketing monopoly and to retain the export marketing monopoly only for the "shortest possible transition period". Both States have now passed legislation to complete domestic market deregulation by 30 June 1999 and export market deregulation by 30 June 2001. The Australian Barley Board (ABB) has been transferred to grower ownership.

New South Wales' review of its *Grain Marketing Act 1991* commenced in April 1998 and is near completion. As well as the marketing of barley, this Act regulates the marketing of other coarse grains and oilseeds, and establishes the New South Wales Grains Board. Western Australia is also reviewing its *Grain Marketing Act 1975*. These reviews will be considered in the Council's third tranche assessment.

The relevant jurisdictions for the second tranche assessment are Victoria, South Australia and Queensland.

Assessment

Victoria and South Australia's joint review of their respective legislation set a benchmark for the conduct of independent and rigorous reviews of agricultural

[28] New South Wales, Victoria, Queensland, Western Australia and South Australia.

marketing arrangements. Both Governments have implemented the recommended reforms following consultation with industry through the Implementation Working Group. The automatic right of traders, other than the ABB, to export bagged and containerised barley during this period will assist them to prepare for an open market. By June 2001, the Council expects that all parties will be well placed to compete on the open market.

The Council has, on several occasions, stated its view that it is important, for purposes of ensuring appropriate independence and objectivity of review processes, that industry representatives are not included on review panels; rather, that industry participate through submission to a review. The Council is particularly concerned where a body under review is represented on the review panel as was the case in the Queensland grains review. Having said that, the Council welcomes the move to deregulate domestic marketing arrangements in Queensland.

Since the completion of the review, the conditions it prescribed for reviewing the export monopoly earlier than the year 2002 appear to have been satisfied. That is:

- the JFA indicated in April 1999 that it is gradually lifting its control over barley imports into Japan, which has allowed Australian and other exporters to earn a premium in that market; and
- the export marketing reforms in Victoria and South Australia substantially erode the risk that, if the statutory monopoly in Queensland was removed, the JFA would switch its purchases to other States.

Further, the domestic market structure is changing. The two largest barley producers, Victoria and South Australia, are progressively opening their markets over the next two years to full competition.

The Council, therefore, encourages Queensland to initiate a review of the export monopoly as soon as practicable. The Council will revisit the issue of Queensland barley arrangements in its third tranche assessment.

Sugar (Queensland)

Background

The *Queensland Sugar Industry Act 1991* establishes a statutory authority, the Queensland Sugar Corporation (QSC), as the single desk marketer of raw sugar to domestic and export customers. The Corporation compulsorily acquires all raw sugar produced in Queensland; pools returns to growers from raw sugar sales; and sets quality standards. The legislation also regulates cane production and milling through establishing local boards with powers to assign rights to grow cane and rights to mill capacity.

In September 1995, the then Queensland Government commissioned a review of this legislation and the industry. The Sugar Industry Review Working Party (SIRWP) reported in July 1996. It recommended:

- retention of the single desk subject to export price parity for domestic sales;

- changes to local cane supply and milling arrangements to permit individual growers to opt-out of collective agreements upon their expiry, and to transfer cane supply to other mills;
- removal of the tariff on raw sugar imports; and
- a ten year moratorium on further review of the marketing arrangements.

The Queensland and Commonwealth Governments endorsed the recommendations.

In its first tranche assessment, the Council indicated that it was not convinced about the evidence for continuation of the domestic monopoly. The Council proposed the Queensland Government reconsider the marketing arrangements for sugar before ten years expires should changes in market conditions suggest that the arrangements are no longer in the community interest. The Queensland Government agreed to this approach.

Developments

As of July 1997, the tariff was removed and the QSC shifted from import to export price parity for domestic raw sugar sales. With the removal of the tariff, and substantial falls in world prices, the domestic price for raw sugar has fallen by more than $200 per tonne.

Over this period, the Queensland Government has determined the detail of the other reforms in consultation with the industry, and is preparing legislation for introduction in the Winter 1999 Parliamentary session. The Council is aware of one key change from the agreed reform package – the legislation will now prevent growers from transferring cane supply unless their existing mill will not meet grower demand for expanded capacity. According to Queensland, this change is intended to avoid threats to mill viability from transfers of existing cane supply.

Assessment

The Council recognises the progress that Queensland has made with introducing sugar industry reform since its first assessment in 1997. Evidence suggests domestic consumers of sugar are benefiting from price reductions resulting from the abolition of the tariff on imports and the QSC's shift to export parity pricing for domestic sales.

The Council notes the slippage in timeframe to implement the remainder of the agreed reform package. However, the Council recognises the complexities involved with the task, the considerable amount of development and consultation undertaken over the past two years, and that legislation to give effect to the reforms is imminent.

Overall, the Council is satisfied that Queensland has met its second tranche obligations in relation to sugar industry reform.

Having said that, the Council raises the following matters which it will consider in its third tranche assessment.

The Council is not convinced that the export parity pricing rule for domestic raw sugar sales is delivering the full net benefit which domestic deregulation would bring.

While domestic raw sugar purchasers have certainly gained from the substantial falls in world prices, by including the “Far East” regional premium in the pricing rule, domestic prices are likely to be held above a level sustainable under open domestic competition. The single desk and associated price pooling arrangements are also likely to lower incentives for efficiency and innovation in the supply chain between growers and domestic users.

More importantly, available evidence casts doubt on the sustainability of the principal benefit identified by the SIRWP of the single desk arrangement – maximisation of the “Far East” regional premium. The SIRWP found that the single desk was able to manage its sales into Asian markets so as to increase its returns to growers – this arose from the strong growth in market demand and the relatively high shipping costs faced by Australia’s out-of-region competitors. Since then market conditions have changed dramatically. According to the Australian Sugar Milling Council, demand has fallen in Asia and Russia following their respective financial crises, while supply from Western Europe, India, China and Brazil has expanded. Aided by a currency devaluation, and reduced shipping costs, Brazilian sugar exports to the Middle East and Asian markets have shown particularly strong growth, where competition is now intense. These changes in market conditions mean the single desk exporter is unlikely to sustain a premium over what competitive Australian exporters would earn.

Asian demand for raw sugar should, of course, strengthen again as these economies recover. Nevertheless, without a return to earlier supply conditions, which seems unlikely, a single desk premium is unlikely to be sustainable.

Given these recent developments, the Council considers there is now a prima facie case that the single desk marketing arrangements may no longer be in the community interest. It would, therefore, be appropriate for the Queensland Government to revisit the regulatory arrangements for the sugar industry prior to the third tranche assessment. This would ensure that, should the arrangements no longer be justified, the cost to the community could be minimised and the Government could amend the proposed legislation as appropriate. It may also highlight pro-competitive options for improving returns to the industry that could be more important than ever given the clearly difficult times ahead.

The decision to prevent growers from transferring existing cane supply between mills represents an important departure from the recommended reform package. This will protect mills from competition and, therefore, from pressure to improve productivity, even while returns to the industry are falling. However, the Council recognises the issues associated with milling industry reform, and that transitional arrangements may be desirable.

The Council is working with the Queensland Government to find the best way forward for the sugar industry and the wider community. Progress in both areas – the single desk and the constraints on growers – will be considered as part of the Council’s third tranche assessment.

Poultry meat (Queensland, New South Wales, Victoria, South Australia, Western Australia)

Background

All jurisdictions with significant poultry meat industries regulate commercial relations between poultry growers and processors. The legislation generally establishes an industry committee of grower and processor representatives to approve grower entry and to negotiate standard contract terms (including fees) for the supply of poultry to processors. The intention is to increase the bargaining power of growers, through collective arrangements, to countervail that of processors.

Developments

The Governments of South Australia, Western Australia and Queensland have each agreed to remove regulated entry barriers and to retain some degree of collective bargaining subject to allowing individual growers the right to "opt out" – that is, to separately negotiate a supply agreement with a processor. Their approaches to achieving this have differed.

South Australia reviewed its *Poultry Meat Industry Act 1969* in 1994. The review found that the industry no longer required specific legislation to provide security for chicken growers. The Government subsequently introduced a Bill to repeal the legislation that was passed by the Lower House. Passage through the Upper House was adjourned pending authorisation by the ACCC of collective negotiation arrangements between each processor and their respective growers. Authorisation for five years has now been granted, and the repeal Bill is awaiting space in the legislative program.

Queensland completed a review of its *Chicken Meat Industry Committee Act 1976* in 1997 and, in December 1998, the Government agreed to implement the recommendations. Amendments currently before the Queensland Parliament reduce the Industry Committee's role to a facilitative one - convening representative groups of growers to negotiate with each processor, and referring disputes to mediation or arbitration. The Committee will be specifically barred from making recommendations or providing information on growing fees.

Western Australia reviewed its *Chicken Meat Industry Act 1977* in 1996. As noted above it recommended removal of entry regulations and permitting growers to opt out of collective negotiations. It also recommended retention, subject to review in another five years, of the Industry Committee's power to set a fee for supply contracts between growers and processors. The Government endorsed these recommendations and intends to amend the Act by the year 2000.

New South Wales and Victoria have reviews of their respective legislation underway. These will be addressed in the third tranche assessment.

Assessment

Subject to the passage of legislation, the decisions by South Australia, Queensland and Western Australia accord with the outcomes of their respective reviews which seem to have been sufficiently open and objective. South Australia's approach is of

particular note as it illustrates how general competition law can, in some circumstances, render specific legislation unnecessary.

While retaining industry specific legislation, the approaches taken by Queensland and Western Australia are likely to have a largely similar impact as South Australia's. However, Western Australia could usefully look at drafting its amendments to provide for collective negotiations on a processor basis, rather than on an industry-wide basis. The Council is satisfied that, once each Government makes its respective legislative changes, they will have met their CPA clause 5 commitments in this area.

Wheat (Commonwealth)

Background

During 1997 and 1998, the Commonwealth introduced new legislation to facilitate the transfer to growers of the Australian Wheat Board (AWB, now AWB Ltd) and to delegate the existing wheat export monopoly to the privatised entity via the statutory successor to the AWB, the Wheat Export Authority (WEA). The legislation is discussed in section B4.2.

The Commonwealth has confirmed that its NCP review of the *Wheat Marketing Act 1989*, scheduled for 1999-2000, will examine all aspects of the legislation underpinning wheat marketing arrangements, including the WEA and the export monopoly, in accordance with NCP principles.

The privatisation of the AWB, and similar moves in respect of several State-based grain marketers and handlers, have stimulated considerable debate about the future structure of the Australian grains industry. It is generally accepted that there will be, over time, some rationalisation among former statutory grain marketers and handlers. The commercial and investment decisions made over the next couple of years by growers, handlers, marketers and investors will have important long term consequences for them individually and for the industry as a whole. The Council is also aware of concerns that the export monopoly may advantage AWB Ltd's position in domestic marketing and handling markets and, hence, disadvantage other players in these markets.

The credibility of the review and any reform recommendations will rest on the bona fides of the review process. In particular, the Council will be looking for:

- the terms of reference to include all material NCP questions;
- the reviewer to be well qualified in regulatory review and independent of industry and other affected interests;
- the process and the material NCP questions to be well publicised, with ample opportunity for public participation;
- the review to be released and summarised in a form that will assist public understanding; and
- recommendations of the review to be implemented in a timely manner.

Turning to the outcome of the review, if it recommends retention of the wheat export monopoly, it will need to demonstrate that the monopoly provides a net benefit to Australia. Essentially, this means showing that AWB Ltd is able to exert market power in the international wheat market such that it can sustain a price premium for Australian wheat which exceeds any losses (for example, reduced innovation and efficiency) consequent on its monopoly. Should the review find the monopoly is not beneficial for Australia, the Commonwealth will need to consider how to open wheat exporting to competition.

This review, and any subsequent reform, will be a matter for the third tranche assessment.

B5.5.2 Pharmacy regulation

Background

Retail pharmacy is a highly regulated sector of the economy with both Commonwealth and State regulations governing practitioners and the practice of pharmacy.

The core elements of state-based regulation of pharmacists and pharmacy practice are largely the same across jurisdictions. State regulations typically include:

- registration of pharmacists;
- pharmacy ownership limited to registered pharmacists;
- limits on the number of pharmacies a pharmacist can own;
- premises standards and site regulations;
- advertising restrictions on the promotion of pharmaceuticals; and
- drugs and poisons scheduling.

Typically, State regulations have been justified on the basis of maintaining professional ethics and standards, controlling access to drugs, encouraging responsible use of pharmaceuticals and ensuring community access to services.

The Commonwealth also regulates the pharmacy sector. Under the Pharmaceutical Benefits Scheme (PBS), the Commonwealth subsidises a wide range of pharmaceuticals to consumers. The PBS is aimed at improving community access to, and constraining the cost of, PBS drugs. In this context, the Community Pharmacy Agreement between the Commonwealth and the Pharmacy Guild of Australia determines:

- dispensing fees for PBS drugs; and

- limits the number and location of pharmacies approved to dispense PBS drugs.[29]

The current five year agreement expires on 30 June 2000.

Pharmacy practice in Australia is also subject to therapeutic goods legislation. The classification of drugs is determined by the Australian Health Ministers' Advisory Council (AHMAC), which includes the Health Minister from each jurisdiction. The Commonwealth is responsible for the registration of drugs through the *Therapeutic Goods Act 1989*. States and Territories are responsible for the scheduling of drugs for the purposes of retail distribution. The state-based schedules, underpinned by legislation, are based on schedules determined by the National Drugs and Poisons Committee of AHMAC.

Developments

All States and Territories identified their pharmacy regulations as restricting competition in their 1996 legislation review schedules.

In May 1998, all governments agreed to a national review examining State and Territory legislation relating to pharmacy ownership and the registration of pharmacists, together with Commonwealth legislation relating to the regulation of the location of pharmacy premises approved under the PBS.[30] The Commonwealth is co-ordinating the establishment of this review, which is expected to commence in mid-1999. As a result, a number of state-based pharmacy reviews have been deferred until the national process is concluded.

The Commonwealth, State and Territory governments have also commissioned a review to examine legislation and regulation pertaining to drugs, poisons and controlled substances. The scope of this review will extend beyond the human use of drugs, to include issues relating to drugs for veterinary use, agricultural chemicals and household chemicals. The Commonwealth is currently consulting with the States and Territories on the terms of reference for this review.

Stage 1 of the Queensland health practitioner review (see Section B5.5.3) examined the regulatory framework relating to pharmacists in that State. It recommended the retention of registration of pharmacists and the reservation of the practice of "*professional dispensing of medicines, mixtures, compounds and drugs*". The review recommended that ownership of pharmacy practices continue to be restricted to registered pharmacists, but that pharmacists be allowed to incorporate their businesses. As Queensland is participating in the national pharmacy review, its pharmacists registration and pharmacy ownership regulation will be revisited.

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[29] Refer section 90, *National Health Act 1953* (Clth) and Determination No PB 21 of 1996 made under section 99L(1) of that Act.

[30] Noting that in the case of Queensland and Tasmania the national review will not cover the registration of pharmacists as this has already been addressed in state-based pharmacy reviews.

Assessment

The Council considers that the national approach to the review of pharmacy regulation and the review of the related drugs and controlled substances regulation provides an opportunity for a considered and co-ordinated approach to determining the most appropriate regulatory environment for retail pharmacy.

Given the proposed review schedule, the Council will consider the outcomes of the national reviews and reviews of the residual state-based regulation in the third tranche assessment. In particular, the Council will look for the national review of pharmacy arrangements to consider whether the restrictions imposed on pharmacy ownership generate a net community benefit.

B5.5.3 Professions regulation

Many professions have traditionally been shielded from competitive pressure through specific legislation and/or self-regulatory arrangements. NCP has changed this significantly, first, through extension of the *Trade Practices Act 1974* to the professions under the Conduct Code Agreement, and second, through the review of legislation which regulates the professions.

Professions regulation typically affects the market structure for professional services - for example, through reservation of professional title, registration and ownership restrictions and the market conduct of practitioners – for example, through fee limits/scales, advertising restrictions and professional and ethical standards.

In the main, States are responsible for the regulation of the professions. Consequently, each State and Territory has scheduled a wide range of professions legislation for review under the NCP. The Table 5.8 provides a summary of government's professions reviews and reforms to date.

Table B5.8 Summary of professions related reviews

	Profession	Review status	Reform status
National reviews	• Mutual recognition	Recommendations with governments	Not applicable (n/a)
	• Travel Agents	Commenced	
	• Architects • Pharmacists (registration & ownership regs)	To commence in 1999	
NSW	• Legal practitioners • Medical practitioners	Completed	Recommendations with government
	• Chiropractors • Dentists • Nurses • Optical dispensers • Optometrists • Physiotherapists • Property, stock & business agents	Commenced	n/a

	Profession	Review status	Reform status
	• Psychologists • Surveyors • Valuers • Veterinary surgeons		
	• Podiatrists	To commence in 1999	n/a
	• Dental technicians	Review under consideration	n/a
Vic	• Chiropractors • Chiropodists • Finance brokers • Legal practitioners • Optometrists • Osteopaths • Physiotherapists • Veterinary surgeons	Completed	In general –retention of registration –reservation of professional title –retention of some advertising restrictions –removal of some ownership restrictions –professional fee reform –some specific reservation of practice e.g., eye testing with dispensing of glasses –opening up of some professional services e.g., extending limited prescribing rights to orthoptists under referral –introduction of negative licensing for finance brokers
	• Dentists • Psychologists	Completed	Reform pending along similar lines as above
	• Surveyors	Completed	Recommendations with government
	• Medical practitioners • Nurses • Estate agents	Commenced	n/a
Qld	• Health and Medical Practitioner registration: – Chiropractors – Osteopaths – Dentists – Dental technicians & prosthetists – Medical practitioners – Occupational therapists – Optometrists – Pharmacists – Podiatrists – Psychologists – Speech pathologists	Stage 1: review completed Stage 2 : in progress, application of principles to specific legislation	Stage 1 proposed minimalist regulatory framework based on a risk assessment to be applied to specific Acts in Stage 2 (see following discussion)
	• Legal practice incl. non-lawyer conveyancing	Commenced	On 30 June 1999 the Queensland Government announced significant reforms to its legal profession, including: - a Legal Practice Authority to handling complaints; - a disciplinary board to hear conduct charges; - Supreme Court committees to set admission rules and approve cost scales; - allowing non-lawyer property conveyancing; - allowing lawyers to join multi-disciplinary

	Profession	Review status	Reform status
			practices.; and - a cap on payouts for damages caused by unscrupulous lawyers.
	• Auctioneers & Agents	Proposed legislation being revised and subject to public benefit test in 1999	n/a
WA	• Surveyors	Completed	Retain entry restriction but defined so as to remove Board discretion; equal consumer representation on Board; and reduce minimum supervised field training for trainees
	• Finance brokers	Completed	Act to be repealed & replaced with a code of conduct under *Fair Trading Act* and reliance on the TPA (Clth)
	• Health practitioner legislation: – Chiropractors – Dentists – Dental prosthetists – Medical practitioners – Nurses – Occupational therapists – Optical dispensers – Optometrists – Osteopaths – Physiotherapists – Podiatrists – Psychologists	Commenced	Acts to be repealed & replaced with new legislation consistent with CPA. Adopting similar approach as Qld (see following discussion)
	• Architects	Commenced but see national reviews	n/a
	• Legal Practice	Due to commence in March 2000	n/a
SA	• Health practitioner legislation: – Chiropodists – Chiropractors – Dentists – Medical practitioners – Nurses – Occupational therapists – Optometrists – Physiotherapists – Psychologists	Completed	Recommendations with government
	• Architects	Commenced	See national review
	• Legal practice • Surveyors • Teachers • Veterinary surgeons	Commenced	n/a

	Profession	Review status	Reform status
Tas	• Chiropractors	Completed	New Act retains registration requirement
	• Physiotherapists • Nurses • Psychologists • Radiologists • Podiatrists	Commenced	Will build on program of Act replacement; framework based on *Optometrists Registration Act 1994* which: — retained reservation of professional title; - retained a requirement for professional indemnity insurance; and - removed advertising restrictions
	• Auctioneers & estate agents • Surveyors	Commenced	n/a
	• Non-lawyer conveyancers	Will be subject of new legislation	n/a
	• Legal practitioner • Veterinary Surgeons	To commence in 1999	n/a
	• Dentists • Medical practitioners • Optometrists	Deferred until 1999 to utilise Committee on Regulatory Reform 1999 guidelines	Will build on program of Act replacement; framework based on *Optometrists Registration Act 1994* which: — retained reservation of professional title; — retained a requirement for professional indemnity; and insurance. - removed advertising restrictions.
	• Hairdressers	Yet to commence	n/a
ACT	• Surveyors	Commenced	n/a
	• Legal practitioners incl. non-lawyer conveyancing	To commence in 1999	n/a
NT	• Architects	Completed	Government deferred response given national review
	• Nurses	Commenced	Act to be repealed & replaced. New Act, which retains registration and Board, will be reviewed
	• Veterinary surgeons • Surveyors • Health practitioners: – Aboriginal health workers – Chiropractors – Dentist – Dental therapists & hygienists – Medical practitioners – Occupational therapists – Optometrists – Osteopaths – Physiotherapists	Commenced	n/a

	Profession	Review status	Reform status
	– Psychologists – Radiographers		
	• Legal practitioners	To be advised	n/a

Source: Jurisdictions' Annual Reports (1999)

Health Practitioner Legislation

Health practitioner legislation represents a large proportion of the professions legislation scheduled for review by States.

Queensland has completed the first stage of a major review of health and medical practitioner registration acts and associated regulations covering 13 professions.[31] The review presented a systematic approach to regulation based on risk assessments. It recommended the retention of registration/licensing provisions and the reservation of several professional titles (for example, physiotherapist, medical practitioner, doctor and surgeon). The review also recommended the winding back of commercial controls[32] and significant lessening of advertising restrictions. The second stage of the process is now underway and involves developing new practitioner legislation reflecting the principles and recommendations arising from Stage 1.

The Council considers this to be a thorough approach to review and reform. Stage 1 provided an objective consideration of the need to regulate health practitioners and their practice and the most appropriate manner in which to regulate. The resultant minimalist risk management approach is being applied across the health professions in Stage 2. Applying a framework reduces the risk of regulatory anomalies arising between often related professions while allowing issues specific to a particular profession to be taken into account.

Western Australia and South Australia are adopting a similar approach to reviewing professions regulation.

Victoria's review of the physiotherapists regulation maintained the restriction on the use of the title "physiotherapist" and advertising restrictions requiring fair and accurate advertising and the power for the Physiotherapy Board to investigate advertising as necessary. No restrictions on professional practice or practice ownership were retained.

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[31] Chiropractors, osteopaths, dentists, dental technicians, dental prosthetists, doctors, occupational therapists, optometrists, pharmacists, physiotherapists, podiatrists, physiologists and speech pathologists.

[32] Noting that ownership restrictions for pharmacy and optometry will be the subject of separate reviews in 1999.

Legal Practice

Legal practice remains a highly areas of professional practice. There continues to be many restrictions on entry to the profession and to practice. These restrictions are primarily contained in each State's *Legal Practice/Practitioners Act* while others arise from professional and ethical standards determined within the profession.

Typically, restrictions on legal practice include: restriction on entry to the profession; professional or legal practice training for graduates; ownership restrictions prohibiting incorporation of practices; restrictions on advertising; the setting of legal fees; the reservation of practice in certain areas to legal practitioners (for example, property conveyancing); and Legal Practice Boards which have disciplinary powers over practitioners.

Under NCP, each State is reviewing its legal practice legislation, while standards and/or policies set by a profession are subject to scrutiny against Part IV of the TPA by the ACCC. Victoria completed a review in 1996 that led to a range of reforms being implemented including: the removal of the distinction between solicitors and barristers; direct access by clients to barristers; the introduction of non-lawyer property conveyancing; incorporation of legal practices; removal of binding fee scales; and the abolition of compulsory membership of professional associations.

The Victorian review recommended the retention of professional licensing of lawyers based on a defined minimum level of qualification. The review determined that the benefits arising from the restriction exceeded the costs. The review argued that the restriction avoided the costs otherwise imposed on the community of allowing unqualified people to perform specialised work requiring legal knowledge and skill – for example, costs to business associated with inefficient handling of procedures, and litigation costs arising from non-lawyer professional failures. The review also recommended the retention of the Solicitors' Guarantee Fund or Fidelity Fund (see Section B5.4.7). This is a statutory fund administered by the Legal Practice Board to provide automatic reimbursement of client monies which have been misappropriated from solicitors' trust accounts. The rationale behind this was that the private insurance market would not provide a comprehensive and cost effective coverage with no limits on claims.

New South Wales completed its review of the *Legal Profession Act 1987* in December 1998 and the recommendations are currently before the Government for response. Reviews of legal practice are underway in Queensland and South Australia. The Tasmanian and ACT reviews are due to commence later in 1999. The Western Australian review is scheduled for March 2000 while the timing of the Northern Territory review will be advised.

In all jurisdictions, solicitors are required to hold legal professional indemnity insurance. In most cases this is only available through a monopoly provider. As discussed in Section B5.4.7, these arrangements are also the focus of NCP review.

An apparent regulatory anomaly in legal practice is the continuing prohibition on non-lawyer conveyancers in Tasmania and the ACT. Over the past two decades all other states have removed the legal practitioner monopoly over property conveyancing. Indeed, non-lawyer conveyancers have existed in South Australia for

140 years. With the appropriate professional accreditation of non-lawyer conveyancers, the benefits to consumers are clear. The liberalisation of conveyancing in New South Wales in 1992 resulted in a 17 per cent reduction in costs (or some $86 million per annum) for New South Wales consumers (NCC 1998a).

On 30 June 1999, the Queensland Government announced a wide-ranging package of reforms for the legal practice in that state. The package includes:

- the establishment of a new independent Legal Practice Authority to handle complaints about lawyers;
- a disciplinary board to hear conduct charges against lawyers;
- Supreme Court committees to set admission rules and approve cost scales;
- the introduction of non-lawyer property conveyancing, allowing lawyers to join multi-disciplinary practices with other professionals; and
- the capping of payouts for damages arising from unscrupulous behaviour by lawyers to $60 000.

Assessment

The Council views the application of NCP principles to professions regulation as a key reform area. The Council recognises that certain aspects of professions regulation may well be justified, particularly given the information problems facing consumers in some circumstances. However, in assessing professions reviews the Council is keen to ensure that, where restrictions are retained, they are clearly supported by a net public benefit.

The Council recognises that the Law Council of Australia is working with governments to reform a number of features of the profession. The Council considers that Victoria has met its CPA commitments in relation to its legal practice review and reform, with one exception, professional indemnity insurance (see Section B5.4.7).

The Council will maintain a close interest in the outcomes of the remaining State's legal practice reviews in the context of the third tranche assessment, particularly the issue of non-lawyer conveyancing in Tasmania and the ACT.

National professions related reviews

Governments are conducting national reviews of regulation relating to the licensing of travel agents and the mutual recognition regime (see following discussion). The Commonwealth and States are currently establishing national reviews of architects regulation and the registration and ownership of pharmacists (see Section B5.5.2) which are due to commence in the second half of 1999.

Professional associations have raised concerns about the lack of national reviews of professions legislation to date. They argue that the predominantly state-based approach to legislation review:

- duplicates effort for both reviewers and the professions with the conduct of multiple reviews across jurisdictions;
- does not adequately focus on the national dimension of the market for professional services; and
- could result in different regulatory outcomes across jurisdictions for the same profession, thereby potentially undermining gains made this decade toward a national professional services market in the context of the development of the mutual recognition regime.

The Council sees considerable benefit in adopting a national approach to the review of professions regulation. However, support for, and participation in, such processes is a decision for each government. The CPA provides for, but does not require, joint-jurisdictional and national reviews. Similarly, there is no requirement that the outcomes of reviews of professions legislation be uniform across jurisdictions. Further, the Council is not aware of any evidence to suggest that the NCP reviews are undermining the effectiveness of, and benefits for professionals associated with, the mutual recognition regime.

Fewer national processes have been undertaken than might have been expected. In view of this, governments have established alternative means of ensuring that a national focus is brought to state-based reviews through the oversight of the COAG Committee on Regulatory Reform (CRR). This has included the development of guidelines for the review of professions regulation (CRR 1998). The mutual recognition regime itself continues to act as a standardising influence on professional registration regulation. The influence of mutual recognition and its recent review are discussed in the following section.

Mutual recognition

The nation-wide introduction of mutual recognition laws in 1993 has been a significant driver of reform in the area of professions regulation.

The aim of mutual recognition is to remove regulatory barriers to the free movement of goods and labour between Australian States and Territories. This is achieved by jurisdictions recognising each other's regulation with respect to goods and registered occupations. The principles of mutual recognition now extend to New Zealand under the Trans-Tasman Mutual Recognition Agreement.

For registered professions, such as architects, surveyors, chiropractors, nurses, legal practitioners, and real estate agents, variations in regulation between jurisdictions had created barriers to entry, providing protection from competition for practitioners within a jurisdiction. The recognition of professional registration across state borders has helped to facilitate a national market for professional services.

Mutual recognition relates solely to registration or entry requirements. It mitigates regulatory differences by ensuring that if a professional satisfies the registration criteria in their home state, that registration is recognised elsewhere in Australia. Mutual recognition does not, and was not intended to, address differences in

regulation relating to the conduct or delivery of professional services between jurisdictions.

Mutual recognition is given effect through Commonwealth, State and Territory legislation. COAG established a working group to conduct a national review of mutual recognition arrangements. Queensland was lead jurisdiction for the review with the Commonwealth, New South Wales, and Western Australia represented on the Working Group. The review was completed in mid-1998 following public consultations.

The Queensland Annual Report states that "*the review essentially found that the legislation is working properly and is generally consistent with national competition policy, and that no major change is in order*" (Queensland Government 1999, p. 6). The CRR will prepare a detailed response to the review recommendations for consideration by COAG.

Travel agents

All Australian travel agents (other than those in the Northern Territory) are licensed under a national scheme of state/territory legislation. This requires each travel agent to be licensed in each state/territory where they operate and to be contributing members of the national Travel Compensation Fund. The aim of licensing is to protect consumers from losses by restricting entry to agents who have satisfied certain probity, educational and financial hurdles. The aim of the Fund is to provide compensation for losses suffered by consumers due to agent fraud or dishonesty.

The Ministerial Council on Consumer Affairs commissioned a national review of the legislative scheme, co-ordinated by the Western Australia Ministry of Fair Trading. The review is underway and, following an initial round of consultations with relevant peak bodies and regulatory agencies, the reviewer released an issues paper in June 1998 and invited written submissions. A final report will be delivered to the Ministerial Council this December.

B5.5.4 Employee choice in public sector superannuation

Background

In most jurisdictions, public sector superannuation schemes have been provided by statutory public monopolies. These legislative arrangements are significant restrictions on competition. By constraining which fund the employer's guaranteed charge is paid into, they prevent access by alternative providers to a significant component of the market.

Several jurisdictions are now addressing this legislative restriction through reforms that give public sector employees choice over which fund their employer payments are paid into.

A related issue raised with the Council by a private sector organisation active in superannuation administration is the alleged anti-competitive nature of legislation that protects government superannuation scheme administrators from competition.

Scheme administration can be subjected to competitive tendering (although this is not a requirement under NCP). This exposes the incumbent administration to the challenge of the market on cost and service criteria. Parallel tests can be made for other elements of the scheme, such as funds management. Indeed, requirements for market testing have been built into legislation in a number of jurisdictions.

Although the operation of public sector superannuation funds is underpinned by legislation, both South Australia and Tasmania do not believe that NCP legislation review obligations are relevant. Both jurisdictions consider that the operation of their respective funds relates more to the manner in which the Government, as an employer, chooses to conduct its internal affairs.

Current status of reviews of superannuation provision

Following an approach from the Council, New South Wales, Queensland and Western Australia either confirmed that the relevant legislation is already in their review program or that they will consider it for review. The three jurisdictions propose to consider both the question of allowing choice of funds and the matter of contestability for funds administration.

The Commonwealth had legislation before the Parliament to give current employees, both in the private and public sectors, choice in their superannuation provider. The legislation was scheduled to take effect as from 1 July 2000 but delays in consideration recently led to debate on the Bill being deferred. The Commonwealth's legislation was intended to restructure arrangements for public sector superannuation by creating a single co-ordinated Board of Trustees for the two main public sector schemes, the Commonwealth Superannuation Scheme (CSS) and Public Sector Scheme (PSS). It also provided for market testing of scheme administration after a three year transition period. The legislation is now not expected to take effect until July 2001, at the earliest.

Australian Government Employees Superannuation Trust, the default fund for temporary and casual federal government employees, has always had its administration provided by the private sector.

New South Wales has recently passed legislation to corporatise its Superannuation Administration Authority, with effect from 1 July 1999. This process includes provision for competitive challenge for the administration of the scheme, after a mandated fixed term for the incumbent provider. First State Super, the largest of the public funds, allows members both choice of fund provider and of investment strategy.

The Northern Territory reviewed its Northern Territory Government and Public Authorities Superannuation Scheme (NTGPASS) in 1998. NTGPASS is to be closed from 1 July 1999 and all new employees will be free to choose any complying superannuation fund.

In the ACT, prior to this year, all government employees were covered by Commonwealth superannuation arrangements. As far as existing employees are concerned, the ACT is continuing to track developments by the Commonwealth. That is, ACT members of CSS or PSS will be given choice over their fund provider at the

same time as all other members of those funds, subject to the legislative timetable as set out above. However, both the CSS and the PSS are now closed and all new ACT employees, after 1 July 1999, will be offered unlimited choice of complying funds or will be allocated to a default fund, which was chosen following a formal tender exercise.

Victoria and Tasmania are not reviewing their relevant legislation, noting that, in each case, it already enables the relevant board to engage a third party and that this is a commercial decision for the board independent of government. However, neither the Victorian Superannuation Board nor Tasmania's Retirement Benefits Fund (RBF) Board (which are the current providers of superannuation administration services in their jurisdictions) has as yet invoked the option to engage a third party. Nonetheless, both Governments provided a commitment to introducing choice in superannuation arrangements, and Victoria has provided for market testing of its closed fund within two years.

In South Australia, the *Superannuation (Benefit Scheme) Act 1992* and the *Southern State Superannuation Act 1994* tie South Australian Government employees to the Southern State Superannuation (SSS) Fund for any employer contributions. South Australia conducted a preliminary examination of the *Southern State Superannuation Act 1994* using the same methodology as CPA clause 5. This examination concluded that restrictions in the Act were trivial.

The current review status of legislation relating to the provision of public sector superannuation is summarised in Table B5.9 below.

Table B5.9 Progress with reviews of legislation governing provision of public sector superannuation funds by jurisdiction, at 30 June 1999

	Legislation	**Review and Reform Status**
Commonwealth	a) *Superannuation Act 1976* b) *Superannuation Act 1990*	Legislation before the Senate would have removed the administrative monopoly created by a) & b) and allowed contestability of funds administration in due course.
	c) *Defence Force Retirement and Death Benefits Act 1948* d) *Military Superannuation and Benefits Act 1991*	Amendments for c) & d) would have mirrored the civilian Bills.
	e) *Parliamentary Contributory Superannuation Act 1948*	The Commonwealth stated that review of the Department of Finance and Administration of e) is not cost effective as administration costs are trivial ($200 000 pa) and there are efficiencies in co-locating administration and policy functions.
	f) *Judges' Pension Act 1968*	Act f) does not set aside funds, there are no employer or employee contributions to manage and therefore no funds administrator which may be exposed to competition.

	Legislation	**Review and Reform Status**
New South Wales	*Superannuation Administration Act 1996*	Legislation to corporatise the Superannuation Administration Authority enacted, with provision for market testing of administration. Government considering whether the Act should be subject to legislation review. Largest public sector super providers allow for choice.
Victoria	*Public Sector Superannuation (Administration) Act 1993*	Public sector employees have choice in their funds manager. Victoria considers the Act does not restrict competition as it allows the VSB to enter into agreements with any person to carry out its functions. Victoria has restructured administration of public sector superannuation to introduce contestability.
Queensland	*Superannuation (Government and Other Employees) Act 1988*	Superannuation arrangements are the subject of an on-going general review. This will address the matter of a statutory monopoly funds manager. Residual NCP matters to be reviewed, commencing in 1999.
Western Australia	*Government Employees Superannuation Act 1987*	Review expected to be completed by June 2000, but consideration being given to earlier scheduling.
South Australia	*Southern State Superannuation Act 1994*	South Australia has decided not to conduct a full review of the Act (clause 5 of the CPA) on the basis that a preliminary examination applying the same methodology as clause 5 showed that restrictions in the Act are trivial.
Tasmania	Retirement Benefits Act 1993	Tasmania considers the Act does not restrict competition as it allows the RBF Board to enter into agreements with any person in connection with the administration of the Act. Tasmania is to provide employees with a choice of funds, as from early 2000. Government to ensure RBF is competitively neutral.
ACT	*See Commonwealth*	Existing employees will be provided with choice. New employees will have free choice of funds provider.
Northern Territory	*Superannuation Act 1986*	Act establishes the NT Government and Public Authorities Superannuation Scheme (NTGPASS). Scheme reviewed in 1998. NTGPASS to be closed from 1 July 1999 and all new employees will be free to choose any complying super fund.

Source: Jurisdiction's Annual Reports (1999)

Analysis of competition issues

The Commonwealth had broadly pro-competitive proposals before the Senate to provide both for choice of fund and competition over administration. However, the legislation has now been deferred. The Council will monitor the Commonwealth's progress with this legislation as part of its third tranche assessment.

Victoria declined to review its previous legislation, as it claimed the Act already allowed for choice on administration. In addition, most Victorian Government Departments allow freedom of choice as to super fund provider for employer guaranteed payments.

Recent Victorian legislation, the *Government Superannuation Act 1999*, introduced additional pro-competitive aspects. This Act, which takes effect from 1 July 1999, separates the arrangements for the closed, defined-benefits fund, the State Superannuation Fund (SSF), from the continuing accumulation fund, the Victorian Superannuation Fund (VSF). The SSF will be subject to new trustees, the Government Superannuation Office (GSO). Section 6 of the Act places a duty on the GSO to market-test the administration of the SSF within two years. VicSuper Pty Ltd will be the new trustee of the VSF and prudential supervision will be transferred to the Commonwealth as from 1 July 1999. Any future decision as to the management of the fund will be taken on strictly commercial grounds and are outside the State Government's ambit.

Tasmania has decided to provide choice to contributors to super funds. This has been implemented through the *Public Sector Superannuation Reform Act 1999*, which will shortly give all employees choice as to a complying superannuation scheme.

The ACT proposes to mirror Commonwealth changes for existing employees and provide choice for new employees.

The Northern Territory has reviewed its arrangements, and will permit new employees to choose from complying superannuation schemes.

South Australia

The current position in South Australia provides for neither:

- right of choice for employees as to the superannuation funds provider for the employer's superannuation guarantee charge; nor
- competitive challenge to the administration of the government monopoly provider.

In South Australia, the Government's employer contributions, prescribed by the Superannuation Guarantee legislation, have traditionally been paid into one of two schemes, the State Superannuation Benefits Scheme (SSBS) or the Southern State Superannuation Scheme (the Triple S Scheme). Unlike the SSS, the SSBS had not allowed employee contributions. These two schemes were merged on 1 July 1998.

The *Superannuation (Benefit Scheme) Act 1992* and the *Southern State Superannuation Act 1994* mandate payments into these schemes. These Acts tie South Australian Government employees to the Southern State Superannuation Fund,

managed by the Superannuation Funds Management Corporation of South Australia (Funds SA). Employees are prevented from nominating another fund manager for any employer contributions, whether these represent the superannuation guarantee charge required by Commonwealth legislation or are part of State Government remuneration.

South Australia does not accept that its legislation contains any non-trivial restrictions on competition and provided the results of an examination by the Crown Solicitor to support its view. The Crown Solicitor's main arguments are set out below.

- The design and implementation of State Government employee benefits are a matter solely for the State Government. There is no obligation to outsource government functions. Therefore any challenge on competition grounds is limited to the Commonwealth required superannuation benefits.

- South Australia retains the option of outsourcing any aspect of the scheme, including its administration and has followed this course for its funds management role.

- The fees charged for administration of the fund are very low in comparison with others in the market. Funds SA has therefore retained administration in-house.

- The level of 'economic activity' associated with scheme administration is irrelevant in terms of the South Australian economy and therefore is trivial in relation to anti-competitive concerns.

- The South Australian Government uses the statutory fund, required under Commonwealth superannuation legislation, as a vehicle to provide a range of additional benefits to its employees, including death and disability benefits. There are considerable economies of scale and scope from this co-ordinated arrangement. The current arrangement therefore meets the net benefit test.

- Any alternative arrangements would involve considerable transaction costs and dis-benefits for the State and employees.

- In any case, State Government employees have the right to make payments to any private sector superannuation scheme.

It is not clear that the South Australian legislation contains only trivial restrictions on competition. The sums involved from employer contributions are significant and, arguably, represent a non-trivial impact. The Triple S Scheme itself had employer contributions of $11.85 million in 1997-98, whilst the parallel SSBS had employer contributions of $99.27 million. Between them the two schemes provide for an annual contribution in excess of $100 million, representing payments for 150 000 public servants. As such, the management of the funds represents significant economic activity and a market opportunity for other superannuation fund providers were it not that the current legislation restricts entry by potential competitors.

The Council is also not persuaded by the other arguments presented for retention of the monopoly provision, noting the developments in other jurisdictions where public sector employees have been given choice as to their funds manager.

Finally, on the question of market-testing funds administration, the Council notes both New South Wales and Victoria have introduced legislation that will explicitly require market testing of their funds administration after a specified period.

For the reasons above, the Council considers that the South Australian legislation may have more than a trivial effect on competition. Accordingly, the Council proposes to continue to work with South Australia on this matter in the period leading to the third tranche assessment. The Council's objective is to clarify the magnitude of restrictions on competition in the legislation and to ascertain that, by the end of the year 2000, any non-trivial restrictions provide a net community benefit.

B5.5.5 Gaming regulation

Background

Governments are reviewing legislative restrictions affecting gambling activity throughout the period of the NCP legislation review program. Consistent with the CPA, they are to review and, where appropriate, reform existing restrictions on competition and ensure that new restrictions are in the public interest.

In the first assessment in June 1997, the Council found that some governments were not proposing to schedule legislation supporting monopoly casino licences for review and/or had not provided a public interest case in support of recently enacted legislation providing monopolies in areas of gambling activity. Given that such arrangements restrict competition, the Council considered that they should form part of the NCP review program. The Council asked governments to add monopoly licensing legislation for gambling activities to their review schedules.

In June 1998, the Council looked at progress in this area as part of a supplementary NCP assessment. It took into account reviews of casino licensing arrangements by Queensland and South Australia and of the TAB monopoly by New South Wales. These reviews highlighted the complexities and sensitivities associated with the social and economic impacts of gambling and wagering.

Competition issues

Restrictions on competition and market behaviour are common in gambling legislation. Typically, these include restrictions on:

- who can participate in the provision of the gambling activity, such as through probity checks;

- the accessibility of gambling operations – for example, caps on the number of gaming machines;

- the kinds of gambling activities which may take place at a particular venue – for example, gaming machines are not permitted at the Canberra Casino, but are restricted to clubs, hotels and taverns in the ACT. Further, there is a cap on the number (and in the case of hotels and taverns on the kind of) machine at each venue;

- the kinds of horse races which can be staged;
- the involvement of third parties – for example, there are some restrictions in some jurisdictions on leasing and/or ownership of gaming machines in licensed venues; and
- gambling operators by use of licences, particularly exclusive licences – for example, exclusive licences have been granted to some TABs and casinos.

Many of the restrictions in gambling legislation reflect a desire to address actual or perceived social problems, for example, by limiting access to gambling opportunities. Licensing restrictions on operators are, in part, a response to the community's desire to minimise the probability that these activities might be involved with criminal elements (for example, as money laundering operations).

Nonetheless, restrictions often also have economic consequences. These consequences affect participants in gambling activities in a variety of ways, including:

- exclusive licensing, which by its nature, excludes other operators;
- consumers may be unable to purchase services as they would wish;
- effort can be directed into circumventing restrictions, as the Canberra Casino has done by opening a club in order to circumvent gaming machines being limited essentially to clubs;
- restrictions on involvement by third parties may alter the financing options available to some venue operators; and
- how restrictions are implemented – for example, the capping of the number of gaming machines in a jurisdiction should also take into account the best way of allocating the number of machines available.

Assessment

Given the complex social and economic issues raised, the Council decided that gambling regulation would be better examined outside the NCP assessment process. Noting that the Commonwealth had proposed a national inquiry by the PC into the social and economic impacts of gambling, the Council decided that it should wait for the outcome of that inquiry before considering governments' competition policy performance on compliance. The PC is due to report to the Federal Treasurer in November 1999.

While there have been some gambling regulation issues which could have been considered prior to the PC report, the Council considers that, rather than adopt a piecemeal approach to NCP assessment, there is greater value in a comprehensive assessment of all gambling legislation as part of the third tranche assessment.

Other gambling regulation matters

In December 1997, the New South Wales Government passed legislation which, amongst other things, granted the New South Wales TAB exclusive licences to operate on and off course totalisator wagering, linked jackpots and the Centralised Monitoring System (CMS). As required under clause 2(1) of the Code of Conduct, the New South Wales Government notified the ACCC and the Treasury that the legislation enacted provisions which relied on an exemption to competition law under section 51 of the *Trade Practices Act*. At the request of the Council, the New South Wales Government commissioned the Centre for International Economics (CIE) to undertake a net public benefit analysis of the exemptions. However, as has been noted before, all gambling legislation will be assessed by the Council in the light of the PC report. The CIE report will be considered at that time.

In May 1998, the New South Wales Government enacted further legislation granting the TAB an exclusive licence that required a section 51 exemption. This exclusive licence, known as an investment licence, will allow the TAB to purchase approved gaming devices and supply them to hotels, to finance the acquisition of devices by hoteliers and to share in the profits of a device supplied or financed by the TAB.

In notifying the ACCC and the Treasury (29 May 1998) of the section 51 exemption, the NSW Government noted that it is:

> *..of the view that the benefits to the community from the legislative exemption outweigh the costs, and that the objectives achieved by restricting competition by means of the legislative exemption can only be achieved by means of the legislative exemption.*

No further information has been provided. The granting of this licence raises clause 5(5) issues. A more detailed net benefit analysis will be necessary to satisfy the third tranche assessment.

B5.5.6 Taxis (all jurisdictions other than the Commonwealth)

Background

The taxi industry in Australia has been heavily regulated for many years. Key elements are:

- limits on licence (plate) numbers;
- regulation of taxi fares; and
- conduct (safety and quality) rules.

Owing to their scarcity in many areas, taxi licences have accrued a substantial market value. Licensees who obtained their licences some years ago have received substantial capital gains. However, this has been to the cost of taxi users as licensees seek a return on their investment ultimately via fares higher than they would be without limits on licence numbers.

The 1994 Industry Commission inquiry found that better access to taxi licences would have significant community benefits. It also acknowledged, as the Council does, that change will not be easy, because of the effects of deregulation on licensee wealth and differences in the circumstances of current licensees. Regulatory risk to wealth is a fact of life for all businesses and investors and, hence, it is factored into asset values and required returns. On the other hand, in respect of taxi licences, the values may also have had factored in an expectation of compensation or other measures to ameliorate the wealth impact should deregulation occur.

So far the Northern Territory has made the most progress in reviewing taxi licensing. Amendments to the *Commercial Passenger (Road) Act*, passed late last year, removed limits on the number of taxi licences from 1 January 1999. The Government has compensated existing licensees for the loss of value of their licence (which traded at up to $230 000 in Darwin). It is recovering this cost by charging operators an annual fee, ranging from $4 500 in Tennant Creek to $16 000 in Darwin, for the new licences. According to the Government, the number of taxis in Darwin has risen by 10 per cent just three months after deregulation and two new taxi networks have started operation.

The Northern Territory still has in place maximum fare restrictions that it intends to review in July 2000. The Government also introduced a new restriction on competition – minimum taxi network sizes[33] – as an interim measure this year with the aim of ensuring that networks are of a sufficient size to meet customer response time expectations. In response to Council concern about the justification for this new restriction, the Government has undertaken to treat it as an interim measure only and to start a competition policy review of it within a month.

Reviews are currently underway in Queensland, New South Wales, Victoria, South Australia and Western Australia. Tasmania and the ACT have yet to commence their respective reviews.

Assessment

The Council welcomes the progress made by the Northern Territory Government so far in removing several restrictions on competition in its taxi licensing regime. This has satisfied the Government's second tranche obligations in this area. The Council looks forward to the Government building on this very creditable progress by reviewing the restrictions on minimum taxi network size and fare maximums.

The Council highlights the compensation provided by the Government to licensees as illustrating one way in which barriers to reform in the community interest can be handled in a manner which is sensitive to sometimes concentrated wealth impacts of reform.

With all other jurisdictions still to complete their respective reviews, it is clear that taxi licensing will be a significant third tranche assessment issue. The Council will be looking to ensure that each jurisdiction does not allow the difficult issue of licence

[33] The minimums are: Darwin – 20 standard taxis or 5 executive taxis; and Alice Springs – 10 standard taxis or 5 executive taxis.

value impacts to colour their evaluations of the net community benefit of reform, but that it is dealt with as an adjustment matter.

B5.5.7 Animal Welfare Act 1992 and Food Act 1992 (ACT)

Background

In September 1997, the ACT Legislative Assembly passed amendments to the *Animal Welfare Act 1992* and the *Food Act 1992.* These amendments were intended to prohibit the sale in the ACT of eggs produced under the battery cage system, and to provide for labelling of eggs which are produced under the battery cage system. Clearly, there is an overlap in the effect of these two legislative amendments.

For the legislation to achieve its objective of prohibiting the sale of battery eggs in the ACT, it required that battery eggs be exempt from the *Mutual Recognition Act 1992*. Exemption from the *Mutual Recognition Act* requires the unanimous agreement of all other jurisdictions. Given that it introduced new restrictions, the legislation also triggered ACT Government responsibilities under clause 5(5) of the CPA: in essence, to show that the restrictions provided a net public benefit and were necessary to achieving the objective of the legislation.

Productivity Commission findings

In line with its obligations, the ACT Government commissioned the PC to undertake a public inquiry on whether it would be in the public interest for the ACT to:

- ban the sale of eggs from battery hens in the ACT;
- ban the production of eggs from battery hens in the ACT; and
- introduce a labelling requirement to indicate the conditions under which the hens produced their eggs.

The PC found that a ban on battery egg production in the ACT would improve hen welfare. It noted that the costs, which it estimated to be no more than $940 000 annually, would be borne by ACT consumers and it would be for the ACT to decide if the benefits, in terms of improved hen welfare, exceeded the estimated costs of such a ban.

ACT Government response

The ACT Government accepted the PC’s recommendations and moved to ban the sale and production of all battery eggs in the ACT. However, the ACT failed to gain unanimous support from the other jurisdictions for its legislation. Consequently, the legislation has no effect.

The labelling rules require the ACT producer to disclose how their eggs are produced. The ACT Government argued that this is consistent with competition policy because it means that consumers are in a position to make better informed decisions about their egg purchases. However, egg producers outside the ACT would not be subject to the additional labelling requirements for eggs they offer for sale within the ACT.

Assessment

The Council considers that the ACT has met its CPA obligations with respect to the *Animal Welfare Act 1992* and relevant provisions of the *Food Act 1992*.

B5.5.8 Resource development agreement legislation (Western Australia)

Background

At the first tranche assessment in June 1997, Western Australia had 84 Agreement Acts in place, including 64 resource development Agreement Acts. Only three Agreement Acts were scheduled for review. Other jurisdictions had similar, although fewer, Acts, and in most instances had listed these for review. Western Australia indicated it intended to repeal all non-operative and non-resources development Agreement Acts.

The Council sought and obtained a commitment from Western Australia to examine a small sample of its resource development Agreement Acts to determine the extent of competitive restrictions and to determine arrangements for reviewing other agreement legislation if significant restrictions on competition were found in the Acts reviewed. The sample Acts were agreed with the Council.

The review found that the three Agreement Acts impose few restrictions on competition. It also noted that the benefits flowing from the Acts are often not at the expense of taxpayers or other industries and are an ‘efficiency bonus’ for the developer arising from greater certainty and risk reduction.

The review identified several clauses which it recommended be removed, including those which impose small levels of cost that are not offset by benefits. It concluded that removal of these restrictions would confer only a small public benefit and that it would only be in the public interest to amend the agreements if this were done by mutual consent. For new agreements, the review suggested these clauses be excluded.

Western Australian Government response

The Western Australian Government stated that it endorses the findings of the review report. The Government also said that as the three Acts reviewed are representative of other resource development Agreement Acts, it does not consider it necessary to review remaining Agreement legislation.

Western Australia has undertaken to consider removal of restrictions imposing a net community cost at the time each Agreement Act is reviewed or varied. It will also ensure there is increased focus on the community impacts of new State Agreement Acts and will exclude provisions which do not confer a net community benefit through the State’s new legislation gate-keeping process.

Assessment

The Council considers that Western Australia’s approach meets the State’s obligations under the CPA.

B5.5.9 Digital television (Commonwealth)

Background

The *Television Broadcasting Services (Digital Conversion) Act* and *the Datacasting Charge (Imposition) Act*, assented to in July 1998, establish the framework for the conversion of free-to-air (FTA) television broadcasters to digital broadcasting and the basis for charging for access to the broadcasting spectrum for datacasting.[34]

Under the legislation, the Commonwealth will provide to each incumbent FTA broadcaster an additional 7 megahertz (MHz) of spectrum, for no additional charge, on condition that they (inter alia):

- commence digital transmissions by 1 January 2001 (later for regional broadcasters);
- transmit a minimum level of high definition programming (HDTV); [35]
- simulcast their programs on the existing analogue channels for at least eight years; and
- return a 7 MHz channel to the Government at the end of the simulcast period.

In addition, spectrum not required by the FTA broadcasters will be made available for datacasting on a competitive basis, and FTA broadcasters will be charged if they use their channels for datacasting purposes.

This legislation restricts competition in various ways, significantly by:

- extending the prohibition against new commercial television broadcasters until at least 31 December 2006, giving incumbent broadcasters protected access to Australian consumers and a head start in introducing the new technology; and
- prohibiting commercial FTA broadcasters from providing multiple and/or subscription programs on their digital channel, and requiring a minimum level of HDTV transmission.

The Commonwealth addressed its CPA clause 5(5) responsibilities through the preparation and release of a Regulation Impact Statement (RIS). Having examined three options, the RIS concluded that the restrictions are necessary to achieve the Government's objectives of: minimising disruption to consumers; maximising the use of existing transmission infrastructure; introducing digital television in Australia not significantly behind the rest of the world; and maximising viewer choice and diversity of product. It also noted that many of the regulations, including these restrictions, will be reviewed during the introduction and transition periods.

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[34] Datacasting is yet to be precisely defined but is generally understood to mean an Internet-style data service.

[35] HDTV provides a cinema-like viewing experience – a higher quality and widescreen picture with surround sound.

On 4 March 1999, the Commonwealth Treasurer asked the PC to examine regulatory arrangements for Australia's broadcasting services, including this legislation. This Inquiry will, amongst other things, apply the Commonwealth's analytical requirements under CPA clause 5(1). A draft report will be released for comment by October this year and a final report provided to the Treasurer by 5 March 2000.

Assessment

Current regulation of broadcasting in Australia reflects a legacy of restrictions on competition that aim to pursue multiple and sometimes conflicting policy objectives. The 1998 legislation attempts to facilitate technological change without disturbing this legacy and the associated balance of vested interests. However, the result has been, in the Council's view, that the restrictions extended or introduced by the legislation are not well targeted to achieve the Government's stated objectives.

The prohibitions on new commercial television broadcasters, and restrictions on the use of digital channels, are not obviously necessary to achieve the objectives of minimising disruption to consumers or maximising the use of existing infrastructure, and will directly frustrate the objective of maximising viewer choice and product diversity.

The linkage of the restrictions to the objective of introducing digital television on a timetable not significantly behind the rest of the world is not clear. The Commonwealth has argued that prohibiting entrants will avoid undermining the available advertising revenue base, and thus commercial viability, of incumbent broadcasters during the expensive conversion to digital. Typically, however, competition and the threat of entry is a powerful spur for the adoption of new technology. It might be that other factors, such as the long-standing ownership controls, constrain investment in digital broadcasting technology by incumbents and potential entrants alike. The Commonwealth has not presented sufficient evidence to determine whether this is the case and, if so, how long Australians might otherwise have had to wait before digital transmissions commenced.

Furthermore, the prohibition on multiple and/or subscription programs on the digital channels will both deny consumers important product choices, thus reducing the benefits of investing in digital reception equipment, and harm the economics of conversion for incumbent broadcasters. HDTV, which has been mandated by the Government, may well be of less net benefit to consumers – HDTV requires the consumer to invest in considerably more expensive reception equipment than is required to enjoy multiple and/or subscription digital programs.

The Council's view is that the RIS may have reached a different conclusion had it examined options better directed at achieving the Government's stated objectives, and had it given the impact of each on the community as a whole more weight. However, the legacy of restrictive regulation with its associated balance of vested interests means that incremental change is difficult and could have unintended and harmful long term consequences. The Council, therefore, welcomes the PC inquiry as an opportunity to consider, with a clean slate, what might be the minimum and most well targeted regulation necessary for this industry, in light of the forces of technological and global change. The Council will consider in its third tranche assessment the outcome of the inquiry and the Commonwealth's subsequent decisions.

B5.5.10 Commonwealth Government matters continuing from the first tranche assessment

National Health Act 1953 (Part 6 and Schedule 1) and the Health Insurance Act 1973 (Part 3) - Community Rating

In 1996, the Commonwealth referred to the (then) Industry Commission (IC) an inquiry into private health insurance. This inquiry included a review of the *National Health Act 1953 (Part 6 and Schedule 1)* and the *Health Insurance Act 1973 (Part 3)*. It reported in February 1997.

In its first tranche assessment, the Council found that the Commonwealth had not met its CPA obligations in this case. This was because the terms of reference for the inquiry specifically prevented examination of the Commonwealth's policy of retaining Medicare, bulk billing and community rating. The IC reported that community rating, which prevents registered funds from discriminating in relation to a contributor or a contributor's dependants, is perhaps the main regulatory influence on product and price competition amongst funds.

The Commonwealth noted in its second annual report that the *Health Legislation Amendment Act (No. 2) 1998* addressed a number of issues raised by the inquiry. The report did not otherwise respond to the Council's first tranche finding that the Commonwealth had failed to meet its CPA commitments.

In its 1999 Budget, the Commonwealth announced "Lifetime Health Cover", an initiative to promote private health insurance, under which insurance premiums paid by individuals will reflect the age at which they first join. As noted by the Commonwealth, it "*allows health funds to offer lower premium rates to people entering insurance early in their lives and higher premiums for people joining later*" (Commonwealth Department of Health and Aged Care, 1999). Notwithstanding this initiative, community rating will continue to underpin regulation of health insurance products and pricing.

Human Services and Health Legislation Amendment Act (No. 2) 1995, Health Insurance Amendment Act (No. 2) 1996 – Medicare provider numbers

The Commonwealth introduced new legislation, the *Human Services and Health Legislation Amendment Act (No. 2) 1995* and the *Health Insurance Amendment Act (No. 2) 1996*. This legislation has the effect of limiting the Medicare provider numbers available annually to new doctors, therefore, restricting entry to private medical practice. According to the Commonwealth its objective is, inter alia, to restrain increasing Medicare costs induced by an increasing supply of general practitioners.

The Council found in its first tranche assessment that the Commonwealth had failed to provide a substantive public benefit justification in support of the new restriction and appeared not to have examined alternative (non-restrictive) means of achieving the objectives of this legislation.

The Commonwealth's second annual report notes that this legislation contains review mechanisms. Specifically:

- section 19AA inserted in the *Health Insurance Act 1973* sunsets on 1 January 2002 – this section denies Medicare benefits in respect of medical services provided by/on behalf of practitioners who commenced practice on or after 1 November unless the practitioner meets certain criteria; and

- section 3GC inserted in the same Act establishes a Medical Training Review Panel, to compile and publish information on medical training and employment opportunities, whose reports are laid before Parliament by the Minister.

In the Council's view, these mechanisms do not discharge the Commonwealth's CPA obligation to have evidence that the legislation is consistent with the guiding legislative principle.

Health Insurance Act 1973 (Part IIA) – pathology licensing

Part IIA of the *Health Insurance Act 1973* has the effect of limiting the number of pathology outlets that can provide services eligible for Medicare benefits. In the first tranche assessment, the Council outlined its view that this piece of legislation, which was not then on the Commonwealth's review program, warranted review. Subsequently, the Minister for Health and Family Services agreed to examine competition matters associated with this piece of legislation under the review program.

The Commonwealth's second report to the Council confirms that this piece of legislation has been added to the Commonwealth's program for review in 1998-99.

Quarantine Act 1908

The Council's first tranche assessment noted that the Nairn Review of the *Quarantine Act 1908* did not address the fundamental questions expected of an NCP review. The assessment also noted that the Commonwealth had agreed to identify those elements of the Act which restrict competition and were not examined by the Nairn Review and test them for compliance with the CPA.

The Commonwealth's second report notes that the Department of Agriculture, Fisheries and Forestry will commence this review in 1999.

B6 The Conduct Code Agreement

B6.1 The Conduct Code obligations

Under the Conduct Code Agreement, the Commonwealth, States and Territories are required to report legislation reliant on section 51(1) of the *Trade Practices Act 1974* to the Australian Competition and Consumer Commission (ACCC). The reporting obligations are:

- to notify the ACCC of legislation that relies on section 51(1) within 30 days of the legislation being enacted or made (clause 2(1)); and
- to have notified the ACCC by 20 July 1998 of legislation relying on the version of section 51(1) in force at 11 April 1995 that will continue pursuant to the current section 51(1) (clause 2(3)).

In assessing progress against the Conduct Code obligations, the Council sought advice from the ACCC, to determine whether jurisdictions satisfied the notification requirements of the Conduct Code.

In addition, because new legislation reliant on section 51(1) is, by definition, new legislation that restricts competition, jurisdictions are required to demonstrate that new legislation reliant on section 51(1) satisfies the competition tests in clause 5(5) of the CPA. The Council wrote to all jurisdictions on 18 June 1998 to ensure that jurisdictions were aware that Conduct Code obligations were relevant to the June 1999 assessment of NCP progress.

B6.2 Compliance with obligations by jurisdiction

The current progress of each jurisdiction is outlined below, based on information which jurisdictions and the ACCC have provided to the Council.

Commonwealth

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation reliant on section 51(1) has been enacted since 11 April 1995:

- *Trade Practices Amendment (Country of Origin Representations) Act 1998* (notified 7 August 1998);
- *Australian Postal Corporation Act 1989* (notified 15 July 1998);
- *Wheat Marketing Legislation Amendment Act 1998* (notified 11 August 1998); and
- *Year 2000 Information Disclosure Act 1999* (notified 10 March 1999).

Commitment under clause 2(3)

The Commonwealth has advised that it has no legislation that has implications for clause 2(3).

New South Wales

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation reliant on section 51(1) has been enacted since 11 April 1995:

- *Liquor and Registered Clubs Legislation Amendment (Community Partnership) Act 1998* (notified 29 May 1998);
- *Totalizator Legislation Amendment Act 1997* (notified 10 December 1997);
- *Sydney Organising Committee for the Olympic Games Act 1996*;
- *Marketing of Primary Products Amendment (Rice Marketing Board) Act 1998* (notified 30 July 1998);
- *Marketing of Primary Products Amendment (Wine Grapes Marketing Board) Act 1997* (notified 30 July 1998);
- *Diary Industry Amendment (Trade Practices Exemption) Act 1998* (notified 30 July 1998);
- *Farm Produce (Repeal) Act 1996* (notified 30 July 1998);
- *Competition Policy Reform (NSW) Amendment (Waste) Regulation 1998* (notified 30 July 1998);
- *Competition Policy Reform (NSW) Amendment (*Grain Marketing*) Regulation 1998* (notified 30 July 1998); and
- *Competition Policy Reform (NSW) Amendment (SOCOG and SPOC) Regulation 1998* (notified 30 July 1998).

Commitment under clause 2(3)

The New South Wales Government advised the ACCC on 10 July 1998 of the following legislation that had implications for clause 2(3):

- *Marketing of Primary Products Act 1983*;
- *Grain Marketing Act 1991*; and
- *Co-operatives Act 1992*.

New South Wales further advised that these Acts are either currently under, or scheduled for, competition policy legislation reviews.

Victoria

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *Legal Practice Act 1996* – Schedule 2 of the Act provided for a temporary exemption which expired on 30 June 1997;
- *Electricity Industry (Trade Practices) Regulations 1994* – Regulation 4 operated until 30 June 1996;
- *Competition Policy (Gas Supply Contract Exemption) Regulations 1996* – Regulations 5 & 7 operated until 20 November 1997;
- *Gas Industry Act 1994* (notified 17 July 1998);
  - Part 6B, Competition Policy Authorisation;
    - = section 62M as from 3 June 1997, amended by 91/97;
    - = section 26 as from 8 June 1998;
    - = section 27 as from 11 December 1997 and amended by 40/98;
    - = section 62O as from 3 June 1997;
    - = section 62P as from 3 June 1997;
  - Part 6C, Master Agreements;
    - = section 62Q, section 62S and section 62T as from 8 June 1998;
- *Electricity Industry Act 1993* – section 91AA inserted by 8/1996, section 13, as from 25 June 1996 and to be repealed from 1 January 2001 by section 14 of 8/1996 (notified 17 July 1998).

Commitment under clause 2(3)

Victoria has advised that it has no legislation that has implications for clause 2(3).

Queensland

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *Competition Policy Reform (Queensland – Dairy Produce Exemptions) Amendment Regulation (No. 1) 1997* (notified 12 July 1997);

- *Competition Policy Reform (Queensland – Dairy Industry Exemptions) Regulations 1998* (notified 31 July 1998);
- *Competition Policy Reform (Queensland – Chicken Meat Industry Exemptions) Regulations 1998* (notified 31 July 1998); and
- *Competition Policy Reform (Qld Sugar Industry Exemptions) Regulation 1998*, to expire 31 December 1999 (notified 31 July 1998).

Commitment under clause 2(3)

Queensland has advised that it has no legislation that has implications for clause 2(3).

Western Australia

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *North West Gas Development (Woodside) Agreement Amendment Act 1996* (notified 2 August 1996).

Commitment under clause 2(3)

The Western Australian Government advised the ACCC on 18 July 1998 of the following legislation that had implications for clause 2(3):

- *North West Development (Woodside) Agreement Act 1979*.

Western Australia further advised that this Act is scheduled for competition policy legislation review.

South Australia

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *Dairy Industry Act 1992* (notified 15 July 1998).

Commitment under clause 2(3)

The South Australian Government advised the ACCC on 15 July 1998 of the following legislation that had implications for clause 2(3):

- *Cooper Basin (Ratification) Act 1975;*
- *Stony Point (Liquids Project) Ratification Act 1981;*
- *Roxby Downs (Indenture Ratification) Act 1982* – has an enabling provision to provide for authorisation, however no authorisation has been provided to date; and

- *Industries Development Act 1941* – contains an enabling provision to provide for authorisation that has not been used to date.

Tasmania

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *Electricity Supply Industry Act 1995* (notified 16 July 1998); and
- *Electricity Supply Industry Restructuring (Savings and Transitional Provisions) Act 1995.*

Commitment under clause 2(3)

Tasmania has advised that it has no legislation that has implications for clause 2(3).

Australian Capital Territory

Commitment under clause 2(1)

The ACCC has been notified that the following new legislation relying on section 51(1) has been enacted since 11 April 1995:

- *Milk Authority (Amendment) Act 1997* – the exemption was initially for a period of 12 months however, an extension has been agreed by the ACT until June 2000 (notified 9 September 1998, ACCC has not been notified of extension).

Commitment under clause 2(3)

The ACT has advised that it has no legislation that has implications for clause 2(3).

Northern Territory

Commitment under clause 2(1)

The Northern Territory has advised that it has no legislation that has implications for clause 2(1).

Commitment under clause 2(3)

The Northern Territory has advised that it has no legislation that has implications for clause 2(3).

B6.3 Assessment

The Council is satisfied that all jurisdictions have met their obligations under clauses 2(1) and 2(3) of the Conduct Code.

The Council notes that jurisdictions have an ongoing obligation under clause 2(1) of the Conduct Code to notify the ACCC of all new legislation reliant on section 51(1) of TPA within "***30 days*** *of the legislation being enacted or made"***.**

B7 Electricity

B7.1 NCP commitments

State and Territory governments' electricity NCP commitments arise from the *Agreement to Implement the National Competition Policy and Related Reforms,* the *Competition Principles Agreement* (CPA) and other Agreements on Related Reforms for the Electricity Sector (Electricity Agreements).[1]

First, clause 4 of the CPA provides that, before introducing competition into a market traditionally supplied by a public monopoly and before privatising a public monopoly, governments will:

- remove from the public monopoly any responsibilities for industry regulation; and
- conduct a review of structural and competitive arrangements in the industry.

Second, the *Agreement to Implement the National Competition Policy and Related Reforms* requires that each participating State and Territory implement electricity reforms specified in the relevant Council of Australian Governments (COAG) agreements with the aim of establishing a competitive National Electricity Market (NEM) by 1 July 1999.

Third, the Electricity Agreements on the structure of the electricity industry commit jurisdictions, prior to their participation in the NEM, to have:

- structurally separated generation from transmission; and
- ring-fenced the retail and distribution businesses.

As early as 1994, COAG identified the main objectives for a fully competitive NEM to operate from 1 July 1999 as follows:

- the ability for customers to choose the supplier, including generators, retailers and traders, with which they will trade;
- non-discriminatory access to the interconnected transmission and distribution network;
- no discriminatory legislative or regulatory barriers to entry for new participants in generation or retail supply; and
- no discriminatory legislative or regulatory barriers to interstate and/or intrastate trade.

COAG supported these broad objectives in the April 1995 inter-governmental agreements that link NCP payments to the implementation of specified electricity

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[39] NCP agreements on electricity are reproduced in the Council's *Compendium of National Competition Policy Agreements (June 1998).*

reforms. Subsequently, on 10 December 1996, the Prime Minister wrote to all Heads of Government seeking endorsement of a revised implementation timetable for national electricity reform. Under the 10 December 1996 timetable, participating jurisdictions agreed to:

- have the *National Electricity Code* (NEC) authorised by the Australian Competition and Consumer Commission (ACCC) (for the purposes of Part VII of the *Trade Practices Act 1974*[2]) and accepted as an industry access code by the ACCC (for the purposes of the undertaking provisions of Part IIIA of the *Trade Practices Act 1974)* by April/May 1997; and

- fully implement the market arrangements specified in the NEC by early 1998 requiring:

  - the National Electricity Market Management Company (NEMMCO) to have successfully installed and tested the information technology systems;

  - each jurisdiction to have promulgated and applied the National Electricity Law; and

  - NEMMCO and the National Electricity Code Administrator (NECA) to have assumed full operational responsibilities for the national market.

Achievement of the COAG objectives therefore requires the formal commencement of the NEM and participating jurisdictions (New South Wales, Victoria, South Australia and the ACT) to complete the transition to a fully competitive NEM, by 1 July 1999, to fulfil the second tranche NCP commitments.

The NEC also includes derogations where each participating jurisdiction has specified transitional provisions that will operate to ensure a smooth transition from the existing electricity industry regulatory arrangements to the NEM. Derogations from the NEC include technical requirements, contestability timetable,[3] transmission and distribution network connections and transmission losses. The derogations also enable jurisdictions to honour existing contracts which do not conform to the NEC.

Most of the derogations are scheduled to terminate on or before 31 December 2002, which means that they are largely a third tranche issue. However, for the second tranche assessment, NCP commitments require jurisdictions to have made sufficient progress to enable the year 2002 timetable to be met.

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40 Authorisation under Part VII of the TPA provides immunity from court action for certain types of arrangements or conduct that would otherwise be in breach of Part IV of the TPA.

41 Contestable customers in the retail market are those customers who can choose their supplier from the various licensed retailers operating in the market. The NEC requires each jurisdiction to nominate the persons that may register as a contestable customer under the NEC.

The National Electricity Market

The NEM is a wholesale market for the supply and purchase of electricity combined with an access regime for use of the transmission and distribution networks in New South Wales, Victoria, South Australia and the ACT. Queensland and Tasmania are expected to participate in the NEM upon interconnection with New South Wales and Victoria, respectively.

The NEM commenced on 13 December 1998 and is expected to increase efficiency in the electricity supply industry by introducing competition directly into the generation and retail sectors.

The principles of the NEM are set out in the NEC that consolidates new and existing interstate trading arrangements such as the wholesale market pool, technical standards and access to the network. Two new organisations, NECA and NEMMCO have been established to regulate and manage the NEM.

Market behaviour is regulated in a light-handed manner with market conduct and pricing oversight subject to national competition law administered by the ACCC. State and Territory regulators are responsible for the economic regulation of distribution services, contestability timetable, environmental standards, distribution and retail licence conditions, and health and safety. State and Territory regulators are currently responsible for the regulation of transmission services, however, the NEM arrangements provide for the ACCC to assume, on a progressive basis from 1 July 1999, the regulation of transmission services.

Conduct Code Agreement: reporting obligations

The *Conduct Code Agreement* requires that jurisdictions notify the ACCC of legislation that is reliant on section 51(1) of the TPA. Legislation reliant on this section is anti-competitive and this places an obligation on jurisdictions to demonstrate that such legislation satisfies clause 5 of the CPA. The Council is aware of two jurisdictions that have electricity industry related legislation reliant on section 51(1) of the TPA: Victoria and Tasmania.

B7.2 Progress against NCP commitments

Introduction

The NEM commenced on 13 December 1998 resulting in a competitive market for the supply and purchase of electricity in the participating jurisdictions, namely, New South Wales, Victoria, South Australia and the ACT. This satisfies the *Agreement to Implement the National Competition Policy and Related Reforms* requirement that each participating State and Territory must implement the required reforms to enable the establishment of a competitive NEM by 1 July 1999.

The ACCC received applications from:

- NECA and NEMMCO to authorise, under Part VII of the TPA, the proposed electricity wholesale market arrangements within the NEC; and

- NECA to accept, under Part IIIA of the TPA, an access code for the electricity transmission and distribution networks.

On 10 December 1997, the ACCC authorised the NEC. The ACCC accepted the NEC as an access code under the TPA on 16 September 1998. In making its authorisation and access decisions, the ACCC recognised that the current arrangements are an appropriate starting point but that significant deficiencies remain. When authorising the NEC, the ACCC imposed a number of conditions highlighting these deficiencies in the design of the NEM. These deficiencies include:

- market distortions due to price caps and floors;
- the potential for more commercially orientated solutions in areas such as reserve trader and ancillary services provision; and
- competition implications of various jurisdictional derogations such as generator technical standards.

The Council considers that the ACCC's authorisation and acceptance of the NEC signifies that the market arrangements specified in the NEC are an appropriate start to the NEM. But the Council also acknowledges that the ACCC's decisions were highly qualified, and improvements to the current arrangements are an ongoing requirement to facilitate the establishment of a satisfactory set of arrangements.

The Council notes that, in accordance with the Prime Minister's letter of 10 December 1996, NEMMCO and NECA have assumed full operational responsibilities for the national market.

Issues common to jurisdictions

Generally, the NEM is achieving its objectives. However, the Council accepts that implementation problems have had an impact on realising the full benefits of electricity reforms. To varying degrees, jurisdictions have encountered the following problems:

- timetable slippage in derogations (such as retail contestability) as a result of the delayed NEM start;
- implementing metering arrangements in relation to the introduction of retail contestability;
- inability to pass desired legislation; and
- understanding the operational responsibilities of NEMMCO and NECA.

Emerging NEM issues

Now that the NEM is operational, and competition in contestable services well established, some important issues are emerging which may require a reconsideration of reform policy, or raise questions about future compliance with NCP agreements. The Council will retain an ongoing interest in these issues – and anticipates that electricity reform will be a major focus of the third tranche assessment.

First, questions are being raised about the efficacy of NEC rules on the approval of regulated versus unregulated transmission interconnectors. This is a difficult issue. On the one hand, there appears to be growing interest in the construction of strategic unregulated interconnects (for example, the proposed unregulated connection between New South Wales and Queensland). On the other hand, many argue that the current rules for approving regulated interconnects are unworkable, citing experience with the proposed SANI regulated inter–connect between New South Wales and South Australia as an example. As a result, it is argued, regulated interconnects which are demonstrably in the public interest won't be constructed. The National Electricity Code Authority (NECA) pricing review is examining this issue. The Council would be concerned by any Government actions – outside the formal NEM processes – to impede construction of interconnectors.

Second, there are suggestions that publicly owned electricity generators have been competing on unfair terms with private generators. It is suggested that the publicly owned generators are not required to earn a commercial return on their assets and/or are subsidised in some way by their owner governments and, as a consequence, are gaining a greater share of the NEM market than they otherwise would. This is a competitive neutrality issue, since the claim is that businesses are attaining a market advantage derived solely from public ownership. However, no complaint has been lodged with the appropriate competitive neutrality complaints authority, and so the suggestions have not been tested.

Third, there have also been suggestions that States should revert to state–based markets and interstate trade in electricity should be abandoned. The Council would have serious concerns over any moves to restrict the operation of the NEM. The development of national markets in electricity services, and other utility services such as gas, is a cornerstone of NCP. NCP includes a mechanism to deal with any competitive neutrality problem, to the extent that it exists, and any inadequacies in this mechanism should be addressed directly.

Jurisdictions' ongoing commitments

Jurisdictions are at various stages with their electricity reform program. The Council considers that realistic and therefore achievable timetables are necessary to ensure effective and efficient implementation of NCP commitments. The electricity reforms adopted to date are a starting point against which the future electricity reforms will be measured.

The Council intends to closely monitor jurisdictions' ongoing progress against electricity reform commitments to ensure that an environment conducive to the introduction of competition is fostered. The Council's third tranche assessment will focus on the progress jurisdictions have made in achieving a fully competitive electricity market. The Council will focus on whether jurisdictions have achieved, or have an appropriate timetable to achieve, full retail competition. This will include contestability timetables, mechanisms to deal with issues such as metering and the ongoing effect of vesting contracts. The Council will also examine the continued appropriateness of any remaining derogations, recognising that while jurisdictions need mechanisms to allow for a smooth transition to a fully competitive market, derogations should only be in place for the minimum time possible to achieve a smooth transition.

The Council recognises that the establishment of the NEM and the structural reforms made by each jurisdiction are an important start to the creation of a fully competitive electricity market. However, considerable work remains to be done to see the full benefit of the reforms flow through to users and the Council will be considering, in its third tranche assessment, how well this has been achieved.

B7.2.1 NEM participating jurisdictions

New South Wales

Structural reform

In February 1995, the transmission activities of the government-owned vertically integrated electricity utility, Pacific Power, were separated to become the Electricity Transmission Authority (trading as TransGrid), with Pacific Power's activities confined to generation.

In early 1996, Pacific Power was separated into three independent, government-owned generation businesses known as Pacific Power, Delta Electricity and Macquarie Generation. Pacific Power is responsible for the State's entitlement of 58 per cent of the Snowy Mountains Hydro Electric Authority.

Twenty five distributors were amalgamated to form six State-owned corporations with the monopoly network functions being ring-fenced from retail services.

Regulatory reform

The Independent Pricing and Regulatory Tribunal (IPART) will regulate transmission pricing until 30 June 1999, when it will be regulated by the ACCC. IPART will continue to regulate distribution pricing and electricity tariffs for franchise customers until the retail market is fully contestable.

Interconnection with Queensland

A New South Wales Government-owned distributor and retailer, NorthPower, has commenced development of DirectLink, which is an interconnection to link the Tweed Valley to the New South Wales electricity grid. The project is scheduled for completion by January 2000.

TransGrid and Powerlink Queensland intend to build an interconnector between New South Wales and Queensland. This is due for completion in the year 2001.

National Electricity Law

Through the *Electricity Supply (NSW) Act 1995*, New South Wales has adopted the National Electricity Law.

Retail competition in electricity supply

From October 1996, customers who use in excess of 40GWh per year have been able to choose suppliers. As of 1 July 1998, customers in the range of 160MWh to 750 MWh per annum have been contestable. By 1 July 1999 businesses with many

small sites of 100MWh per annum and greater, will be able to aggregate their consumption to become contestable. Small customers who consume less than 160 MWh per annum will become contestable over a period commencing from 1 January 2001.

Assessment

The Council is satisfied that New South Wales has met its second tranche electricity reform commitments for the following reasons:

- New South Wales has met its structural commitments by restructuring the regulatory and operating sectors of the electricity sector;
- the separation of the natural monopoly (transmission and distribution) and competitive components (generation and retail) is consistent with the Electricity Agreements;
- New South Wales is continuing to pursue NorthPower's DirectLink interconnection and TransGrid/Powerlink's Queensland interconnector;
- New South Wales has promulgated and applied the National Electricity Law; and
- consistent with a competitive NEM, New South Wales is progressively allowing customers to choose their electricity supplier.

As part of the third tranche assessment, the Council intends to consider New South Wales' progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Victoria

Structural reform

In October 1993, the Victorian Government reformed the State Electricity Commission of Victoria (SECV) into three separate businesses: Generation Victoria (generation); National Electricity (transmission); and Electricity Services Victoria (distribution).

National Electricity was separated into two businesses: the Victorian Power Exchange (administers the market and oversees the system control); and PowerNet Victoria (owns and maintains the transmission assets that form the physical network). Electricity Services Victoria was separated into five distribution businesses, each comprising an energy retailing arm and a regulated, local, geographic wires monopoly. Generation Victoria operated as an interim structure comprising five groups of power stations trading as independent, competing generators.

During the second half of 1995, all five distribution businesses were sold to the private sector. Subsequently, Victoria has privatised all wholly-owned generation businesses, its share of the Loy Yang B generator and its transmission utilities.

Regulatory reform

Victoria has established an independent economic regulator, the Office of Regulator General, who monitors price and service levels. The Office of Chief Electrical Inspector has been created to ensure industry compliance with set regulations, and auditing and monitoring of industry behaviour against statutory safety outcomes. An Energy Ombudsman has also been established to protect consumer interests and to resolve disputes between customers and energy businesses in the gas and electricity industries.

Conduct Code Agreement: reporting obligations

In accordance with clause 2(1) of the CCA, the Victorian Government has notified the ACCC of section 91AA of the *Electricity Industry Act 1993* which is new legislation that relies on section 51(1) of the TPA. Section 91AA of the *Electricity Industry Act 1993* will be repealed from 1 January 2001.

In accordance with clause 5 of the CPA, Victoria has reviewed the *Electricity Industry Act 1993*. This review was completed in January 1998. It is yet to be released as the Government is considering the recommendations.

National Electricity Law

The *Electricity Industry Act 1993* enables Victoria to apply the National Electricity Law to Victoria.

Retail competition in electricity supply

Customer thresholds for participation in the wholesale market have been, and will continue to be, progressively reduced. On 1 July 1996, approximately 2000 customers with annual consumption of at least 750 MWh became contestable. From 1 July 1998, customers with an annual consumption of at least 160 MWh became contestable. The final phase is scheduled for 1 January 2001, when all sites, including households, will be contestable.

Assessment

The Council is satisfied that Victoria has met its second tranche electricity reform commitments for the following reasons:

- Victoria has completed all its structural reform commitments through the structural separation of generation and transmission, and ring-fencing of retail and distribution businesses;

- Victoria has separated the regulatory role from the commercial aspects of the industry through the establishment of the Office of Regulator General;

- Victoria has promulgated and applied the National Electricity Law; and

- sufficient progress has been made with the contestability timetable such that all customers will become contestable on 1 January 2001.

As part of the third tranche assessment, the Council intends to consider Victoria's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

South Australia

Structural reform

On 1 January 1997, Optima (South Australian Generation Company) was separated from the Electricity Transmission South Australia (ETSA) Corporation.

During June 1998, the South Australian Government undertook a review of the restructuring of the South Australian electricity supply industry pursuant to clause 4 of the CPA. This review recommended that South Australian electricity sector be restructured into three separate generation companies: a transmission company; a single stapled ring-fenced distribution/retail company (with distribution and retail assets held in separate subsidiaries under a common holding company); and a separate gas trader.

On 12 October 1998, in accordance with the review recommendations, Optima was restructured into three new generation companies, namely, Optima Energy, Flinders Power and Synergen and a separate gas trader company was formed. The charters of the three government-owned generation companies contain provisions requiring them to operate on a competitive basis.

The remainder of the ETSA Corporation was disaggregated to form ElectraNet SA (transmission entity with ring-fenced system control), with the distribution and retail businesses maintained under a common holding company as stapled ring-fenced subsidiaries called ETSA Utilities Pty Ltd and ETSA Power Pty Ltd respectively.

Each of the businesses (with the exception of ElectraNet SA) were transferred to new Corporations Law companies.

The *Electricity Corporations (Restructuring and Disposal) Act* permits the long term lease of electricity generation, transmission and distribution assets, and the sale of associated assets.

Regulatory reform

South Australia proposed a range of new regulatory arrangements in conjunction with the structural reforms. These arrangements cover the following:

- an Electricity Ombudsman to deal with customer complaints;
- an Independent Industry Regulator, responsible for pricing, licensing and network access;
- an Electricity Supply Industry Planning Council;
- a Sustainable Energy Authority; and

- a Technical Regulator, responsible for safety and technical service requirements.

The legislative package to give effect these arrangements will be introduced into Parliament in June 1999. It is expected that the legislation will be passed in August 1999.

National Electricity Law

As lead legislator for the NEM, South Australia passed the *National Electricity (South Australia) Act 1996* in June 1996 and proclaimed the Act on 8 December 1998, providing for South Australia's entry into the NEM on 13 December 1998.

Retail competition in electricity supply

Since 20 December 1998, customers with an annual single site average load of at least 4GWh have been able to choose their own supplier. Customers with an annual usage of at least 750MWh and 160MWh will become contestable from 1 July 1999 and 1 January 2000 respectively. The remaining customers will become contestable on 1 January 2003.

Derogations

The South Australian government has lodged an authorisation application with the ACCC for the South Australian vesting contracts.

Assessment

The Council is satisfied that South Australia has met its second tranche electricity reform commitments for the following reasons:

- South Australia has separated the natural monopoly (transmission and distribution) and competitive components (generation and retail);
- South Australia's clause 4 review was rigorous and independent;
- the South Australian Government's announced intention to adopt the review recommendations ensures compliance with the Electricity Agreements and CPA obligations;
- South Australia has promulgated and applied the National Electricity Law; and
- the staged implementation of retail competition is in progress.

South Australia proposes to establish the regulatory bodies recommended in the clause 4 review by August 1999. The Council will undertake an interim assessment of South Australia's progress before 31 December 1999.

As part of the third tranche assessment, the Council intends to consider South Australia's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Australian Capital Territory

Structural reform

ACTEW was corporatised on 1 July 1995. Progressively since 1995, the ACT government has implemented structural reforms consistent with those required by clause 4.

In preparation for the proposed sale of ACTEW, the ACT Government commissioned two reviews to determine the most appropriate structure and public benefit issues that would arise from privatisation. The Fay Richwhite Review (1998) examined risks and strategic issues in a changing business environment. The ABN AMRO/DGJ Projects Scoping Study of ACTEW (1998), considered structure and ownership options.

ABN AMRO/DGJ Projects recommended that the preferred course of action is to sell ACTEW as a multi-utility, however, if a sale does not proceed, the Government should continue to operate ACTEW as a multi-utility. A key issue raised in the scoping study is that under either public or private ownership, the Government should implement a full regulatory framework for electricity, water and sewerage. This could be achieved by broadening the regulatory powers of the independent pricing and access regulator, the Independent Pricing and Regulatory Commission (IPARC).

Regulatory reform

In 1995 when ACTEW was corporatised, the regulatory functions that were traditionally undertaken by the Electricians' Licensing Board (a public monopoly), were transferred to the Department of Urban Services.

Under the *Electricity Supply Act 1997*, the ring-fencing of electricity retail and distribution businesses is a licensing requirement (there are separate requirements for distribution and retailing). IPARC, the economic regulator, examines and tests the adequacy of ring-fencing in the context of its pricing references.

National Electricity Law

The relevant ACT legislation that gives effect to the National Electricity Law, the *Electricity (National Scheme) Act 1997*, was passed prior to the commencement of the NEM.

Retail competition in electricity supply

Since 28 June 1998, customers with an annual usage of more than 160 MWh at a single site are able to choose their retailer. A process, whereby all customers will be contestable, is scheduled for 1 January 2001.

Assessment

The Council is satisfied that the ACT has met its second tranche electricity reform commitments for the following reasons:

- since corporatisation of ACTEW in 1995, the ACT has implemented a number of structural reforms. These reforms include the separation of the regulatory and commercial functions of ACTEW, consideration of the appropriate commercial objectives of ACTEW and analysis of the merits of separating the potentially competitive elements of ACTEW;
- the ACT has promulgated and applied the National Electricity Law; and
- the ACT has made sufficient progress towards full customer contestability by 1 January 2001.

As part of the third tranche assessment, the Council intends to consider the ACT's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

B7.2.2 Proposed NEM participating jurisdictions

Queensland

Structural reform

In January 1995, the Queensland Government divided the Queensland Electricity Commission (QEC) into AUSTA Electric (generation) and the Queensland Transmission and Supply Corporation (QTSC). QTSC operated as a holding company for eight subsidiaries, comprising seven regionally-based electricity boards and the Queensland Electricity Transmission Corporation (trading as Powerlink Queensland).

On 1 July 1997, AUSTA Electric was separated into three independent and competing generation corporations:

- Stanwell Corporation;
- Tarong Energy Corporation; and
- CS Energy.

An engineering corporation, AUSTA Energy, was also established.

QTSC's subsidiaries were established as independent government-owned corporations. However, the retailing functions were removed from the distributors and three retail corporations were established.

In February 1999, the Queensland Government announced the following reforms to the electricity industry:

- the engineering corporation, AUSTA Energy is to be wound up;
- the establishment of an Electricity Monitoring Unit to address concerns about maintenance practices within the industry;

- the six separate regional distributors, which currently own Ergon Energy, will be amalgamated into a single corporation known as Ergon, with Ergon Retail operating as a subsidiary; and
- regional electricity councils are to be created across the State to provide direct community input to distribution corporations.

The restructure of the distribution corporations aims to reduce the number of reporting lines to shareholding Ministers, facilitate a more co-ordinated approach to regional development of the distribution sector, and provide a more workable arrangement for the ownership and business development of the retailing corporation.

Regulatory reform

It is not clear to the Council whether the Minister for Mines and Energy or the Queensland Competition Authority is the economic regulator in Queensland.

From 1 January 2002, the ACCC assumes the role of transmission pricing. However, this date may be brought forward in line with other jurisdictions.

Interconnection with New South Wales

Although Queensland is not physically linked to the NEM, it is currently operating the same market model as the NEC. Upon interconnection with New South Wales, Queensland intends to fully participate in the NEM.

Queensland has accelerated the completion of the Powerlink/Transgrid interconnector from the original date of October 2001 to January 2001. Interconnection may occur prior to January 2001 due to the construction of a private unregulated link.

National Electricity Law

Legislative amendments made to the *Electricity Act 1994* during 1997 gave effect to the establishment of a NEM.

Retail competition in electricity supply

Queensland has implemented the second stage of retail competition (for customers using greater than 4 GWh per year). Work is continuing on the implementation of the remaining tranches of contestability, with a view to having full retail contestability in January 2001.

Assessment

The Council is satisfied that Queensland has met its second tranche electricity reform commitments:

- Queensland has met its Electricity Agreements commitments by structurally separating generation from transmission and having separate distribution and retail companies, in preparation for its participation in the NEM;

- Queensland has reaffirmed its commitment to interconnect with New South Wales by 2000-01. The Council acknowledges that once Queensland is connected to the NEM it will become a full participant in the NEM; and
- implementation of the second stage of retail competition is on track to achieve full retail contestability in January 2001.

As part of the third tranche assessment, the Council will consider Queensland's progress in achieving a fully competitive electricity market, focussing on retail competition, particularly contestability timetables, mechanisms to deal with issues such as metering, the ongoing effect of vesting contracts and continued appropriateness of any remaining derogations.

Tasmania

Structural reform

On 1 July 1998, Tasmania structurally separated its vertically integrated public utility, the Hydro-Electric Corporation (HEC). The HEC has been separated into the following three businesses:

- Transend Networks Pty Ltd (Transend), a state-owned company that operates under the Corporations Law with responsibility for the transmission of electricity through the extra high voltage transmission network;
- Aurora Energy Pty Ltd (Aurora), a state-owned company that also operates under the Corporations Law with responsibility for the distribution of electricity (through the lower voltage networks) and retailing. Aurora has an exclusive retail licence for all of Tasmania, excluding the Bass Strait Islands; and
- HEC, a government business enterprise responsible for the generation of electricity and system control (ring-fenced) on mainland Tasmania. HEC is also responsible for generation, distribution and retailing on the Bass Strait Islands.

Structural review of the distribution/retail business

Prior to the establishment of Aurora, a CPA clause 4 review of HEC's distribution and retail businesses was conducted. In its final report of December 1997, the review committee made the following recommendations:

- prior to the introduction of competition, the distribution and retail businesses of the HEC should remain as an integrated entity, with ring-fencing (accounting separation) of the distribution and retail functions;
- when competition is introduced into the Tasmanian retail electricity market, the distribution and retail businesses of the HEC should be carried out by separate legal entities; and
- that there be no further disaggregation into multiple distribution and retailers.

The Tasmanian Government accepted the majority of these recommendations, particularly in relation to establishing appropriate regulatory arrangements for the

distribution/retail business. However, the Government did not accept the recommendation that distribution and retail should be conducted by separate legal entities when competition is introduced. The Government considered that ring-fencing would provide appropriate competitive safeguards. Consequently, Aurora was established as a single distribution/retail business.

Structural review of the HEC's generation activities and the system control function

A clause 4 review of HEC's generation business commenced in March 1999. The review team released an Issues Paper on 29 March 1999 and was required to report to the Government by 30 April 1999.

Regulatory reform

The independent Electricity Regulator is responsible for the regulation of electricity prices, ensuring that the regulatory framework is transparent, independent of government and co-ordinated within a single body.

A key objective of the Electricity Regulator is to promote efficiency and competition in the electricity supply industry, which means that the Electricity Regulator has obligations to ensure that the ring-fencing arrangements are effective in facilitating competition.

Third party access

The Tasmanian Government introduced the Tasmanian Electricity Code (TEC) from 1 July 1998 to provide for third party access to the Tasmanian transmission and distribution network.

Basslink

Tasmania has informed the Council that the Basslink (proposal to interconnect Tasmania with Victoria) is a fundamental part of the Tasmanian Government's energy strategy. The Basslink Development Board has been appointed to facilitate Basslink as a commercial opportunity in the NEM. The Board is acting as the notional proponent to progress key issues prior to the selection of a preferred proponent in February 2000. Two issues are the NEC rules for non-regulated interconnectors and the environmental and developmental approvals process. The Government's objective is to have Basslink commissioned in October 2002.

Through Basslink, the Government aims to:

- improve the security of electricity supply and reduce the exposure to drought conditions in Tasmania;
- provide Tasmania with access to electricity at prices determined competitively in the NEM;
- provide a means for electricity generated in Tasmania to be sold into the NEM;
- provide a new source of peak generating capacity in the NEM; and

- ensure that the cost of Basslink is minimised through a competitive selection process.

While Basslink will be built, owned and operated by the private sector, the Government has set a minimum link capacity of 200MW. The proponents are to determine other issues such as, the route and whether the link is to be developed as a regulated, non-regulated or hybrid interconnector under the NEC.

In the coming months, the Government will work with other jurisdictions and the NEM regulatory bodies to progress a number of structural and regulatory issues, including derogations and/or changes to the NEC associated with Tasmania's entry to the NEM.

National Electricity Law

The government has enacted the *Electricity – National Scheme (Tasmania) Act 1999* in preparation for becoming a NEM participant. This Act is the legislative vehicle for the adoption of National Electricity Law in Tasmania and is a precondition for Tasmania's entry to the NEM. The Government will proclaim the Act once the arrangements required for Tasmania's entry to the NEM are finalised.

Conduct Code Agreement: reporting obligations

In accordance with clause 2(1) of the CCA, the Tasmanian Government had notified the ACCC,[4] within 30 days of the legislation being enacted, of new legislation reliant on section 51(1) of the TPA. These electricity industry related Acts and their relevant sections are:

- *Electricity Supply Industry Act 1995* (section 44);
- *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* (section 7); and
- *Electricity Supply Industry Amendment Act 1998* (section 49F(2)).

The *Electricity Supply Industry Act 1995* is scheduled for review in 1999 under Tasmania's Legislation Review Program and the *Electricity Supply Industry Amendment Act 1998* will be reviewed in conjunction with the review of this Act. The *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* is currently being reviewed as part of the implementation of COAG's water reform agenda.

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42 The Commonwealth Treasurer was notified of the *Electricity Supply Industry Act 1995* and the *Electricity Supply Industry Restructuring (Savings and Transitional Provisions) Act 1995* as the ACCC had not yet been established.

Assessment

The Council considers that Tasmania's NCP commitments involve participating in the NEM if the Basslink eventuates, and conducting relevant CPA clause 4 reviews.

The Council is satisfied that Tasmania has met its second tranche electricity reform commitments for the following reasons:

- Tasmania has indicated a commitment to join the NEM by the end of the year 2002 if the Basslink proposal proceeds. In preparation for participation in the NEM, the Council considers that Tasmania has implemented the appropriate structural reforms required under the Electricity Agreements;

- as the TEC sets out a framework for third party access which has the potential to introduce competition into the Tasmanian electricity industry, Tasmania was required to undertake a clause 4 review of structural and competitive arrangements. The Council considers that the Government's decision to establish Aurora initially as a single distribution/retail business is consistent with the review recommendations. The review further recommended that following the introduction of competition, distribution and retail should be carried out by separate legal entities. As this separation has not yet been undertaken, the Council will assess the status of the distribution and retail businesses during the third tranche assessment; and

- the *Electricity Supply Industry Act 1995*, the *Electricity Supply Industry Restructuring (Saving and Transitional Provisions) Act 1995* and the *Electricity Supply Industry Amendment Act 1998* are to be reviewed as part of Tasmania's Legislation Review Program. The Council will consider the outcomes of these reviews in accordance with clause 5 the CPA, in the third tranche assessment.

The Council notes that the Tasmanian Government commenced a clause 4 review of the HEC's generation activities and system control function in March 1999. Tasmania advised the Council that the review team is required to report to the Government by 30 April 1999. The Council will assess this review in the third tranche assessment.

B7.2.3 Non-NEM participating jurisdictions

Western Australia

Structural reform

Western Australia is not a party to the Electricity Agreements, and consequently not a participant in the NEM, but is committed to applying competition policy in the electricity sector. Clause 4 of the CPA is relevant as Western Australia has introduced some competition by providing for third party access to Western Power's electricity transmission and distribution network.

In 1995, the State Energy Commission (SEC) was restructured into Western Power, Alinta Gas and the Office of Energy (OOE). The Western Australian Government also determined appropriate commercial objectives for Western Power in the context of its 1 January 1995 corporatisation.

Western Power's activities have been partially ring-fenced through the *Electricity Corporation Act 1994*, that requires Western Power to report annually on a segmented basis on the following:

- generation of electricity;
- transmission of electricity;
- interconnected distribution and sale of electricity in the state's south west;
- Pilbara interconnected system; and
- remote power systems.

Regulatory reform

The OOE is responsible for regulation of the electricity supply industry. These responsibilities include the licensing of electrical workers, authorising the supply of electricity, and regulating and monitoring the technical and safety aspects of the production, transmission, distribution and use of energy.

The *Electricity Corporation Act 1994* provides for third party access to Western Power's electricity transmission network.

Retail competition in electricity supply

Customers with a single site average load of at least 5 MW have been allowed to choose their own supplier from 1 July 1998. Since 1 January 1999 customers with an annual electricity consumption greater than 300 MWh have been contestable. The next stage involves Western Australia extending its contestable retail market to all customers with a single site average load of at least 1 MW from 1 January 2000.

Assessment

Western Australia's introduction of a third party access regime has the potential to introduce competition to the high voltage transmission system and distribution network, which gives rise to a NCP commitment under clause 4 of the CPA. Western Australia has advised the Council that the Minister for Energy has announced options for encouraging greater competition that will be considered. A clause 4 review of Western Power will be an integral part of these considerations.

The Council notes that Western Australia's progress in electricity reform is not as advanced as other jurisdictions, and intends to monitor future progress and the impact of competition on the Western Australian electricity supply industry, particularly during the third tranche assessment.

Northern Territory

Structural reform

The Northern Territory is not a participant in the NEM and has no obligations under the Electricity Agreements. However, clause 4 of the CPA is relevant to the Power and Water Authority (PAWA).

PAWA is a public monopoly established by the *Power and Water Authority Act* to provide electricity, water and sewerage services. In October 1998 the government undertook a review of PAWA. The review covered:

- future direction, structure, operations;
- regulatory and governance arrangements;
- separation of regulatory and commercial functions; and
- third party access arrangements.

The consultants recommended that the most effective competition model for PAWA was a regulated core business with a competitive periphery. (The competitive periphery involves the establishment of arrangements to provide competing electricity generators with access to customers and competitive tendering for inputs and significant system augmentation.)

The consultants also advised that there is merit in retaining the integration of PAWA's electricity, water and sewerage network and retailing businesses. This is due to the size of the Northern Territory market and existing economies of scale.

In its response on 1 December 1998, the Government decided to provide PAWA with an opportunity to achieve significant efficiency improvements under public ownership. The Government has indicated that it will revisit privatisation if the efficiency improvements are not achieved.

In response to the PAWA review, the following reforms are proceeding:

- over the next three years, electricity tariffs for commercial customers are to become progressively cost reflective;
- Territory-based arrangements are being developed to progressively open the electricity generation and retail markets to competition, commencing in the year 2000;
- competitive bids are to be sought when PAWA's electricity, water and sewerage systems require significant augmentation;
- regulatory functions are to be transferred from PAWA to relevant government agencies;
- an interdepartmental committee headed by Northern Territory Treasury has been established to consider the appropriate extent and form of economic regulation of electricity, water and sewerage services. In order to permit competition, the

regulatory arrangements will include an access regime to enable third parties to access electricity transmission and distribution networks; and

- PAWA's business has been reorganised along product lines comprising, among other things, power generation, transmission and distribution networks and retail services. This aims to separate the natural monopoly elements of transmission and distribution from the contestable elements of power generation and retail services.

The Northern Territory Government anticipates that the above reform program will take two to three years.

Assessment

The Northern Territory is not a NEM participant and therefore the only NCP commitments relevant to Northern Territory's electricity industry arise from clause 4 of the CPA. The Council considers that the review of PAWA, and the Government's response to this clause 4 review, is consistent with its NCP commitments.

The Council is satisfied that the Northern Territory Government has met its second tranche electricity reform commitments. However, the Council notes that the Northern Territory's progress in electricity reforms is not as advanced as other jurisdictions, and intends to monitor future progress and the impact of competition on the Northern Territory electricity supply industry, particularly during the third tranche assessment.

B8 Gas

B8.1 NCP commitments

Under the April 1995 *Agreement to Implement the National Competition Policy and Related Reforms*, the first tranche NCP obligation in gas was that (relevant) States and Territories implement any arrangements agreed between the parties as necessary to introduce free and fair trading in gas, between and within the States, by 1 July 1996 – or such other date as agreed between the parties, in keeping with the 1994 COAG gas reform agreement.

The central plank of the 1994 COAG gas reform program was a uniform national framework for third party access to natural gas transmission pipelines. In addition, COAG agreed to remove all legislative and regulatory barriers to trade in gas and to achieve structural reform of gas utilities.

The second tranche NCP obligation in gas is that (relevant) jurisdictions fully implement free and fair trading in gas, between and within the States, including the phasing out of transitional arrangements in accord with a schedule to be agreed between the jurisdictions.

In accord with the COAG principles on free and fair trade in gas, the Council's second tranche assessment considers jurisdictions' performance against the following obligations:

- effective implementation of the National Gas Pipelines Access Code, including satisfactory progress in phasing out transitional arrangements;
- removal of all legislative and regulatory barriers to free and fair trade in gas; and
- structural reform of gas utilities.

The National Gas Pipelines Access Code

The 1994 COAG agreement envisaged that a national code for access to gas transmission pipelines be in place by 30 June 1996. However, both COAG's original timetable and the scope of the reform agenda were modified after the NCP agreements were signed in April 1995.

In June 1996, COAG broadened the scope of reform and extended the timeframe, deciding that the national access framework should apply to distribution systems as well as transmission pipelines, and that the reforms be in place by 30 September 1996.

When this timeframe was not met, the Prime Minister in December 1996 proposed a new timeframe for introducing the national gas pipelines access code. The Prime Minister also sought agreement on certain regulatory and implementation issues. Apart from Western Australia, which expressed concern with the pace of deregulation and the proposed national transmission regulator, all jurisdictions agreed to the Prime Minister's proposals.

Subsequently, all Heads of Government signed *the Natural Gas Pipelines Access Agreement* (1997 Gas Agreement) on 7 November 1997. The Agreement incorporates a National Gas Pipelines Access Code (National Code), a legislative framework under which each jurisdiction would implement the Code, and a revised implementation deadline of 30 June 1998.

As at 30 June 1998, all States and Territories other than Western Australia and Tasmania had enacted legislation to give effect to the National Code.[43] However, at the time, the Commonwealth had not enacted the legislative amendments necessary for the State and Territory laws to become operational.[44] By 30 June 1999, the National Code was operational in all relevant jurisdictions other than Queensland.

The 1997 Gas Agreement established a number of implementation schedules, including a timetable under which each jurisdiction agreed to submit its application of the National Code to the Council for certification as an effective access regime under Part IIIA of the *Trade Practices Act 1974* (TPA). As at 30 June 1999, all relevant jurisdictions other than Victoria and the Northern Territory had applied for certification.

In addition, the Agreement established principles for the approval and phasing out of transitional arrangements and derogations from the National Code. In particular, transitional arrangements and derogations must be approved by all Ministers, be identified in the relevant jurisdiction's access legislation, and – except in certain specified instances – be phased out or removed by 1 September 2001. As at 30 June 1999, the Council is not aware of any jurisdictions imposing transitional arrangements and derogations outside the parameters of the Agreement.

Alongside the provisions on access, the 1997 Gas Agreement establishes complementary reform commitments on franchising principles and licensing principles. The Council regards these as ongoing commitments.

In accord with the 1995 NCP agreements, read in conjunction with the 1997 Gas Agreement, the Council assesses jurisdictions as having met their second tranche obligations in regard to the national gas access framework subject to:

- the National Code being operational in the jurisdiction;
- the continued phasing out of transitional arrangements in accord with the schedule in the 1997 Gas Agreement; and
- continued observance of the franchising principles and licensing principles in the 1997 Gas Agreement.

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[43] Western Australia passed its access legislation on 23 December 1998. Tasmania's commitments on this matter are not activated until such time as a natural gas industry commences in that State.

[44] The Commonwealth legislation received Royal Assent on 30 July 1998.

Removing regulatory barriers to free and fair trade in gas

Jurisdictions agreed under COAG 1994 to remove all legislative and regulatory barriers to free and fair trade in gas, between and within their boundaries, by 1 July 1996. The Council regards this an ongoing commitment.

The Council understands that many jurisdictions are addressing this area of reform in the context of their legislation review programs under clause 5 of the Competition Principles Agreement (CPA). As such, all relevant jurisdictions have scheduled gas-related legislation and regulation for review by the year 2000.

The Council has previously indicated that the June 1999 assessment will consider progress by jurisdictions in addressing any regulatory or legislative barriers to free and fair trade in gas, identified by the Upstream Issues Working Group (UIWG), which reported to COAG in December 1998.

Two areas highlighted by the UIWG are:

- the need for greater transparency in acreage bidding processes, including the publication of winning acreage bids; and
- the need for progress on access to upstream facilities.

The Council would expect that these principles be reflected in reviews under the clause 5 legislation review program of petroleum legislation, ratification Acts and other relevant legislation and regulation.

Given that a number of such reviews are currently in progress, the Council will continue to monitor reform in this area for the third tranche assessment.

Structural reform of gas utilities

COAG 1994 included a number of commitments on structural reform of gas utilities:

- structural separation of publicly owned transmission and distribution activities;
- the introduction of legislation to ‘ring fence’ transmission and distribution activities operated by the private sector by 1 July 1996; and
- corporatisation of gas utilities owned by the Commonwealth, State and Territory governments by 1 July 1996.

The Council regards these commitments as ongoing.

The Council notes that the National Code applies provisions on ring fencing to all gas transmission and distribution service providers. The provisions take effect in a particular jurisdiction once the National Code is operational in that State or Territory, in accord with Section 4 of the Code.

Conduct Code compliance: legislation relying on section 51 of the Trade Practices Act

As noted in Section B3, the Conduct Code Agreement requires that jurisdictions notify the Australian Competition and Consumer Commission (ACCC) of legislation reliant on section 51(1) of the TPA.

Because legislation reliant on section 51(1) is *prima facie* anti-competitive, jurisdictions are required to demonstrate that such legislation satisfies the competition test in clause 5(5) of the CPA.

As such, assessment issues in gas arise with regard to section 51(1) exemptions that might potentially affect free and fair trade in gas. In particular, the Council expects that the competition test in section 5(5) has been applied.

B8.2 Progress against NCP commitments

Commonwealth

National Code

The Gas Pipelines Access (Commonwealth) Bill was passed on 9 July 1998. The Commonwealth Act, which received Royal Assent on 30 July 1998, underpins the National Code by providing for the use of Commonwealth bodies, such as the ACCC and the Council, in the operation of the National Code. The Act also ensures that the Code applies to offshore waters and to the Moomba-Sydney pipeline.

The Commonwealth legislation provides for a derogation from the Code to allow for the continuation of any existing arbitration determinations which rely on Part 6 of the *Moomba-Sydney Pipeline Systems Sale Act 1994*, to allow for their continuing enforcement. This derogation was provided for in the 1997 Gas Agreement.

Removing regulatory barriers to free and fair trade in gas

The Council is not aware of Commonwealth legislative or regulatory barriers currently affecting free and fair trade in gas.

The Commonwealth has scheduled a number of Acts, affecting the supply of gas, for review under its clause 5 legislation review program. These include the *Moomba-Sydney Pipeline System Sale Act 1994* and the *Petroleum (Submerged Lands) Act 1967* (both scheduled for review in 1999-2000).

The Commonwealth amended the *Moomba-Sydney Pipeline System Sale Act 1994* and the *Petroleum (Submerged Lands) Act 1967* in 1998, under the *Gas Pipelines Access (Commonwealth) Act 1998,* to facilitate the application of the National Code in all jurisdictions and in Commonwealth waters.

Structural reform of gas utilities

The Council is not aware of any issues for the Commonwealth relating to structural reform of gas utilities.

Assessment

The Council assesses that the Commonwealth has satisfied its second tranche commitments in gas.

- The *Gas Pipelines Access (Commonwealth) Act 1998* is operational.
- The Commonwealth derogation affecting the Moomba-Sydney pipeline was specified in the National Code.
- The Council considers there are no matters relevant for the Commonwealth in respect of regulatory or legislative barriers to free and fair trade in gas.
- The Council considers there are no matters relevant are relevant to the Commonwealth in respect of structural reform issues.

New South Wales

National Code

New South Wales introduced an interim access regime in 1996, based on an early version of the National Code, to give customers access to the State's gas distribution networks.

The *Gas Pipelines Access (New South Wales) Act 1998* implements the National Code as adopted by all jurisdictions in November 1997. The legislation was passed on 3 June 1998 and was proclaimed on 14 August 1998.

The New South Wales Gas Pipelines Access Regime (incorporating the National Code) contains transitional arrangements, derogations and savings provisions consistent with the 1997 Gas Agreement. In February 1999, New South Wales notified the Council that it was delaying its customer contestability timetable under the National Code. However, the revised timetable remains ahead of the final deadline required under the 1997 Agreement.

New South Wales applied to the Council for certification of its access regime on 28 October 1998. The Council's recommendation has been conveyed to the Commonwealth Minister for Financial Services and Regulation.

Removing regulatory barriers to free and fair trade in gas

New South Wales has scheduled a number of Acts affecting the supply of gas for review under its clause 5 legislation review program. These include the *Gas Industry Restructuring Act 1986* and the *Pipelines Act 1967*.

New South Wales reports that a fundamental review of the *Pipelines Act 1967* was undertaken during 1998. The review examined transparency and effectiveness of approvals procedures; barriers to entry; whether government and non-government entities would be treated differently; and whether there is any urgent need to remove the third party access provisions of the Act.

Accordingly, the review examined restrictions on competition in the context of pipeline approvals, construction and operation. The review identified some provisions of the Act which, in theory, could restrict competition. These matters have been taken into account in the preparation of an Issues Paper on the Pipelines Act review, which is expected to be released for public consultation in the first half of 1999.

Structural reform of gas utilities

There are no publicly owned gas transmission utilities in New South Wales. The distribution network in the Wagga Wagga area is operated by Great Southern Energy, a New South Wales Government-owned electricity distribution business, which operates on a commercial footing.

Transmission and distribution services in New South Wales are operated by separate businesses: EAPL and Transmission Pipelines Australia (transmission); and AGL, the Albury Gas Company and Great Southern Energy (distribution). EAPL is 51 per cent owned by AGL. No company in New South Wales operates *both* transmission and distribution services.

The National Code establishes ring-fencing principles to apply to all gas transmission and distribution assets. AGL has implemented a corporate restructure to separate its network operations from retail functions, to comply with the provisions of the National Code.

More generally, New South Wales is providing for the staged removal of cross-subsidies provided by industrial to domestic gas markets. The State has also reviewed arrangements for dealing with Community Service Obligations to facilitate competitive neutrality between the gas and electricity sectors of the energy market.

Assessment

The Council assesses that New South Wales has satisfied its second tranche commitments in gas for the following reasons.

- The National Code is operational in New South Wales.

- New South Wales' transitional arrangements and derogations under the National Code are within the parameters of the 1997 Gas Agreement.

- The Council considers there are no matters relevant for New South Wales in respect of regulatory or legislative barriers to free and fair trade in gas.

- New South Wales is satisfactorily progressing the structural reform commitments in the COAG 1994 Agreement on gas.

Victoria

National Code

Victoria introduced the Victorian Access Code in December 1997. The Code mirrors the National Code, and was introduced as an interim measure to allow for the introduction of a package of gas reforms in the State.

The *Gas Pipelines Access (Victoria) Act 1998*, which applies the National Code in Victoria under the 1997 Gas Agreement framework, was passed on 19 May 1998 and proclaimed on 29 June 1999.[45] Victoria has informed the Council that proclamation was delayed due to interface issues between the Victorian Code – and processes already commenced under it – and the National Code. Victoria had also sought an amendment to the savings provisions in the Act, requiring the approval of COAG Ministers.

Removing regulatory barriers to free and fair trade in gas

Historical legislative and regulatory barriers to free trade in gas were removed as part of the November 1996 settlement of the dispute between the Commonwealth Government, Victorian Government and the Bass Strait producers (Esso-BHPP) regarding liability for the Petroleum Resource Rent Tax on Bass Strait gas production.

The settlement removed the State's exclusive contractual franchise and allowed other gas suppliers to enter the market on a competitive basis. In particular, restrictions were removed that had prevented:

- Esso or BHPP from selling gas, directly or indirectly, to end consumers;
- GASCOR buying gas from suppliers other than Esso or BHPP; and
- GASCOR's customers from on-selling gas.

Victoria has scheduled a number of Acts, affecting the supply of gas, for review under its clause 5 legislation review program. These include the *Petroleum Act 1958* (to which the Government responded in March 1999) and the *Pipelines Act 1967* (review completed February 1997). Victoria has listed the *Gas Industry Act 1998* and *Gas Safety Act 1997* as new legislation that restricts competition. The State's Annual Report to the Council includes an explanation as to why the benefits of the restrictions are considered to outweigh the costs.

Significant Producer Legislation

Concerns have been raised with the Council regarding Victoria's Significant Producer Legislation (SPL), set out in the *Gas Industry (Amendment) Act 1998.*

Esso and BHPP argue that the legislation imposes restrictions on significant producers in both the wholesale and retail markets, with adverse consequences for competition.

The SPL has two elements:

- introduction of a *Competition Rule* which prohibits significant producers from engaging in conduct that discriminates amongst gas retailers in a manner that has

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[45] With the exception of provisions conferring jurisdiction on the Federal Court. Victoria received legal advice following a recent High Court decision on cross-vesting that these provisions may not be workable.

the purpose, effect or likely effect of substantially lessening competition in a Victorian gas market; and

- prohibition on significant producers from retailing gas to any customer using less than 5 Petajoules (PJ) per year (essentially the 35 largest customers in Victoria).

The Council considered that elements of the legislation could be anti-competitive and sought information from the Victorian Government on the costs and benefits of the restrictions to the community, as well as evidence that the objectives of the legislation could not have been achieved in a less restrictive manner.

The Victorian Government responded that the provisions of the SPL were to address specific competition concerns that may arise during the transition to a fully competitive Victorian gas market. These concerns arose from the dominance of the upstream natural gas market in Victoria by Esso/BHP.

The Government was concerned that producers could act to restrict the development of competition in two possible ways:

- a significant producer could offer special terms for gas supply to retailers who did not seek alternative supplies; and

- a significant producer could specifically target (by means of special deals) customers of retailers who seek those alternative supplies.

The Government feared that the effect of either would be that retailers might not pursue alternative supplies and that this would limit the development of a more diversified producer structure in the Victorian gas market.

Esso and BHPP argue that the legislation is unnecessary in that any anti-competitive behaviour could be dealt with under Part IV of the TPA. They further argue that the Competition Rule in SPL could have the effect of reducing competition by requiring them to offer standard term contracts to all purchasers and preventing legitimate discrimination. SPL also prevents them from getting a retail licence to sell gas to customers taking less than 5PJ per year.

The Victorian Government denies that the SPL would require only standard term contracts being offered, and argues that Part IV of the TPA is insufficient to deal with the issues of regulating competition in a developing competitive market, claiming that SPL is analogous to Part XI of the TPA.

The SPL is to be reviewed before June 2003 to assess the costs and benefits of the legislation and determine whether it should be repealed.

The Council recognises the concerns of the Victorian Government in seeking to ensure that increased downstream competition is not frustrated by the behaviour of dominant upstream players. The Council accepts that the Government has carefully analysed the issues and developed the approach it believes is most appropriate.

The Council raised with the Victorian Government the concern that the SPL could have the unintended consequence of limiting legitimate contract variation between significant producers and retailers. Both Esso and BHPP claimed that this was the

position and provided legal advice to support their arguments. It is difficult to assess the practical impact of the legislation before it has a chance to operate and the Council was concerned that the review in 2003 may be too late to deal with negative competitive impacts.

The Victorian Government has given an undertaking to the Council that if there is evidence that the provisions of SPL are adversely affecting the development of the market and competition, the review will be brought forward.

The Council is satisfied that this is an appropriate way to deal with the issues and will be monitoring the operation of the legislation. The Council will further consider this issue in its assessment in June 2001.

Structural reform of gas utilities

Under the *Gas Industry Act 1994*, Victoria has structurally divided its state-owned gas transmission, gas distribution and gas retailing activities into separate corporations.

The new gas distribution and retail structure comprises three holding companies each owning one retailer and one distributor. Each of the 'stapled' businesses is subject to legal and operational separation in accord with the National Code and Victoria's interim Access Code. The Victorian Government has privatised all three gas retailer/distributors.

The former transmission corporation, GTC, has been separated into Transmission Pipelines Australia Pty Ltd (which maintains high pressure transmission pipelines in Victoria) and an independent system operator, Victorian Energy Networks Corporation (VENCorp), to manage capacity on the transmission network and the proposed spot market in gas. Victoria privatised Transmission Pipelines Australia Pty Ltd in 1999.

Conduct Code compliance: legislation relying on section 51 of the Trade Practices Act

The Council has been advised by the ACCC of the following new legislation reliant on section 51(1) of the *Trade Practices Act 1974:*

- *Gas Industry Act 1994* (notified 17 July 1998);
  - Part 6B, Competition Policy Authorisation;
    - = section 62M as from 3 June 1997, amended by 91/97;
    - = section 26 as from 8 June 1998;
    - = section 27 as from 11 December 1997 and amended by 40/98;
    - = section 62O as from 3 June 1997;
    - = section 62P as from 3 June 1997;
  - Part 6C, Master Agreements;

= section 62Q, section 62S and section 62T as from 8 June 1998.

Victoria informs the Council that Parts 6B and 6C of the Gas Industry Act implement a section 51(1) exemption under the TPA for revised arrangements between Esso/BHPP and GASCOR (and, by extension, the companies disaggregated from GASCOR) following resolution of the Petroleum Resource Rent Tax dispute in November 1996. Victoria notes that the use of section 51(1) was agreed by the Commonwealth and Victorian Governments as a means to provide commercial certainty as part of the resolution of the dispute.

In addition, a statutory exemption under section 51(1)(b) of the TPA was provided on 2 February 1999 for section 62PA of the Gas Industry Act, granting statutory authorisation to the Victorian Gas Industry Market and System Operation Rules (MSO Rules). The authorisation is co-incident within Victoria with the authorisation of the MSO Rules granted by the ACCC on 19 August 1998.

Assessment

The Council assesses that Victoria has satisfied its second tranche commitments in gas.

- The National Code is operational in Victoria.
- Victoria's transitional arrangements and derogations under the National Code are consistent with the 1997 Gas Agreement.
- Victoria is progressing reforms of regulatory and legislative barriers to free and fair trade in gas.
- Victoria satisfies the structural reform commitments in the COAG 1994 Agreement on gas.

Queensland

National Code

Queensland introduced the Gas Pipelines Access (Qld) Bill into Parliament on 21 April 1998. It was passed on 13 May and assented to on 18 May. The legislation had not been proclaimed as at 30 June 1999, and was therefore not operational.

Queensland informs the Council that it has chosen to delay making the National Code operational in the State until the Council has determined whether the Queensland Gas Pipelines Access Regime (incorporating the National Code) should be certified as an effective access regime under Part IIIA of the TPA.

Queensland's access legislation incorporates a number of derogations from the National Code affecting major transmission pipelines in the State. Queensland has indicated to the Council that it regards the derogations as an integral part of the State's access regime.

The Council notes that Queensland's derogations significantly alter the application of the National Code to the affected pipelines. While the derogations were signed off by

all jurisdictions in the 1997 Gas Agreement, the Council is currently in the process of determining possible implications for certification.

The Council accepts that, given the extensive nature of the derogations and the pending issue of certification, it may be a practical for Queensland to await the conclusion of the Council's certification process before making the National Code operational.

The Council would expect that this matter be resolved once the certification process has been completed.

Removing regulatory barriers to free and fair trade in gas

Queensland has reported to the Council that, in accord with issues raised by the UIWG, the Government is currently undertaking a targeted public review of the *Petroleum Act 1923*, the *Gas Act 1965* and *Gas Regulations 1989*.

Queensland has informed the Council that it intends to update the legislation to ensure that it is consistent with the UIWG recommendations in regard to the following key upstream gas issues:

- greater transparency in processes for allocating exploration permits and the award of acreage on an open and competitive basis; and
- provisions to enable the incorporation of a national approach to third party access to upstream gas production facilities, should UIWG's current work in this area recommend such an approach.

Queensland has also indicated that the review of these Acts will allow for amendments in accord with the licensing and franchising principles in the 1997 Gas Agreement. More generally, Queensland has reported that the COAG principles on open-ended franchises have been observed in the State. Approvals to develop new distribution franchises have been granted on the understanding that they will be subject to full open access provisions upon the introduction of the National Code.

Queensland has listed the *Gas Pipelines Access (Queensland) Act 1998* as new legislation enacted in 1998 that restricts competition. The restriction reflects the fact that gas pipelines owners and users must comply with the State's access regime.

Structural reform of gas utilities

Queensland's transmission and distribution activities are not structurally integrated. Currently in Queensland there are three main transmission pipeline operators – Epic Energy, AGL and Duke Energy. There are two main natural gas distributors – Envestra, formerly part of Boral Energy, and Allgas, now owned by Energex.

The National Code establishes ring fencing principles to apply to all gas transmission and distribution assets. Queensland reports that major gas industry participants are aware of these provisions, which will be activated once the National Code is operational in the State.

Energex, a Government-owned electricity corporation, made a successful takeover bid for Allgas in 1998. Energex is a corporatised business subject to competitive neutrality principles. Queensland reports to the Council that Energex is free to pursue its day-to-day business but is required to report to Shareholding Ministers on its Statement of Corporate Intent.

Assessment

The Council assesses that Queensland has satisfied its second tranche commitments in gas for the following reasons.

- The Council accepts that the delay in making the National Code operational in Queensland reflects practical concerns arising from the current certification process. The Council expects that this matter will be resolved once the certification process has been completed.

- Queensland's transitional arrangements and derogations under the National Code are consistent with the 1997 Gas Agreement.

- Queensland is progressing reform of regulatory and legislative barriers to free and fair trade in gas.

- Queensland satisfies the structural reform commitments in the COAG 1994 Agreement on gas.

The Council will consider whether Queensland has satisfied its obligations with respect to the National Code in the context of a supplementary assessment to be made on 30 June 2000.

Western Australia

National Code

The *Gas Pipelines Access (Western Australia) Bill 1998* was introduced to Parliament on 18 June 1998 and was passed on 23 December 1998. The Act was proclaimed on 27 January 1999 and took effect from 9 February 1999.

The Act is complementary legislation applying the Gas Pipelines Access Law – including the National Code – and establishing State bodies for regulation and arbitration of disputes. Currently a number of pre-existing access regimes apply to major pipeline systems until 1 January 2000 by way of derogations set out in the Code.

Western Australia's timetable for phasing out derogations and transitional arrangements is consistent with the 1997 Gas Agreement.

Removing regulatory barriers to free and fair trade in gas

Western Australia is implementing a deregulation schedule to unwind the exclusive franchise enjoyed by AlintaGas for gas distribution services to small use customers. The timetable culminates in full access to householder level by 1 July 2002, in accord with a State derogation in the 1997 Gas Agreement

AlintaGas is restricted until 2005 from participating in the Pilbara gas market. Western Australia maintains that this restriction is a necessary part of restructuring the previous gas supply contract between the former State Energy Commission of Western Australia and the North West Shelf Joint Venture, to allow for the development of competition in the Pilbara region.

The Council's first tranche assessment noted that restrictions then in place on the licensing of an alternative pipeline from the Pilbara to the State's south-west constituted a regulatory barrier to free and fair trade in gas. To satisfy the Council's concerns, Western Australia agreed to conduct an open and transparent process to determine whether anyone wished to build a second pipeline.

Western Australia reported to the Council that it has advanced the expressions of interest process for the construction of a second pipeline. The Government nationally advertised an indicative registration of interest process in September 1998.

The Government informed the Council that eleven companies lodged a registration of interest, but none indicated a willingness to proceed immediately with construction. Three firms were subsequently invited to participate in an expression of interest process, all of which have confirmed their willingness to do so.

In the meantime, the Government is taking steps to widen the Dampier to Bunbury Natural Gas Pipeline (DBNGP) corridor under the *Dampier to Bunbury Pipeline Act 1997* to promote competition in gas transmission services from the Pilbara to the south-west. Action has commenced to implement this expansion, which would allow the construction of additional pipelines – including loopings – which would compete with the DBNGP.

Western Australia has scheduled a number of Acts affecting the supply of gas for review under its clause 5 legislation review program. These include the *Dampier to Bunbury Pipeline Regulations 1998,* the *Gas Corporations Act 1994*, the *Gas Transmission Regulations 1994,* the *North West Gas Development (Woodside) Agreement Act 1979,* the *North West Gas Development (Woodside) Agreement Amendment Act 1994* and the *Petroleum (Submerged Lands) Act 1982 and Regulations.*

The reviews of the *Gas Corporations Act 1994* and the *North West Gas Development (Woodside) Agreement Amendment Act 1994* have been completed, with key recommendations endorsed by Cabinet.

Western Australia has listed the following as new legislation that restricts competition: *Dampier to Bunbury Pipeline Regulations;* the *North West Gas Development (Woodside) Agreement Amendment Bill 1996* (see below); and the *Energy Coordination Amendment Bill 1997*. The State's Annual Report to the Council includes an explanation as to why the benefits of the restrictions are considered to outweigh the costs and non-restrictive alternatives considered.

Structural reform of gas utilities

The *Gas Corporation Act 1994* allows AlintaGas to operate in the generation, transmission, distribution and trading/retail segments of the gas market. A clause 5

review of the Act found the legislated vertical integration of AlintaGas to be anti-competitive.

A number of recent events are likely to mitigate the corporation's market power. Firstly, with the sale of the DBNGP, AlintaGas is no longer involved in the gas transmission market.

Second, the National Code's ring fencing provisions will be applied to the corporation's gas distribution business (requiring separation from its trading/retailing arms) from 1 July 2002 when full access to the network becomes available. This is a slower implementation of the National Code's ring fencing principles than in other jurisdictions, but was a derogation approved by governments under the 1997 Gas Agreement.

In December 1998, the Government announced its intention to privatise the distribution, trading and retail businesses of AlintaGas. The Government has committed to a structural review of the corporation under clause 4 of the CPA prior to privatisation.

For pipelines other than the AlintaGas distribution networks in the mid and south-west of the State, the National Code's ring fencing principles are activated once the National Code applies to the relevant pipelines – for the State's major pipelines, this occurs on 1 January 2000.

Conduct Code compliance: legislation relying on section 51 of the Trade Practices Act

The Council has been advised by the ACCC of the following new legislation reliant on section 51(1) of the *Trade Practices Act 1974:*

- *North West Gas Development (Woodside) Agreement Amendment Act 1996*.

Section 41A of the Act provides for a State authorisation, under section 51(1)(b) of the TPA, of a gas contract between the North West Shelf "Domga" Joint Venture Participants and BHP Direct Reduced Iron Pty Ltd. Aspects of the contract that were identified as possibly restricting competition were its length and volume, as well as the provision that incremental gas must be taken from the contract supplier rather than the open market.

Western Australia notified the ACCC of this new statutory exemption within 30 days of enactment of the legislation. Western Australia has informed the Council that a clause 5 review of the Act recommended retention of anti-competitive restrictions on the basis of net public benefit, and followed an assessment that there were no viable alternative means to achieve the objectives of the legislation.

Assessment

The Council assesses that Western Australia has satisfied its second tranche commitments in gas for the following reasons.

- The National Code is operational in Western Australia, although it is not applicable to key pipelines until 1 January 2000 under Code derogations.

- Western Australia's transitional arrangements and derogations under the National Code are consistent with the 1997 Gas Agreement.
- Western Australia is progressing reforms of regulatory and legislative barriers to free and fair trade in gas.
- Western Australia is progressing the structural reform commitments in the COAG 1994 Agreement on gas.

South Australia

National Code

The *Gas Pipelines Access (South Australia) Act 1997* was passed in December 1997 and came into effect upon the commencement of the complementary Commonwealth legislation on 30 July 1998.

As 'lead legislator' for the National Code, South Australia was the first jurisdiction to seek certification of its state-based application of the Code. The South Australian access regime was certified as an effective access regime by the Minister for Financial Services and Regulation on 8 December 1998.

South Australia's derogations and transitional arrangements are consistent with the 1997 Gas Agreement.

Removing regulatory barriers to free and fair trade in gas

South Australia's *Cooper Basin (Ratification) Act 1975* provides concessions to the Cooper Basin producers and exempts certain agreements from the operation of the Trade Practices Act. The ACCC has previously identified the Cooper Basin (Ratification) Act as a significant legislative barrier to free and fair trade in gas.

South Australia reviewed the Act during 1998, releasing its review report on 28 May. The review identified a number of restrictions on competition where the costs outweighed public benefits. It noted that some of the restrictions arise because of the lack of a third party access regime to the Cooper Basin facilities, and because separate marketing by the Cooper Basin producers is effectively precluded. The review recommended that these restrictions be removed.

South Australia is yet to make an official response to the review. South Australia's Annual Report to the Council quotes the following section of a speech by the Deputy Premier, the Hon Rob Kerin MP, given in October 1998:

> *(the) Government has determined that we will establish a transparent process enabling the consideration of any third party access application to use Cooper Basin infrastructure. The infrastructure would encompass facilities from field satellites to the point of sale of the gas and liquids. The favoured minimum option is for an industry based self regulatory Code.* (Kerin 1998)

The Minister's Speech also stated that:

> *My preferred option is for such a code to include publication of access arrangements including capacity and pricing principles, be based on commercial negotiation, and provide for binding arbitration in the event of a dispute. There may be a need to wrap the industry code inside a skin of State legislation to provide a right of access, to guarantee arbitration and appeals on matters of law, and to shield the Industry Code from any Trade Practices Act entanglements.*

In a speech given on 22 March 1999, the Minister noted that the review of the *Cooper Basin (Ratification) Act 1975* had also identified criteria for Petroleum Production Licences as a barrier to trade in gas. The Minister commented that:

> *The Act will be amended to provide that applications for Petroleum Production Licences will be subject to the criteria established under the Petroleum Act.* (Kerin 1999)

South Australia is yet to make an official response to the review. As such, it is not possible at this stage for the Council to be satisfied that the Government has met its commitments in regards to removal of regulatory barriers to free and fair trade in gas. The Council will make a supplementary assessment on this matter in December 1999.

South Australia lists a number of other Acts, affecting free and fair trade in gas, for clause 5 reviews. Reviews have been completed into the *Natural Gas (Interim Supply) Act 1985* (to be repealed), and the *Natural Gas Pipelines Access Act 1995* (partly redundant following implementation of the National Code). A review is currently underway into the *Petroleum Act 1940.*

Acts scheduled for review in 1999 include the *Gas Act 1997* and the *Petroleum (Submerged Lands) Act 1982.*

Structural reform of gas utilities

South Australia's gas transmission and distribution pipelines are privately owned.

South Australia's transmission pipelines are owned and operated by Epic Energy – with exception of the Riverland Pipeline System, which is owned by Envestra Ltd and operated by Epic Energy Pty Ltd. Envestra Ltd also owns and operates the State's gas distribution networks. Neither Epic Energy nor Envestra have been issued with a licence to retail natural gas.

Boral Energy is the principal gas retailer in the State, along with other entities that include Optima Energy. The retailers have not been issued with licences to operate gas pipelines.

The case of Envestra owning both a transmission pipeline and distribution systems in the south-east of the State raises possible concerns under clause 10 of the COAG 1994

Gas Agreement, which requires the ring fencing of transmission and distribution activities.

South Australia argues that the principal issue should be to ensure separation of the natural monopoly elements of the gas industry (gas pipelines) from potentially competitive parts, such as retailing. The State argues that the latter form of separation has been achieved in South Australia. South Australia argues, in its Annual Report to the Council, that the terminology 'distribution activities' in clause 10 pertains to the retailing of gas.

This issue is likely to be addressed under the National Code, which applies ring fencing requirements to specific pipeline assets.

Assessment

On three matters, the Council assesses that South Australia has satisfied its second tranche commitments in gas.

- The National Code became operational in South Australia upon the commencement of complementary Commonwealth legislation on 30 July 1998.
- South Australia's transitional arrangements and derogations under the National Code are consistent with the 1997 Agreement.
- South Australia is satisfactorily progressing the structural reform commitments in the COAG 1994 Agreement on gas.

The Council is unable to provide a positive assessment of South Australia's progress in removing regulatory barriers to free and fair trade until it is notified of South Australia's official response to the review of the *Cooper Basin (Ratification) Act 1975*. The Council will consider this matter in the context of a supplementary assessment to be made on 31 December 1999.

Tasmania

National Code

While there is currently no natural gas industry in Tasmania, the State actively participated with other jurisdictions in the development of the National Code, and was a signatory to the 1997 Gas Agreement.

Under the Agreement, Tasmania's obligations to implement the National Code are not activated until approval for a natural gas pipeline in the State has been granted, or before a competitive tendering process for a natural gas pipeline in the State commences.

The Government intends to introduce Tasmania's access legislation during the 1999 Autumn Session of Parliament, paving the way for a possible introduction of natural gas to Tasmania by the year 2002.

Removing regulatory barriers to free and fair trade in gas

The Council considers there are no matters relevant for Tasmania in regard to regulatory barriers to free and fair trade in gas.

Structural reform of gas utilities

The Council considers there are no matters relevant for Tasmania relating to structural reform of gas utilities.

Assessment

The Council assesses that Tasmania has satisfied its second tranche commitments in gas.

Australian Capital Territory

National Code

The *Gas Pipelines Access Act 1998* was passed by the ACT Legislative Assembly on 30 June 1998. It was proclaimed on 14 August 1998, giving the National Code legal effect in the ACT.

The Council received an application to certify the regime on 11 January 1999.

The ACT's transitional arrangements are consistent with the 1997 Gas Agreement. The ACT has proposed no other derogations from the National Code.

Removing regulatory barriers to free and fair trade in gas

The *Gas Act 1992* was repealed in 1998 and replaced with the *Gas Supply Act 1998* in order to remove barriers to free and fair trade in natural gas. The *Gas Supply Act 1998* introduces a new gas authorisation framework that effectively separates distribution and retail activities to ensure that the National Code's ring fencing requirements are met.

The ACT Government has not identified any other legislative or regulatory barriers to free and fair trade in gas.

Structural reform of gas utilities

There are no publicly owned transmission or distribution activities in the ACT. Gas is transmitted to the ACT via the EAPL pipeline, while gas distribution services are separately owned by AGL Networks.

The ACT Government reports that AGL is currently restructuring its corporate entities in the ACT to separate distribution and retail activities, and put in place operating procedures and reporting mechanisms to meet the ring fencing requirements of the National Code.

Assessment

The Council assesses that the ACT has satisfied its second tranche commitments in gas for the following reasons.

- The National Code is operational in the ACT.
- The ACT's transitional arrangements are consistent with the 1997 Gas Agreement.
- The ACT has progressed reforms of identified regulatory and legislative barriers to free and fair trade in gas.
- The ACT is satisfactorily progressing the structural reform commitments in the COAG 1994 Agreement on gas.

Northern Territory

National Code

The Gas Pipelines (Northern Territory) Act was passed in April 1998 and commenced on 2 September 1998. Consequential amendments were required to the Energy Pipelines Act and the Petroleum (Submerged Lands) Act to make the National Code operational. These amendments commenced on 13 January 1999.

The Northern Territory Regime incorporates no transitional arrangements or derogations from the National Code.

The Territory informed the Council that its certification application will soon be submitted. Negotiations are proceeding with the terms of agreement for the ACCC to act as the Northern Territory regulator for gas distribution services. It is expected that this appointment will commence on 1 July 1999.

Removing regulatory barriers to free and fair trade in gas

The Territory has reviewed, or is in the process of reviewing a number of pieces of legislation affecting trade in gas. Reviews into the Energy Pipelines Act, the Petroleum (Submerged Lands) Act and the Petroleum Act are in progress. The Petroleum (Prospecting and Mining) Act has been repealed.

The Territory has previously informed the Council that its legislation pertaining to gas exploitation, development and transportation contains no legislative or regulatory impediments to the sale of gas.

Structural reform of gas utilities

With the exception of a small minority interest in NT Gas Pty Ltd held by the public sector, the Territory's gas pipelines are owned and operated by the private sector.

As outlined below, transmission and distribution activities in the Territory reflect significant structural integration.

- The 1557 km Palm Valley to Darwin transmission pipeline is leased and operated by NT Gas Pty Ltd (AGL owns 96 per cent of the corporation) under a 20 year

agreement. NT Gas Pty Ltd also operates gas distribution and gas retailing services in the Darwin area.

- The Palm Valley to Alice Springs pipeline is owned by Envestra Ltd, with Boral Energy Asset Management as operator of the pipeline. Gas distribution in Alice Springs is also owned by Envestra and operated by Boral Energy Asset Management. Gas retailing is conducted by Boral Energy.

The Northern Territory Government has informed the Council that ring fencing issues arising from structural integration will be addressed under section 4 of the National Code, now operational in the jurisdiction.

The National Code requires that a service provider, in respect of a pipeline covered by the Code, not carry on a related business (such as retailing). The Code also requires separate accounts in respect of the services provided by each covered pipeline and applies cost allocation principles.

Assessment

The Council assesses that the Northern Territory has satisfied its second tranche commitments in gas for the following reasons.

- The National Code is currently operational in the Territory.
- The Territory's application of the National Code contains no transitional arrangements or derogations.
- The Territory is reviewing gas-related legislation under its clause 5 legislation review program.
- Structural reform issues arising under the COAG 1994 Agreement on gas will be addressed under section 4 of the National Code.

B9 Road Transport

B9.1 Development of the road transport reform program

The national road transport reforms originated with the Heavy Vehicles Agreement and Light Vehicles Agreement signed by Heads of Governments in 1991 and 1992 respectively. These national programs were subsequently incorporated into the NCP through the *Agreement to Implement the National Competition Policy and Related Reforms*. However, this Agreement did not detail the specific reform obligations associated with each of the three tranches of NCP payments.

The Heavy Vehicles Agreement provided for the development of uniform or consistent national regulatory arrangements for vehicles over 4.5 tonnes gross vehicle mass. It also established the National Road Transport Commission (NRTC) to develop the road reform programs and the Ministerial Council for Road Transport (MCRT) to oversee implementation of the reforms and the NRTC. The Light Vehicles Agreement extended the national regulatory approach to cover light vehicles.

The categories of the NRTC's national road transport reform package are conveniently described as six modules, covering:

- registration charges for heavy vehicles;
- transport of dangerous goods;
- vehicle operations;
- heavy vehicle registration;
- driver licensing; and
- compliance and enforcement.

The original notion of implementing national reforms via the adoption of national template legislation was overtaken as individual States and Territories and the Commonwealth employed combinations of legal instruments to make their own road transport (and other) laws achieve the uniform or consistent transport operating conditions for road users intended by the national model. As a result, the pace of implementation varies across jurisdictions, owing to the particular legal processes and constraints in each jurisdiction.

Various elements of the NRTC modules and related reforms were collectively agreed by the jurisdictions as priorities for accelerated implementation nationally. The first Ten Point Plan in October 1994 was followed by a second Ten Point Plan endorsed by the MCRT in February 1997. These two Plans, together with the 11 other remaining elements of the six modules, set out some 31 initiatives identifiable as national road transport reforms. Some of these, in particular Increased Mass Axle Limits and Heavy Vehicle Registration Charges, are noted for their complexity, importance and major economic and financial significance.

Because of concerns about slippage in reform implementation, the Council wrote to Heads of Government to seek their agreement to a specific NCP program for delivery of road transport reforms. Governments charged the Standing Committee on Transport (SCOT) with developing an assessable framework of reforms for endorsement by the Council of Australian Governments (COAG).

The SCOT Working Group selected from the 31 national road transport reforms to develop a 19 Point Plan as the framework for the NCP second tranche assessment. The 19 Point Plan was supported by the Australian Transport Council (ATC) in December 1998, and endorsed by COAG in May 1999.[46] The 19 Point Plan comprises all road transport reforms approved by Ministers and available for implementation, with the exception of the Registration Charges reform which was assessed under the first tranche. Thus the implementation progress of these reforms is not necessarily (nor was it intended to be) indicative of the implementation progress of the whole package of national reforms.

Assessment of each jurisdiction's progress in implementing the 19 Point Plan as at 30 June 1999 provides a 'snapshot' relevant to determining their eligibility for receiving second tranche NCP payments. Although payments are not relevant for the Commonwealth, the Council's assessment includes the Commonwealth, as it is a party to the NCP Agreements. Implementation of reforms by the Commonwealth is integral to the national reform program and some of the 19 Points insofar as they are related to the Federal Interstate Registration Scheme.

The NRTC is continuing to develop the national reform package in conjunction with the jurisdictions. Further reform elements will be made available for implementation following their support by the ATC. In this interactive and evolving way, newly available reforms, and the remainder of the current 31 reforms where they are endorsed by COAG, will be added to the 19 Point second tranche framework, and the target dates and implementation criteria updated prior to the third tranche assessment.

B9.2 The Second Tranche Assessment Framework

Heads of Government established an Assessment Framework specifying the content of each of the 19 Points, including criteria for successful implementation and target dates, by which the Council is to make its assessment. Rather than a literal interpretation of whether every reform, criterion and date is achieved, the Assessment Framework provides for a broader contextual assessment reliant upon self-reporting of progress by each jurisdiction.

The 19 assessable reforms are set out in Box B9.1 below. The fact that reforms 6, 7 and 14 have recently been incorporated in an enhanced Combined Truck and Bus Driving Hours reform is not taken to mean that the earlier three reforms have been superseded for the purpose of this assessment. They are still considered relevant for the assessment even though there is now enhanced reform activity work to be done in the future. The new Combined Driving Hours Regulations is not assessable here.

[46] The endorsement by the Premier of Western Australia was conditional on some assessment interpretation issues.

Similarly, the new Combined Vehicle Standards reform does not supersede the accessibility of Reform 5.

Exemptions from the 19 point Assessment Framework

The Council is aware of endorsed exemptions from the 19 point Assessment Framework for Western Australia, ACT and the Northern Territory. Each jurisdiction has three exemptions, meaning that each has 16 assessable reforms.

Western Australia and the Northern Territory received formal (unconditional) exemption at the outset for Truck Driving Hours Reform 6. The two jurisdictions are also widely assumed to have an exemption for the Bus Driving Reforms (7 and 14). This is because the NRTC's proposed regulatory approach for buses, largely based on prescriptive hours, was met with low industry acceptance in Western Australia and was considered to have high implementation costs. As Western Australia has its preferred regulatory approach already in place, the exemption for Truck Driving Hours was assumed to extend to buses. The situation in the Northern Territory was similar.

The ACT has claimed that reforms 6, 7 and 11 have been deemed 'not applicable' to it and that this 'exempt' status is reflected in the Assessment Framework. The ACT had no previous regulation in these areas. It considered it not cost effective to introduce new law, among other things, because driver fatigue management necessarily relates to trips beyond the ACT's borders. Instead, the ACT has obtained de facto coverage by making administrative arrangements with New South Wales for coverage of interstate trips that encompass the ACT.

The Council accepts that the assessment basis for Western Australia and the Northern Territory should exclude the Bus Driving Reforms as well as the Truck Driving Reform excluded at the outset. Both jurisdictions have implemented comparable codes. Similarly, the Council accepts for second tranche assessment purposes the ACT's statement that it has achieved de facto delivery of reforms 6, 7 and 11.

Box B9.1 Second Tranche Road Transport Assessment Framework

Reform 1: A national package (Act/regulations/code) for the carriage of dangerous goods by road.

Reform 2: As far as practical, uniform or consistent national procedures and requirements for the registration of heavy vehicles.

Reform 3: Uniform national requirements for key driver licensing transactions including issue, renewal, suspension and cancellation (excluding learner and novice drivers).

Reform 4: Common Mass and Loading Regulations, which impose mass limits for vehicles and combinations, Oversize and Overmass Regulations and Restricted Access Vehicles Regulations, covering the operating requirements for larger vehicles.

Reform 5: Uniform in-service heavy vehicle standards.

Reform 6: Nationally consistent legislative and administrative arrangements for managing truck driver fatigue. Subsequent regulations combine truck and bus driving hours.

Reform 7: Nationally consistent regulation for managing fatigue among drivers of larger commercially operated buses. Subsequent regulations combine truck and bus driving hours (also reform 14).

Reform 8: National mass and dimension limits for heavy vehicles.

Reform 9: Common and simplified licence categories and improved processes to eliminate the holding of multiple licences by a single driver.

Reform 10: Expansion of "as-of-right" access for B-doubles and other approved large vehicles.

Reform 11: National in-service pre-registration standards (for heavy vehicles).

Reform 12: Common roadworthiness standards through adoption of roadworthiness standards and guidelines, together with mutual recognition and consistent enforcement.

Reform 13: Enhanced safe carriage and restraint of loads through standard regulations and a practical guide for the securing of loads to apply throughout Australia.

Reform 14: Adoption of national bus driving hours (subsequently included in the Combined Driving Hours Regulations with Reforms 6 and 7).

Reform 15: Simplified cost-free interstate conversions of driver licences.

Reform 16: Support by jurisdictions for development of alternative compliance systems.

Reform 17: Options for 3 and 6 month registration to provide operational flexibility.

Reform 18: Provision for employers to obtain limited information about an employee's driver licence status, with employee consent.

Reform 19: Agreement to link State/Territory databases to enable automatic exchange of vehicle and driver information through the National Exchange of Vehicle and Driver Information System (NEVDIS) – Stage 1.

B9.3 The Council's approach to assessing progress

The Council looks for 'effective observance' of the reforms in assessing NCP performance. The Council considers that 'effective observance' means virtually 100 per cent demonstrated achievement of each of the intended reform outcomes 'on

the ground' with legal enforceability, by the target date specified in the Assessment Framework.

The Council's assessment considers jurisdictions' progress in implementing the required components of each assessable reform as set out in the Assessment Framework, together with the predetermined criteria for successful implementation and the target dates. These criteria are defined in the matrices developed by the SCOT Working Group and endorsed by COAG. The assessment also involves the Council confirming the assessable reforms for each jurisdiction, as some of the jurisdictions have claimed exemptions, and checking the formal grounds for any exemptions.

The Council has assessed progress with implementation of the 19 Points at 30 June 1999 (the second tranche assessment date), there is a later target date set out in the Assessment Framework for some reforms. Target implementation dates later than 30 June 1999 apply in the case of Reforms 9, 13 and 15 (all July 1999) and Reforms 2 and 3 (December 1999). Usually, the target date is six months or so from the time of either ATC approval (that is, when the reform becomes available), or from the time of passing of legislation (thereby allowing time for regulations/rules, administrative systems, enforcement arrangements etc, to be developed and put in place).

The dates are targets rather than binding timetables on governments. However, many of the 19 reforms have been available for periods well in excess of a year (in some cases for several years) prior to 30 June 1999. For example, Reform 13 – Enhanced Safe Carriage and Restraint of Loads – became available for implementation in October 1994, as did many of the reforms in the first 10 Point Plan endorsed by Ministers at that time.

Having confirmed the basis and timing for the assessment, the Council looked to the extent of compliance. The Council relied heavily on information on progress to 30 June 1999 provided in State and Territory annual reports, information from the Commonwealth and evidence of 'on the ground' progress provided by other parties, including the road transport industry.

The Council's assessment was hampered to some extent by a majority decision taken by the ATC that the Council should not have direct access to the NRTC. As the body responsible for, among other things, developing the package of uniform or consistent national rules and regulations for road transport and evaluating implementation, the NRTC is well placed to provide information useful to the Council in clarifying the scope of the endorsed reform framework. The Council considers there are benefits in the ATC reconsidering the matter of access to the NRTC. A more collaborative approach, generally, will assist achievement of agreed NCP reforms, and in the case of road transport, will assist achievement of the benefits of greater national uniformity/consistency in regulation.

The Council considered timeliness, as measured against the target dates, to be very important given the delays of the past. However, the Council recognised that the Assessment Framework emphasises the target date for implementation needs to be considered in relation to the date that the reform first became available for implementation. Thus, the Council did not necessarily assess jurisdictions as having

failed to comply where a confirmed implementation program extends beyond the target date.

Furthermore, the Council sought to encourage implementation, rather than assess a jurisdiction as having failed on technicalities. In particular, where a jurisdiction indicated that a certain reform would not be (100 per cent) completed by 30 June 1999, but that progress is well advanced and completion is expected prior to end-December 1999, the Council did not necessarily see that jurisdiction as failing to meet its second tranche obligations.

Thus, the Council has evaluated each jurisdiction's performance according to the categories below.

- All assessable reforms in the 19 Point Plan were complete by 30 June 1999.
- Some assessable reforms were not complete by 30 June 1999, but implementation in line with the Assessment Framework is well advanced and is confidently expected to be complete by January 2000 at the latest. That is, the jurisdiction's program will be complete by the latest target end date in the Assessment Framework.
- At least one key element of the assessable reforms was absent at 30 June 1999 and there was no commitment to implement the particular reform (where the jurisdiction did not have an approved exemption from the reform).
- Some assessable reforms were not in place by 30 June 1999 and, while there is full commitment to the reform, implementation is not expected to be complete by January 2000.

B9.4 Progress against the Assessment Framework

All States and Territories have been assessed against the 19 reforms except where there are approved exemptions to the program. The approved exemptions – which relate to Western Australia, the Northern Territory and the ACT – were discussed in section B9.2.

The Commonwealth has 9 assessable reforms. It has no role in the other 10 of the 19 reforms as its obligation applies only in respect of heavy vehicles that operate exclusively across State boundaries.

At 30 June 1999, the reports from jurisdictions indicated that only New South Wales and Victoria had fully implemented all 19 reforms. All other jurisdictions have implemented the bulk of their assessable reforms, although not always in every legal detail as set out in the Assessment Framework or by the target implementation date. At 30 June 1999:

- Queensland had implemented 16 of the 19 reforms, with another three reforms to be completed by December 1999;

- South Australia had implemented 14 reforms in full,[47] with the remaining five expected to be substantially finalised by September 1999, although South Australia anticipates that full implementation of reforms 2 (heavy vehicle registration) and 3 (uniform driver licensing transactions) may not occur until 2000 because they require complex computer reprogramming;

- Tasmania had completed 16 of the 19 reforms, with another two reforms to be completed by December 1999, in line with the target implementation date;

- Western Australia had nine of 16 reforms in place, with the remaining seven expected to be implemented by January 2000;

- ACT had 12 of its 16 reforms in place, with the balance to be implemented by December 1999; and

- Northern Territory will have 15 of its 16 reforms in place by July 1999.

According to the Commonwealth, its program will only be completed by 'early to late 2000'. The Commonwealth explained the uncertainty in the implementation date of its reform program as reflecting the need for comprehensive inter-jurisdictional consultation around the current review of the *Interstate Road Transport Act 1985* being undertaken by the Attorney General's Department, and the timing uncertainties associated with introducing amending legislation.

The Commonwealth stated that introduction of reforms 2, 4 and 5 is awaiting finalisation of the review of the Interstate Road Transport Act. In addition to identifying amendments necessary for the implementation of these reforms, the review is to examine options to increase the future effectiveness of this Act and the Federal Interstate Registration System, primarily in response to complaints from States and Territories. The Commonwealth emphasised its commitment to achieving the reforms.

Apart from matters of timing, two jurisdictions reported that they are not intending to implement certain elements of the agreed reform program.

- Tasmania stated that it sees no need to mandate use of driver log books (Reform 6); and

- the Northern Territory said that it is yet to determine its approach to the core 'demerit points' element of national driver licensing reform (Reform 3).

Tasmania indicated to the Council that it has a longstanding policy of not adopting logbooks for recording truck driving hours, and that this has been communicated to the NRTC for some time. The vote recorded by Tasmania's Transport Minister in

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[47] For South Australia, the Council has assessed interim partial reforms (numbers 5, 6, 7 and 14) as complete for this assessment. South Australia stated that it is implementing these reforms, which are now superseded, through the new combined reforms. Legislation to adopt the combined reforms was introduced into the South Australian Parliament in March 1999 and reform implementation is expected by September 1999.

December 1995 on Truck Driving Hours Policy, contained a qualification that the national regulations contain an appropriate mechanism by which Tasmanian intra-state operations can be exempt from log book requirements. However, the Council could find no record that an exemption from the reform had been approved for Tasmania.

Following consultations with jurisdictions, the Council is satisfied that these are the key reforms not yet implemented for the purposes of the second tranche assessment. However, the Council does not rule out the possibility that a more exhaustive analysis might reveal minor aspects of the other reforms that have been set aside by jurisdictions.

Table B9.1 outlines jurisdictions' implementation progress at 30 June 1999, as derived from jurisdictions' annual reports and the Council's subsequent analysis. The table indicates the reforms 'complete' as at 30 June 1999 and those that are still to be completed. The table also sets out the expected implementation dates for reforms not fully in place at 30 June 1999, and the areas of the agreed Assessment Framework that jurisdictions are not proposing to implement.

The Council received comment from the Australian Trucking Association (ATA) that, while many road reform initiatives are implemented, there are several remaining impediments and gaps. A central theme of the ATA's comments is that the 19 reforms endorsed by governments represent a significant watering down of the road reform program as originally intended. The ATA is also concerned that some jurisdictions have not implemented important components of the road transport reform program, contrary to the advice provided by the jurisdictions to the Council. In particular, the ATA questions the extent of implementation of:

- the national program for the carriage of dangerous goods (reform 1) by Western Australia;
- registration of heavy vehicles (reform 2) and uniform national licensing (reform 3) by Victoria;
- uniform heavy vehicle standards (reform 5) by Western Australia, South Australia and Tasmania;
- national arrangements for managing truck driving hours (reform 6) by South Australia;
- national heavy vehicle mass and dimension limits (reform 8) by Western Australia and South Australia; and
- national pre-registration standards for heavy vehicles (reform 11) by Western Australia and South Australia.

Given the ATA's comments, the Council 'double-checked' reform progress with jurisdictions to ensure that information is accurate as at 30 June 1999 before concluding its assessment.

Table B9.1 Reported progress against NCP road transport reforms, by jurisdiction

Reform	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Clth
1 **Dangerous Goods**	Complete	Complete	Complete	Complete	Complete	Complete	Has implemented legislation but requires amendment to Commonwealth law. Being implemented in practice using temporary Emergency Orders	Implemented through Code: regulations due in July 1999	Complete
2 **Registration Scheme**	Complete	Complete	Effectively in place but rewrite of legislation due Sept 99	Incomplete but due Jan 2000	Incomplete. Expected Sept 99, but may not occur in full until 2000 due to computer programming demands	Incomplete but due Dec 99	Incomplete but due Dec 99	Complete	Incomplete but due Dec 2000
3 **Driver Licensing**	Complete	Complete	Incomplete. Variable licence suspensions due Dec 99	Incomplete but due Jan 2000	Incomplete. As above	Incomplete but due Dec 99	Incomplete but due Dec 99	Incomplete. Admin guidelines due July 99. Demerit points not implemented	Not applicable – no legal role

Reform	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Clth
4 **Vehicle Operations**	Complete	Complete	Complete	Incomplete but due Oct 99	Incomplete but due Sept 99	Due for June 99 completion	Mostly implemented. Due Dec 99	Complete	Incomplete but due Dec 2000
5 **Heavy** **Vehicle Standards**	Complete	Complete	Incomplete – emission standards due Sept 99.	Incomplete but due Oct 99	Complete	Complete	Complete	Complete	Incomplete but due Dec 2000
6 **Truck Driving Hours**	Complete	Complete	Complete	Not applicable – uses comparable code	Complete	Incomplete. Log books not mandated	'Not applicable' claim	Not applicable – uses comparable code	Not applicable – no legal role
7 **Bus Driving Hours**	Complete	Complete	Complete	Not applicable – uses comparable code	Complete	Complete	'Not applicable' claim	Not applicable – uses comparable code	Not applicable – no legal role
8 **Common Mass & Load Rules**	Complete	Complete	Complete	Complete	Incomplete but due Aug 99	Complete	Complete	Complete	Complete
9 **One Driver/ One Licence**	Complete	Complete	Complete	Incomplete. Due Jan 2000	Complete	Complete	Incomplete. National driver licence classes due Dec 99	Complete	Not applicable – no legal role

Reform	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Clth
10 **Improved Network Access**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete
11 **Common Pre-Reg Standards**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Not applicable – no legal role
12 **Common** **Roadworth-iness Stds**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Not applicable – no legal role
13 **Safe Carriage & Restraint of Loads**	Complete	Complete	Complete	Incomplete but due Jan 2000	Incomplete but due Aug 99	Complete	Complete	Complete	Participation complete
14 **National Bus Driving Hours**	Complete	Complete	Complete	Not applicable – uses comparable code	Complete	Complete	'Not applicable' claim	Not applicable – uses comparable code	Not applicable – no legal role

Reform	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Clth
15 **Interstate Conversions Of Driver Licences**	Complete	Complete	Incomplete. Proposal to implement the no licence fee reform by Dec 99 under consideration	Incomplete but due Jan 2000	Complete	Complete	Complete	Complete	Not applicable – no legal role
16 **Alternative Compliance**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete
17 **Short Term Registration**	Complete	Complete	Complete	Complete	Complete	Due for June 99 completion	Complete	Complete	Complete
18 **Driver Offences/ Licence Status**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Effective, with privacy guidelines due July 99	Not applicable – no legal role
19 **NEVDIS Stg 1**	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Complete	Not applicable – no legal role

B9.5 The Council's recommendations on compliance with road transport obligations

This section outlines the Council's recommendations on jurisdictions' implementation of their road transport reform obligations against the four assessment categories set out in section B9.3. Because the ATC did not agree to the Council having access to the NRTC, the Council's analysis necessarily relies heavily on the information provided in government's annual reports. The Council has also taken into account the views of the ATA on observed progress with 'on the ground' implementation of reforms discussed earlier in this chapter.

Progress with compliance

The evidence available to the Council indicates that most of the second tranche road reform program endorsed by COAG is in place at 30 June 1999. Across all jurisdictions, taking into account the formalised and practical exemptions from the reform program, at least 125 of the 152 reforms – over 80 per cent – comply with the Assessment Framework in that the required elements have been satisfactorily implemented on time or ahead of time.

Nonetheless, while progress against most reforms is generally satisfactory, the Council's analysis – based on jurisdictions' reporting – indicates that only New South Wales and Victoria have so far completed their entire programs. The other States and Territories are scheduled to complete their second tranche programs at various times over the period to January 2000, and the completion date for the Commonwealth could be as late as the end of 2000. Moreover, two States and Territories have so far only committed to partial performance in that they are not proposing to implement all aspects of the agreed reform package and do not have a formal exemption for the elements not implemented.

Thus, while the bulk of the second tranche program is now in place, full implementation may not occur until late in the year 2000, although this is primarily the consequence of the need for the Commonwealth to undertake extensive inter-jurisdictional consultations. Table B9.2 provides a summary analysis of the delayed or incomplete reforms, by jurisdiction. The section of the table headed 'Comment' provides a summary of the current status of those reforms at 30 June 1999.

While there has been useful progress, the Council is concerned at the potential for further delay. Delay would mean costs to industry, road users and administrators, for example, arising from inconsistencies in parameters such as limits, penalties, administration and operating costs, safety and emission controls. In addition, the lack of uniformity in fees could distort fee collection by jurisdictions. Comments by the ATA emphasise the risk that a lack of uniform or consistent regulation, should agreed reforms be delayed in some jurisdictions, will adversely affect the competitiveness of Australia's road transport operations. The Council gives considerable weight to national uniformity/consistency of road transport regulation in assessing jurisdictions' reform performance.

Table B9.2 Analysis of incomplete or delayed reforms, by jurisdiction, at 30 June 1999

	Reform	Likely date	Comment
Qld	3 Driver Licensing	Dec 99	Has scheme similar to national licensing except for variable licence suspensions, delayed with computer system development
	5 H V Standards	Sept 99	Implemented except for emission standards which became available in Mar 99
	15 I/S Conversion Licences	Dec 99	Not implemented ‘no licence fee’ driving licence conversion but has undertaken to consider a proposal incorporating the reform for possible implementation by Dec 99
WA	2 Registration Scheme	Jan 2000	Act amendments due in second half of 1999 but competing legislative priorities
	3 Driver Licensing	Jan 2000	Act amendments due in second half of 1999 but competing legislative priorities
	4 Vehicle Operations	Oct 99	Mostly in effect; drafting of instructions for amended regulations is underway
	5 H V Standards	Oct 99	Mostly in effect; drafting of instructions for amended regulations is underway
	9 One Driver/One Licence	Jan 2000	Linked to Reform 3
	13 Safe Carriage	Jan 2000	Regulations disallowed by Parliamentary Committee; Act amendments needed. Linked to Reform 2
	15 I/S Conversion Licences	Jan 2000	Linked to Reform 3
SA	2 Registration Scheme	Sept 99	Bill is on its way to being passed. Regulations have been drafted ready for use. Computer programming demands may defer actual implementation until 2000
	3 Driver Licensing	Sept 99	Same Bill as Reform 2. Computer programming demands may defer actual implementation until 2000
	4 Vehicle Operations	Sept 99	Mostly in effect; the maximum limit of the reform has been referred to NRTC for review

	Reform	Likely date	Comment
	8 Common Mass & Load Rules	Aug 99	Mostly in effect for permit vehicles but not yet applicable to general access vehicles. Legislation in Parliament
	13 Safe Carriage	Aug 99	Parliament expected to give effect to Regulations shortly
Tas	2 Registration Scheme	Dec 99	Bill is under consideration; funds allocated for system redevelopment
	3 Driver Licensing	Dec 99	Similar to Reform 2
	6 Truck Driving Hours	No date	Truck driving hours are regulated. Drivers' log books have not been not mandated as the alternative controls are considered more cost effective
ACT	1 Dangerous Goods	Dependent on the C'wealth	ACT legislation in place but requires amendment to Commonwealth legislation to be operational. The ACT applies the reform in practice, pending amendment to the Commonwealth legislation, using 6 monthly Ministerial Emergency Orders
	2 Registration Scheme	Dec 99	Some regulations have been implemented and there is an ongoing commitment and progress towards 100 per cent completion
	3 Driver Licensing	Dec 99	Draft legislation is in progress utilising the New South Wales approach
	4 Vehicle Operations	Dec 99	Progressively applying New South Wales practices where applicable
	9 One Driver/One Licence	Dec 99	Will adopt final element of reform, 'national driver licence classes', as part of Reform 3

	Reform	Likely date	Comment
NT	3 Driver Licensing	No date	Implemented except for administration guidelines on the use and release of information due July 1999 and the 'demerit points' element which the Northern Territory Government is still considering
Clth	2 Registration Scheme	Dec 99	Changes are planned in the context of a review of the IRT Act (FIRS) currently underway. Consultation will follow, then amendments to legislation
	14 National Bus Driving	Dec 99	As for Reform 2
	5 H V Standards	Dec 99	As for Reform 2

Note: HV – Heavy vehicles; I/S – Interstate; IRT Act – *Interstate Road Transport Act 1985*; FIRS - Federal Interstate Registration System

Assessment of performance by jurisdiction

In formulating its assessments and consequent recommendations on payments, the Council took account of a number of considerations, including:

- the degree of difficulty of a reform vis-à-vis a jurisdiction's existing legislation and processes for change;
- the significance of the reform being incomplete nationally;
- the interdependency of jurisdictions and agencies and the reasons for delay, particularly where delay is outside a jurisdiction's control;
- each jurisdiction's progress with the total road reform program beyond the 19 Points; and
- whether evidence of good faith generally across the program warrants discretion for jurisdictions experiencing delays with particular reforms where they have in place a firm timeframe for implementation (albeit beyond 30 June 1999).

For the Council, however, the overriding consideration is the importance to the nation as a whole of all jurisdictions achieving a common regulatory platform consistent with the ATC Assessment Framework. The cost of fully implementing the 19 reforms is likely to be minor relative to the potential gains to governments (including from competition payments), industry and ultimately consumers. In addition, all governments agreed the 19 point framework as the basis for the second tranche assessment. Accordingly, the Council takes the view that, to be assessed as fully complying, each jurisdiction needs to have made a wholehearted contribution to achieving the common platform.

The Council considers that any cessation/suspension of key elements of the agreed road reform program (particularly on cost of implementation grounds) would contravene the principle of national uniformity. Accordingly, except where there are formalised exemptions or accepted alternatives, the Council took the approach that every reform element and success criterion identified in the Assessment Framework must be implemented for the reform to be assessed as complete, and the relevant jurisdiction unconditionally eligible for full competition payments.

Conclusions and recommendations

The Council's assessment of road reform performance has found that only two governments - New South Wales and Victoria - had completed the road transport reform program specified in the ATC second tranche Assessment Framework (as relevant) at 30 June 1999. Most other jurisdictions have implemented the bulk of their programs and are progressing remaining reforms such that most should be in place by late 1999 or, at the latest January 2000.

Where reforms are not in place at 30 June 1999, but are likely within a reasonable (short) period consistent with the ATC target dates, the Council has not recommended payment reductions at this stage. However, the Council will undertake a supplementary assessment prior to 31 March 2000 to determine whether competition payments should continue to be made from that point.

Of greater concern to the Council, because of potentially adverse implications for regulatory uniformity, is that two jurisdictions – Tasmania and the Northern Territory - have not yet given a commitment to implement components of the Assessment Framework (or a satisfactory equivalent). However, in one of these two cases, the jurisdiction is yet to determine its approach and, in the other, the Council believes there was a reasonable expectation on the part of the jurisdiction that the reform not implemented was an exemption from the ATC program.

Accordingly, in each case, the Council recommends that competition payments relevant to the reforms not be reduced pending clarification of the status of the relevant reform. To enable this, the Council is proposing a supplementary assessment prior to 31 March 2000 for each of the two jurisdictions where there is so far no commitment to implement components of the package. In order to demonstrate compliance, and therefore continued receipt of competition payments, each jurisdiction would need to provide evidence either that COAG agrees that the reform is exempt or that, if it is not, the reform is applied.

Jurisdictions with complete implementation of all of the 19 reforms at 30 June 1999

The Council assesses New South Wales and Victoria as complying with second tranche road transport reform obligations.

Jurisdictions where implementation of the majority of reforms is complete at 30 June 1999 and there is a clearly stated program for implementation of all outstanding reforms within a reasonable period. Consistent with COAG endorsed road reform end dates, the Council considers that, for purposes of the second tranche assessment, a reasonable period should be defined as no later than early 2000

There are four jurisdictions in this category.

- Queensland had completed 16 of the 19 reforms by 30 June 1999. For one of the 16 reforms, nationally consistent registration of heavy vehicles, procedures are in operation now, with legislation expected before Parliament in September 1999. Queensland will complete its reform packages covering heavy vehicle standards (emission controls) in September 1999 and driver licensing (variable licence suspensions) by December 1999. Queensland has so far not implemented the no fee element for interstate licence conversions encompassed in reform 15. However, the Government stated that it is preparing a new proposal for licence fee restructuring, which incorporates the Interstate Conversions of Driver Licences reform for consideration by the Queensland Cabinet in September 1999. The Government thought it may be possible to implement this in December 1999.

- South Australia has five reforms still to finalise but is expected to have enacted required legislation and enacted regulations by September 1999. However, South Australia stated that computer programming requirements might delay full implementation of reforms 2 and 3 until 2000.

- Western Australia has seven reforms still to finalise but has committed to implementing in full its 16 relevant reforms by January 2000.

- The ACT will have completed 12 of its 16 relevant reforms by 30 June, and committed to completing its remaining the four reforms by December 1999.

Keeping in mind South Australia's qualification concerning computer programming, these four jurisdictions have expressed a commitment to full implementation of all relevant reforms prior to or by January 2000. Accordingly, the Council recommends that second tranche competition payments not be reduced as a result of the delays, but that payments beyond 31 March 2000 be subject to the relevant jurisdictions providing evidence that the reforms are implemented. The Council would expect South Australia to have satisfactorily advanced its computer programming requirements.

The Council proposes that it undertake a supplementary assessment of road transport reform implementation in these jurisdictions prior to 31 March 2000 to assess whether second tranche competition payments should continue. The Council may recommend to the Federal Treasurer that competition payments be reduced in the event that a jurisdiction has not completed its reform program. The Council's assessment will take into account relevant matters raised by the ATA.

Jurisdictions where implementation of the majority of reforms is complete at 30 June 1999 (including agreement to implement most of those outstanding at 30 June 1999 by early 2000) but where there is so far no commitment to implement one or more of the reforms specified in the ATC Assessment Framework

There are two jurisdictions in this category.

- Tasmania has completed 16 of its 19 reforms by 30 June 1999, with uniform procedures for registration of heavy vehicles and driver licensing expected to be in place by December 1999. However, Tasmania is currently not mandating the use of log books by truck drivers (Reform 6). As discussed previously, while Tasmania has communicated its position on mandating log books the NRTC over a long period, there is no formal exemption from the requirement to mandate log books on the record.

  In addition to mandated log books, Tasmania will not complete all other elements of its reform program until December 1999.

- The Northern Territory will have completed 15 of its 16 relevant reforms by July 1999. However, at 30 June 1999 the Northern Territory had yet to decide whether it would implement the demerit points element of the reform introducing nationally uniform driver licensing or seek an exemption (reform 3).

The Council proposes that it undertake a supplementary assessment of road transport reform implementation in both jurisdictions prior to 31 March 2000 to confirm that:

- the reforms where implementation is delayed beyond 30 June 1999 have occurred; and

- the reforms for which there is at present no commitment to implement are either confirmed as formal exemptions from the Assessment Framework or are implemented as specified in the Assessment Framework.

The Council may recommend to the Federal Treasurer that competition payments be reduced in the event that the jurisdictions fail to either confirm there is a formal exemption or implement the outstanding reforms, including any not in place at 30 June 1999. The Council's assessment will take into account relevant matters raised by the ATA.

The obligation to implement all relevant reforms is agreed but the timetable for implementation is unsatisfactory

The only jurisdiction in this category is the Commonwealth. The Commonwealth has expressed full commitment to the nine reforms relevant to it, but has stated only that implementation is to occur 'early to late 2000'. The Commonwealth explained that it is unable to provide a better indication of its expected completion date because of the requirement to consult widely with other jurisdictions in the context of reviewing and reforming the *Interstate Road Transport Act 1985*.

The Council has made no recommendation on competition payments as these are not relevant for the Commonwealth, but proposes to assess progress achieved by the Commonwealth towards its road reform objectives prior to 31 March 2000.

Appendix A Payments to States and Territories under the National Competition Policy 1999-2000

Under the Agreement to Implement the National Competition Policy and Related Reforms, the Commonwealth is to provide payments to States and Territories that make satisfactory progress with the implementation of National Competition Policy and the related reforms in electricity, gas , water and road transport.

There are two components to the payments. The per capita growth in the Financial Assistance Grants (FAGs) pool available to each State and Territory is an indexed amount, based on weighted population shares, as determined by the per capita relativities recommended by the Commonwealth Grants Commission. The other component is the Competition Payment. The payments are made in three tranches, commencing in 1997-98, 1999-2000 and 2001-02. The annual Competition Payment under each tranche will be, in total, $200 million, $400 million and $600 million (in 1994-95 prices) per year in the tranches, respectively. The Competition Payment is indexed annually to maintain its real value over time.

Total payments available to States and Territories in 1999-2000 for satisfactorily progressing competition reform obligations are estimated to be around $641 million, comprising a per capita growth in FAGs element of some $439 million and Competition Payments of almost $202 million. The estimated maximum amount which could be received by each State and Territory is shown below.

Table A1 Maximum payments to States and Territories under the National Competition Policy, 1999-2000 ($ million)

	Competition Payment	Per capita growth in FAGs pool	Total
New South Wales	148.4	61.2	209.7
Victoria	109.1	43.1	152.2
Queensland	81.4	37.6	119.1
Western Australia	43.3	18.8	62.1
South Austalia	34.5	19.1	53.6
Tasmania	10.8	8.0	18.8
ACT	7.2	3.6	10.8
Northern Territory	4.5	10.0	14.5
Total	439.1	201.5	640.6

Note columns and rows may not total due to rounding.
Source: Commonwealth Treasury

ACCOUNTING SEPARATION OF LOCAL FIXED NETWORK

January 2002

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EXECUTIVE SUMMARY

The National Competition Council's first tranche assessment of Commonwealth Progress with the implementation of National Competition Policy (NCP) considered that:

> *clause 4 of the Competition Principles Agreement placed a responsibility on the Commonwealth Government to have examined, prior to the partial privatisation in 1997, the appropriate treatment of the remaining monopoly element of Telstra's business, the local fixed network. Such an examination should have considered the merits of structurally separating the local fixed network from the non-monopoly elements of Telstra's business or, alternatively, arrangements for ring-fencing the local fixed network and Telstra's business units.*

As part of the Council's second tranche assessment of the governments' progress with NCP Reform at the end of June 1999, Tasman Asia Pacific was asked by the Council to review the status of the Australian Competition and Consumer Commission's (ACCC) proposed record-keeping rules and the Commonwealth Government's proposed arrangements for ring-fencing the local fixed network. In addition, the Consultant was asked to assess the likelihood that the new record-keeping rules will work effectively to facilitate competition in the telecommunications industry.

The proposed record-keeping rules regime is an improvement on the existing Chart of Accounts and Cost Allocation Manual. It addresses the shortcomings of the existing Chart of Accounts/Cost Allocation Manual while incorporating the following new features: wholesale and retail services are separated; internal and external businesses are separated; costs that are specifically associated with providing only retail services and external wholesale services are allocated directly to those services; and revenues, costs and capital employed are generally allocated to each service as directly as possible from the General Ledger.

The new record-keeping rules will provide the Australian Competition and Consumer Commission with the necessary financial information so as to assess anti-competitive behaviour by carriers and carriage service providers. The new record-keeping rules regime is a necessary first step in establishing a broader ring-fencing framework for the telecommunications industry. At present, the Commonwealth Government does not have a coordinated policy with regard to arrangements for ring-fencing the telecommunications industry. Although, the new record-keeping rules, together with the new provisions in the *Telstra (Transition to Full Private Ownership) Bill 1998* and the *Telecommunications Legislation Amendment Bill 1998*, are potentially positive steps towards a ring-fencing model for the industry, these proposed arrangements are still inadequate in addressing anti-competitive issues such as Telstra's dominance in the local fixed network.

A ring-fencing regime will not remove the sources of Telstra's market power and may not be an effective strategy to combat anti-competitive behaviour, which discourages real competition in the telecommunications industry. It has been almost 10 years since competition was introduced in the telecommunications industry in Australia (limited competition in early 1990s and full competition in 1997), and Telstra remains the dominant player, with significant market power, in the local telecommunications services market. Its major rival, Optus, has made little inroad into the local market.

The consultant considers that the ring-fencing regime may not be an effective approach to bring out real competition in the local telecommunications market. Ring-fencing will not remove the key sources of Telstra's market power, and therefore, will not remove the incentive to engage in anti-competitive behaviour. The Consultant considers that the benefits of structural separation outweigh the costs.

THE PROPOSED MODEL

One possible model could be the separation of the Customer Access Network (CAN), the natural monopoly element of the network, from the transmission facilities. The CAN may be operated by an independent telecommunications operator, under the supervisor of a regulator authority, such as the ACCC. The CAN operator provides access to fringe telecommunications operators, and these operators can then use their own transmission and switching facilities to transmit telecommunications services, such as a telephone call, from their network to the CAN operator's network. This model separates the natural monopoly element of the network and introduces real competition in the local loop market (Figure 1).

Figure 1: The Consultant's Proposed Structural Separation Model

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1. BACKGROUND

Telstra is a fully vertically integrated provider of telecommunications products and services, and prior to 1991, was a monopoly provider of all telephone services in Australia. While Telstra has been increasingly exposed to competition primarily from Optus, it retains monopoly control of its local fixed network.

The Commonwealth privatised one-third of Telstra in 1997. It is now intending to divest another tranche of Telstra that will take the level of private sector ownership to 49 percent. The Commonwealth has announced its support, in the longer-term, for divestment of the remaining 51 percent, subject to Telstra meeting prescribed service levels.

The National Competition Council (NCC) considered that clause 4 placed a responsibility on the Commonwealth to have examined, prior to the partial privatisation in 1997, the appropriate treatment of the remaining monopoly element of Telstra's business, the local fixed network. Such an examination should have considered the merits of structurally separating the local fixed network from the non-monopoly elements of Telstra's business or, alternatively, arrangements for ring-fencing the local fixed network and Telstra's business units. The NCC accepts that the framework for the regulation of the telecommunications sector is consistent with CPA principles, at least to the extent that responsibility for regulation is independent of Telstra.

Whilst the Commonwealth has not undertaken a formal clause 4 review, it noted that industry regulation does not lie with Telstra. The Commonwealth also advised the NCC that competition and regulatory matters were addressed in a series of reviews pertinent to both the partial sale of Telstra and the broader telecommunications sector. These reviews include the Telecommunications Policy Review, the Telstra Scoping Study, the Review of the Standard Telephone Service and the Senate Committee report *Telstra: to sell or not to sell?*

The Commonwealth stated that the pre-privatisation reviews had led to the development of the current regulatory framework and other arrangements relevant to clause 4, including delivery of the telecommunications universal service obligation through an industry levy.

The Commonwealth indicated that it did not pursue structural separation of the local fixed network, preferring to prohibit anti-competitive conduct by carriers or carriage service providers (Part XIB of the Trade Practices Act (TPA)) and to facilitate access to services provided by carriers or carriage service providers (Part XIC of the TPA).

Part XIB of the TPA includes provision for the (ACCC) to make 'record-keeping rules' which enable it to, among other things, require telecommunications carriers to furnish specific accounting information necessary for analysis of predatory behaviour and the cost of providing network access. This provision exists because of the potential for vertically or horizontally integrated telecommunications carriers to have internal cost allocation arrangements, which are counterproductive to investigations of predatory behaviour and to determining the cost of providing access to a carrier's network.

Allied with its intention to increase the proportion of private ownership of Telstra, the Commonwealth recently proposed changes to the regulatory regime governing telecommunications, including amendments to the existing telecommunications-specific anti-competitive conduct and access provisions of the TPA. These changes were contained in the

Telstra (Transition to Full Private Ownership) Bill 1998 (as amended), which was defeated in the Senate on 4 July 1998.

The changes proposed by the Commonwealth would allow the ACCC to, among other things, disclose cost information kept by virtue of record-keeping rules and to establish a binding code of practice on how carriers provide other carriers with telecommunications network information, and use this information. Greater transparency of costs and certainty on use of commercial information should assist negotiations under the telecommunications access regime, which is designed to limit Telstra's monopoly power over its local fixed network.

The intended effect of the arrangements in place under Part XIB and Part XIC of the TPA is to limit possible anti-competitive behaviour arising from Telstra's local fixed network monopoly. The additional safeguards proposed in the *Telstra (Transition to Full Private Ownership) Bill 1998*, once in place, would go a considerable way to addressing the Commonwealth's responsibilities under clause 4 with respect to Telstra.

1.1. Tasman's Task

As part of the NCC's second tranche assessment of governments' progress with NCP Reform at the end of June 1999, Tasman Asia Pacific (hereafter referred to as "the Consultant") was asked by the NCC to review the *status* of the ACCC's proposed record-keeping rules and the Commonwealth Government's proposed arrangements for ring-fencing the local fixed network. In addition, the Consultant was asked to assess the likelihood that the new record-keeping rules will work effectively to facilitate competition in the telecommunications industry. In the process of this review, the Consultant has consulted with the relevant policy people in the relevant government departments.

2. ACCC'S RECORD-KEEPING RULES

2.1. Background

In the early 1990s, retail and limited carrier-based competition was introduced to the Australian telecommunications market. The Telecommunications Act 1991 set out the functions and statutory obligations of AUSTEL for the economic and technical regulation of the industry. The Act required AUSTEL to develop Chart of Accounts (COA) and a Cost Allocation Manual (CAM) detailing carriers' financial obligations to AUSTEL.

One of the objectives of the COA/CAM was to establish a horizontal accounting separation regime, requiring each carrier to provide financial data for each of its major retail services. This information was primarily intended to assist AUSTEL in identifying cross-subsidisation between services, and to detect anti-competitive practices by carriers. The COA/CAM, however, suffered from many shortcomings such as:

- Inadequate vertical separation between upstream network services and contestable downstream retail services.
- Internal costs at the access level were not explicitly identified.
- Reported information was historic and not forward looking.
- Certain definitions of services have become obsolete due to changing technology.

In summary, the COA/CAM did not provide the required information for AUSTEL to detect anti-competitive price discrimination and/or potential anti-competitive behaviour such as predatory pricing and cross-subsidisation.

2.2. ACCC's Proposed Record-Keeping Rules (RKR)

On 1 July 1997, the responsibility of administering competition and economic regulation of telecommunications services was transferred from AUSTEL to the ACCC. The ACCC's new responsibilities are primarily centred on:

- new enhanced competition powers under Part XIB of the Trade Practices Act (TPA); and
- new access provisions specific to telecommunications under Part XIC of the TPA.

As mentioned in Chapter 1, Part XIB of the TPA includes provision for the ACCC to make 'record-keeping rules' which enable it to, among other things, require telecommunications carriers to furnish specific accounting information necessary for analysis of predatory behaviour and the cost of providing network access.

In response to its obligation under Part XIB of the TPA, the ACCC chaired a RKR Working Group, comprising industry representatives and the ACCC's staff, to examine methods for developing a more appropriate and effective accounting separation framework than the current COA/CAM procedures.

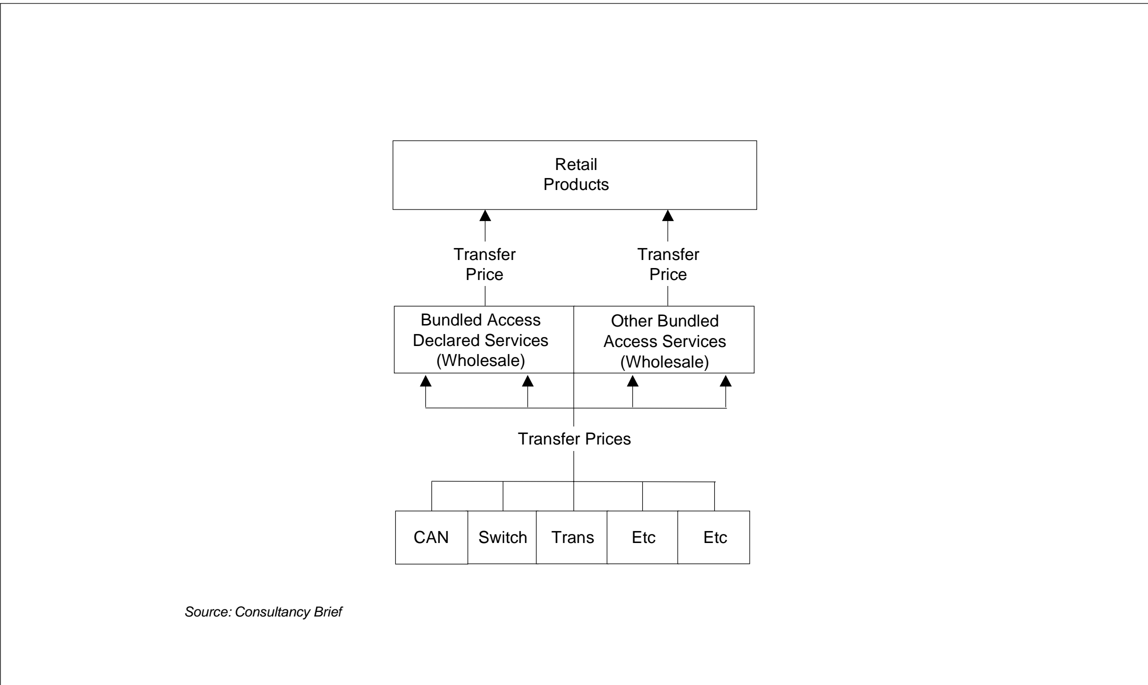
The Working Group developed a preliminary 'Conceptual Model' as a basis for developing a new accounting separation model that would overcome the key shortcomings of the existing COA/CAM procedures. In December 1998, the ACCC commissioned Arthur Anderson to develop a detailed architecture for a new accounting separation model and practical guidelines for the establishment of the revised RKR.

At the time of writing, the ACCC has not released the final draft report "Record Keeping Rules for the Telecommunications Industry" to the public. The information in this chapter is based on the draft report given to the Consultant by the ACCC.

2.2.1. The Conceptual Model

The conceptual model developed by the Working Group divides a vertically integrated carrier's operations into access and retail services (Figure 2)[1].

Figure 2: The Conceptual Model



As shown in Figure 2, a carrier's network services are *access* inputs used for downstream retail services, however, they can also be provided *wholesale* to competing carriers and service providers as well as internal carrier use.

2.2.2. The Proposed Accounting Separation Model

Although the Conceptual Model captures the desired elements of horizontal and vertical accounting separation, however, it is difficult to implement in practice. The proposed RKR architecture represents a practical refinement of the Conceptual Model, it addresses the

[1] The figures used in this report are adapted from the ACCC's draft report.

technical issues while meeting the ACCC's key information requirements. Figure 3 illustrates some of the practical difficulties associated with the Conceptual Model as outlined in the ACCC's Draft Report.

Figure 3: Overcoming Practical Difficulties of the Conceptual Model

	Problems with Conceptual Model	**Proposed Solution by RKR**
Full cost allocation to network elements is neither practical nor helpful.	Cost causality is weakened by the three tier approach as: – Underlying detail is lost as costs are aggregated and unitised for transfer pricing. – Many costs which are attributable to specific services are unattributable to network elements.	– Maintain cost causality as long as possible by allocating costs directly from general ledger to each wholesale service. – Report asset-related costs as line items within each service profit and loss, and consolidated to calculate total costs for each asset.
Declared services are not collectively exhaustive.	An approach that captures all costs associated with the wholesale business needs to be developed.	– Non-retail costs not associated with specified services of interest (declared and other) are captured in an 'other' category.
Declared and potentially declared PSTN services form a hierarchy of increasing network aggregation.	Certain declared PSTN services (e.g. local PSTN) are components of other services (e.g. local carriage). These services are therefore consumed both internally and externally at the wholesale layer.	– Ignore hierarchy and allocate cost only to services which are externally consumed (i.e. by third parties or the carriers retail business).

The proposed accounting separation model is a two-tier accounting model with the following important features (Figure 4):

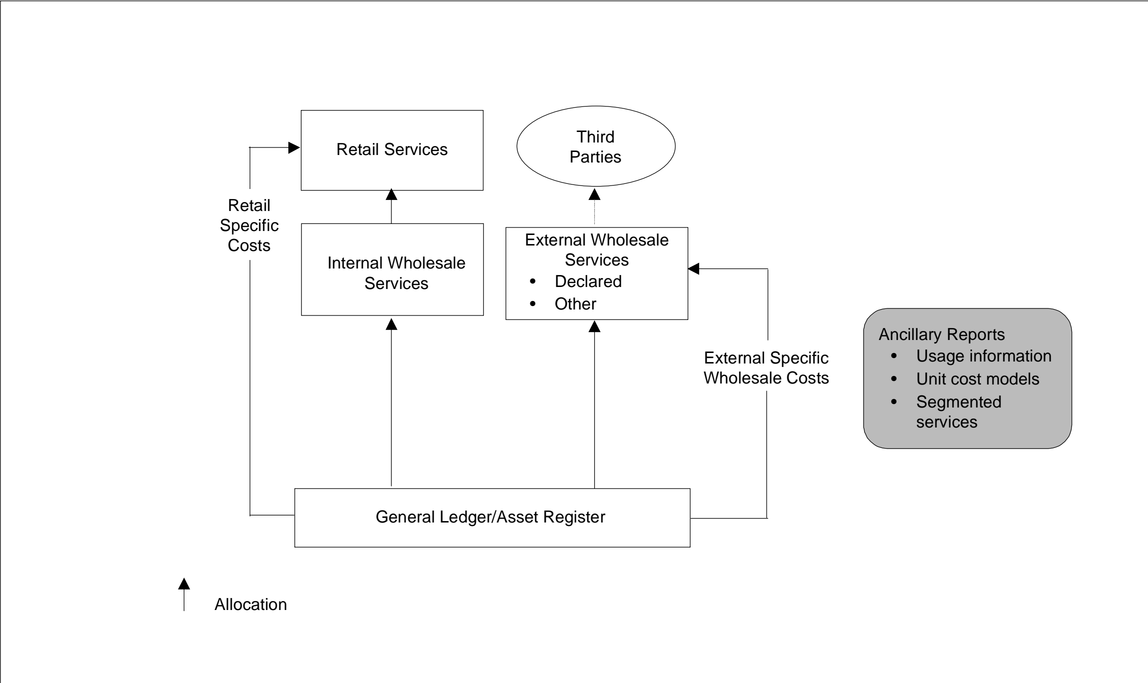
- Wholesale (internal and external) and retail services are separated.
- The internal business (i.e. declared services and other external wholesale services) and the external business (i.e. retail services and internal wholesale services) are separated.
- Costs that are specifically associated with providing only retail services and external wholesale services are allocated directly to those services.
- Revenues, costs and capital employed are generally allocated to each service as directly as possible from the General Ledger.
- There is no transfer pricing mechanism between the internal wholesale and retail services. All relevant costs, including the cost of capital, are incorporated in the retail cost of each service.
- In addition to the core financial reports for the defined services, a number of ancillary reports are required to meet the ACCC's specific information requirements. There are three main ancillary areas:

– Usage information for major services and for network assets underlying PSTN based services.

– Average unit cost models of declared services with little or no current usage.

– Supplementary service profit and loss, and mean capital employed reports based on a segmentation of interest to the ACCC such as geography.

Figure 4: Proposed Accounting Separation Model



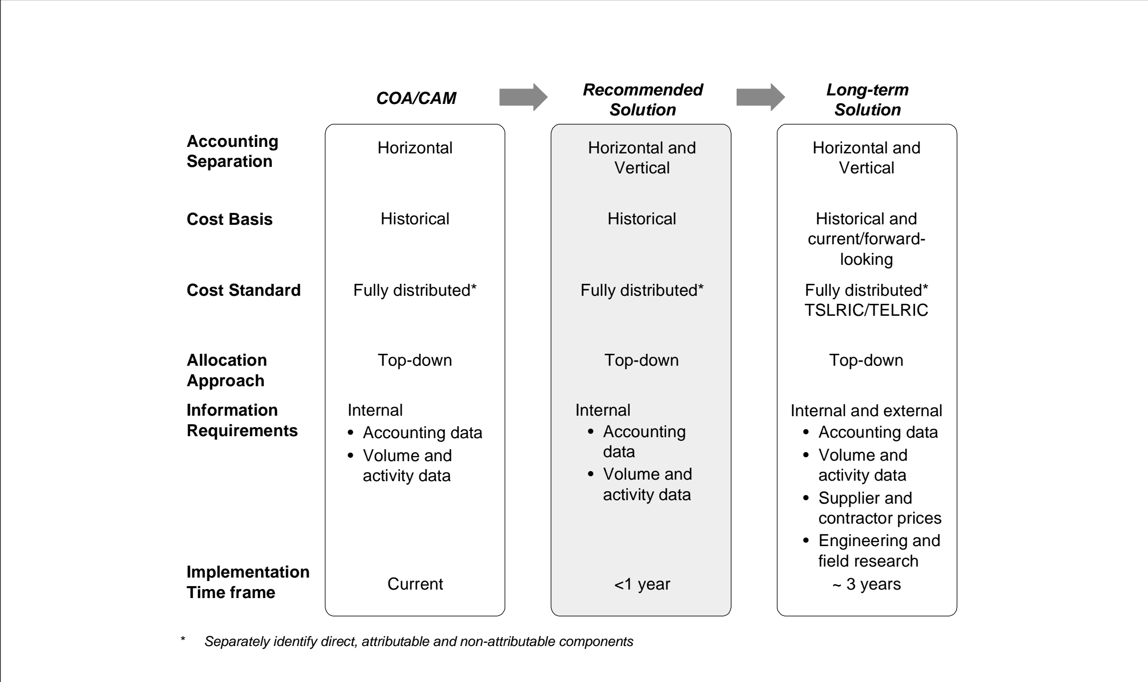
The key differences between the COA/CAM and the new RKR are illustrated in Figure 5.

Figure 5: Key Differences Between the COA/CAM and the New RKR

Area	COA/CAM	New RKR
Accounting Separation	Horizontal	Horizontal and vertical • Wholesale layer introduced. • Indicative Profit and Loss for external wholesale and internal retail businesses provided.
Estimated Costs of New Declared Services	None	Modelling approach to derive indicative costs for new services.
Segmentation for Key Services of Interest	None	Supplementary reports will provide segmented financial data for specific services of interest.
Reporting of Usage Data	None	Usage data reported for key services and key network assets.
Capital Employed	End of period balance sheet.	Statement of mean capital employed provided for each service.
Other	• Regulatory Accounting Procedures Manual (RAPM) requirements not clearly defined. • Weak process for amending RKR.	• Detailed RAPM requirements for greater transparency. • Tighter process to ensure amendments achieved in reasonable timeframe. • General refinement of allocation principles, service definition, etc. • Certain reports removed: reconciliation, transfer pricing, internal usage, chart of accounts listing.

The recommended evolution of the RKR is shown in Figure 6.

Figure 6: Recommended Evolution of Record Keeping Rules



TRADEOFFS

The new RKR involved several tradeoffs such as quality of information, and the pace and scope of change (Figure 7). In addition, a number of technical issues needed to be resolved such as selecting an allocation approach, cost basis (i.e. historical versus current) and cost standard (i.e. fully distributed versus incremental). Figure 8 presents the rationale for the selection of key elements in the design of the new RKR.

Figure 7: Key Tradeoffs in Designing New RKR

Objectives	**Benefits**	**Costs**	**Constraints**
Information Quality – Theoretically sound. – Fine granularity. – Rigorous cost causality in allocation methods.	– Improved ACCC decisions. – Increased industry confidence in ACCC decisions. – Enhanced "self-regulatory" effect.	– Higher costs. – Longer timeframe to develop.	– Carriers' existing costing systems and data.
Pace of Change – Rapid versus gradual.	– Rapid implementation will prevent Telstra consolidating its market power.	– Increased risk of methodological error and implementation failure. – Potentially increased cost of development.	– Implementation practicalities.
Scope of Change – Staged versus "big bang".	– Some improvements achieved earlier. – Implementation risk reduced. – Able to adjust to technology and other changes.	– Greater likelihood of settling for a "satisficing" end point.	– Limitations of interim deliverables.

Figure 8: Rationale for the Selection of Key Elements for the New RKR

Issue	Recommendation	Rationale
Architecture	– Separation between wholesale and retail businesses. – Identification of key upstream costs (facilities and activities).	– Pragmatic first step in evolution of RKR. – Ability to identify upstream versus downstream costs is key to diagnosing vertical cost shifting. – Wholesale pricing is increasing important.
Cost Basis	– Historical	– Moderate scope of change controls development and implementation risk. – Reconciles to statutory accounts, so builds confidence in new separation model. – Foundation for eventual current cost-based RKR. – Operators need time to go down learning curve before implementing current costing methodologies.
Costing	– Fully distributed costs, with direct, attributable and unattributable elements separately identified.	– Common allocation rules provide a basis for comparing costs across different companies and avoids manipulation. – By separately identifying direct, attributable and unattributable elements, proxies for incremental costs can be derived.
Other – **Leverage points**	– Highest granularity in services dependent on bottleneck facilities. – Potential to distinguish between major geographical or other segments.	– Variations in granularity will help to minimise compliance costs while retaining insights. – Anticipate changes likely to impact costs and sources of power, e.g. IP networks, xDSL, wireless technologies.
– **Flexibility**	– Avoid overly prescriptive architecture, e.g. “defined’ hierarchy of network elements and services.	– Rapid technological change makes it harder to use network elements as basic building blocks. – Interdependent service definitions will make it harder to add new services or redefine existing ones.

SERVICES INCLUDED IN THE NEW RKR

The new RKR framework applies to services that are likely to be subject to anti-competitive conduct or access-related investigations. Telecommunications services that are subject to the new RKR are:

- *Internal Carrier Retail Services* including: End User Access; Local Calls; Domestic Long Distance; International Long Distance; International Leased Lines; Domestic Leased Lines; Digital Data Service; ISDN; Packet Switched Data; Fixed to Mobile; GSM Mobiles; AMPS Mobiles; CDMA Mobiles; Payphone Services; Internet Services; Information Services; Specialised Call Services; Directory Services; and Other Retail Services.

- *Internal Carrier Wholesale Services* including: Wholesale Broadcast; Wholesale End User Access; Wholesale Local calls; Wholesale Local Number Portability; Wholesale Domestic Long Distance; Wholesale International Long Distance; Wholesale International Leased Lines; Wholesale Domestic Leased Lines; Wholesale Digital Data Carriage; Wholesale ISDN Carriage; Wholesale Packet Switched Service; Wholesale Fixed-Mobile; Wholesale GSM Carriage; Wholesale AMPS Carriage; Wholesale CDMA Carriage; Wholesale Mobile Number Portability; Wholesale Payphone Services; Wholesale Internet Services; Wholesale Information Services; Wholesale Specialised Call Services; Wholesale Freephone Number Portability; Wholesale Directory Services; and Other Internal Wholesale Costs.

- *External Carrier Wholesale Services* including: Conditional Local Loop (Declared); Domestic PSTN Originating/Terminating (Declared); Transmission (both Declared and Non Declared); Digital Data Access (Declared); ISDN Originating/Terminating (Declared); GSM Originating/Terminating (Declared); AMPS Originating/Terminating (Declared); AMPS-GSM Diversion (Declared); Broadcasting (Declared); Local Number Portability; Freephone Number Portability; Mobile Number Portability, Other External Wholesale Services.

REPORTING REQUIREMENTS

All telecommunications carriers who are or could be providing declared telecommunications services will be subject to the proposed Record-Keeping Rules. The ACCC may also require other carriage service providers to adhere to the RKR requirements. The *core* outputs of the RKR will be:

- A Capital Adjusted Profit statement.

- A Mean Capital Employed statement for each whole and retail service identified.

- A Fixed Asset statement identifying historical/revalued asset cost and accumulated depreciation.

- A Weighted Average Cost of Capital (WACC) report.

In addition, the following ancillary reports will also be required:

- usage information for specific network asset;

- models of unused or limited use declared asset; and
- market segment splits for specific products.

REPORTING CYCLE

Currently, the reporting cycle for the COA/CAM is every three months. The recommended reporting cycle for the proposed RKR is every six months in line with standard statutory reporting requirements (Figure 9).

Figure 9: Reporting Cycle for the Proposed RKR

Report	Period	Submission to ACCC Following Statutory Reporting Date
Profit and Loss Statement	6 months	Within seven days of issue.
Mean Capital Employed Statement	6 months	Within seven days of submission to ASIC or ASX.
Ancillary Reports – Usage – Models of declared services – Segments	6 months	Within seven days of submission to ASIC or ASX.

2.2.3. Implementation Timeframe

The ACCC foresees that the proposed accounting separation model can be implemented relatively quickly. The ACCC notes that the technical implications are fairly modest as the proposed model broadly maintains COA/CAM line item categories which are captured by existing systems; and avoids the problems associated with developing a completely new notion of network elements.

The preliminary implementation timetable for the new RKR is as follows.

- The Final Report on RKR by Arthur Anderson, in collaboration with the ACCC, will be released for Public Consultation in early June 1999. The Draft Instrument will also be released for public comment.
- Modification of RKR and Draft Instrument are expected to be finalised by end of July 1999.
- The Final Report is expected to be issued in August 1999.
- From the date of issuance of the Final Report to December 1999, it is expected that applicable telecommunications carriers and operators carry out the implementation of the new RKR.
- The first set of RKR reports (excluding supplementary segment reports) are expected to be available in January 2000.
- The first set of segmented reports are expected to be available by August 2000.

3. RKR, RING-FENCING ARRANGEMENTS AND COMPETITION

3.1. Commonwealth Government's Policy in Relation to Structural Separation of Telstra

Structural separation differs significantly from accounting separation. Accounting separation usually provides the information necessary to enable a regulatory authority to detect anti-competitive conduct, whereas structural separation removes the incentives for a firm to act in an anti-competitive manner. The main objectives of introducing structural separation in telecommunications are to discourage or eliminate cross-subsidisation between services, and to prevent anti-competitive practices by dominant carriers, with the ultimate aim of increasing competition in the industry.

Currently, the Commonwealth Government does not intend to pursue structural separation of Teltra's business operations. The Government, instead, prefers ring-fencing arrangements to structural separation. Ring-fencing arrangements usually involve accounting separation plus other non-financial arrangements, but leave all structural issues (boundaries, business areas and most incentives) unchanged. While ring-fencing could provide the basis for actions and differing charging policies and levels, to date the Government has no coordinated policy in regard to ring-fencing the carrier's business operations.

ACCOUNTING SEPARATION

Accounting separation:

- Is a means of increasing the amount of information available to the regulatory authority when monitoring and controlling conduct.
- Allows the regulator to see the carrier through a set of information "windows", *as if* it were a number of structurally separated firms, while allowing the firm to remain vertically and horizontally integrated.
- Requires the carrier to provide separate accounts for the different services that it provides.
- Makes transparent the wholesale prices that a carrier charges its own retail businesses, and hence to ensure that the carrier does not discriminate against other operators in setting wholesale charges to them.

The existing COA/CAM regime is a form of accounting separation, however, it has not achieved its main objectives as discussed in the previous chapter. As noted, Part XIB of the TPA includes provision for the ACCC to implement new record-keeping rules. The new RKR is an improvement on the existing COA/CAM, it addresses the shortcomings of the COA/CAM while incorporating new features.

3.2. RKR and Competition

The new RKR will provide the ACCC with the necessary financial information so as to assess anti-competitive behaviour by carriers and carriage service providers. The remainder of the

section will examine how the new RKR will be used to detect anti-competitive behaviour in the telecommunications industry.

3.2.1. Use of RKR to Assist in the Detection of Anti-Competitive Behaviour

1. An access price above the total service long-run incremental cost (TSLRIC) of providing the service will lead to inefficiencies and hinder competition. While an access price below the TSLRIC may be predatory. The ACCC used the following four broad principles in assessing undertakings and in conducting arbitrations in relations to access prices:

1. Access prices should be cost based.
2. Access prices should not discriminate in a way that reduces efficient competition.
3. Access prices should not be inflated to reduce competition in dependent markets.
4. Access prices should not be predatory.

The information provided through the RKR may be relevant in assessing whether an access price is consistent with the above principles (Figure 10).

Figure 10: Use of RKR Data in Assessing Access Price

Rule	Potential relevance of RKR data
"Access prices available to competitors must not be greater than the access provider's best price to its own vertically integrated operations (unless cost justification is provided)"	The RKR require carriers to develop costs for internally provided wholesale services. If the declared service under consideration is similar in nature to one of these internal wholesale services, the cost of the service (including the cost of capital) provides a starting point for determining the access provider's "price" of its own vertically integrated operations. Various adjustments may have to be made to account for specific differences between the declared and internal services, but it should be feasible to produce a first-pass estimate in many cases.
"Any increase in an access price must be based on recognisable changes in the cost of providing the service"	The RKR require carriers to provide detailed cost information for declared services. Changes in access prices should therefore be mirrored by changes in the reported costs. Furthermore, it should be possible to pinpoint these changes to specific line items.

Source: ACCC Draft Report.

The ACCC recognises that measuring the TSLRIC is a difficult, time-consuming and error-prone task, however, it has suggested four criteria which may assist it in determining whether an access price falls within an acceptable (Figure 11).

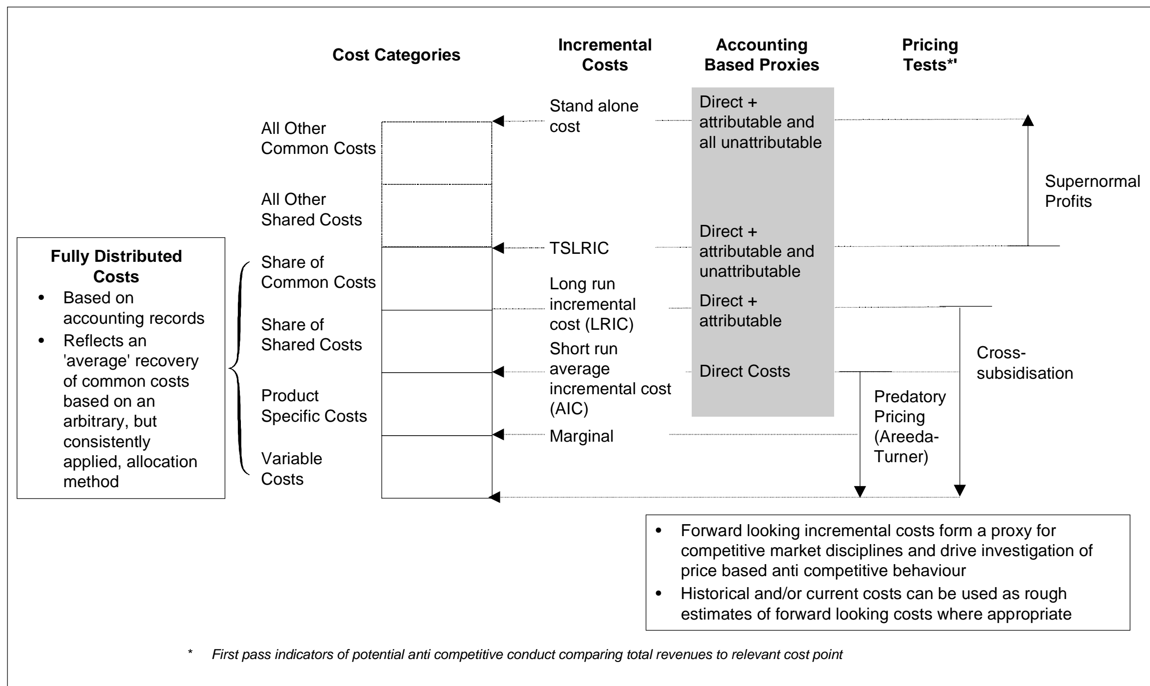
Figure 11: Relevant RKR Information to Access Pricing Criteria

Criterion	Relevance of RKR Data
The total cost of providing the service should not exceed the stand-alone costs.	An upper boundary for the for the stand-alone cost of providing a service could be obtained by subtracting the direct and attributable costs associated with all other services from the company's total wholesale cost base. In practice, this boundary will usually be higher than stand-alone cost, and will exceed any reasonable access price.
The allocation of common costs across a set of services should not exceed total common costs for that set of services.	This will always be the case if the RKR allocation principles are consistently applied.
The common costs must be common to the declared service and not unduly allocated to that service.	The RKR require that all allocation decisions be based on cost causality where possible. Where cost causality is unclear, a general allocator is used to spread costs across services in a non-discriminatory manner.
The vertically integrated internal transfer price should incorporate any common costs incorporated in the access price (i.e. the same common costs should be equally reflected in the internal transfer price and the access price).	All costs, except for retail specific costs, are allocated to both internal and external wholesale services, and the same allocation principles apply to all services. Therefore, common costs will be incorporated in both internal and external wholesale services on the same basis.

Source: ACCC Draft Report.

2. Anti-competitive behaviour such as predatory pricing and cross-subsidisation will lead to inefficiencies and hinder competition. Figure 12 illustrates how accounting based proxies obtained from the RKR can be used to test for supernormal profits, predatory pricing and cross-subsidisation. For example, an access price above TSLRIC up to the stand-alone cost could be used as an indicator for the degree of supernormal profits that a carrier earns from providing the access service. Information from the RKR can be used to determine a proxy for stand-alone cost and TSLRIC: the accounting proxy for stand-alone cost is direct cost plus attributable and all unattributable costs, while for TSLRIC is direct cost plus attributable and unattributable costs associated with the product. In addition, if a carrier charges a price below the average incremental cost for one of its products, then this would indicate that the carrier is engaging in predatory pricing, and is subsidising the product with a higher price charged for another product. The direct costs obtained from the RKR could be used as an accounting poxy for average incremental cost.

Figure 12: Accounting Based Proxies Used to Test for Anti-Competitive Behaviour



Source: ACCC Draft Report.

The key question is that if structural separation is not an option, would accounting separation be a sufficient alternative? A report by London Economics prepared for the then Department of Communications and the Arts (DoCA) noted that[2]:

> *…while accounting separation has theoretical appeal, in practice it may not be so desirable. It may involve a significant cost burden both for the firm and for the regulatory authority, and if not implemented correctly it will not achieve its aim.*

In addition, there is abundant evidence in the UK to show that accounting separation in telecommunications services, such as mobile and other single product relationships, has not removed the incentives or ability to cross subsidise. Moreover, the existing COA/CAM, a form of accounting separation, has not prevented dominant carrier(s) such as Telstra from engaging in anti-competitive behaviour. But would a broader ring-fencing framework achieve the same objective of structural separation?

3.3. Ring-Fencing Arrangements

Ring-fencing is a vague concept, the arrangements that are entailed in a ring-fencing regime are different for different industries. At the centre-piece of a ring-fencing model is accounting separation, however, it also contains a list of arrangements that are designed to limit the dominant carrier's market power.

[2] London Economics (1995), *Accounting Separation*, a paper prepared for the Department of Communications and the Arts.

CURRENT STATUS OF RING-FENCING ARRANGEMENTS

The new RKR is an improved accounting separation model to the COA/CAM as it separates vertically and horizontally a carrier's financial operations. The RKR is a necessary first step in establishing a broader ring-fencing framework for the telecommunications industry. As mentioned, at present the Government does not have a coordinated policy in regard to ring-fencing the telecommunications industry. However, the new RKR, the additional safeguards proposed in the *Telstra (Transition to Full Private Ownership) Bill 1998* plus a number of new provisions in the *Telecommunications Legislation Amendment Bill 1998* are potentially positive steps towards establishing a more comprehensive, if second-best, framework for increasing competition in the industry.

Proposed Amendments to Division 6 of Part XIB of the TPA

Under the new amendments, the ACCC is allowed to disclose:

- A particular report, or particular extracts from a report, given to the ACCC by a carrier or a carriage service provider, in accordance with the record-keeping rules.
- A particular report, or particular extracts from a report, prepared by a carrier or a carriage service provider, in accordance with the record-keeping rules.
- A particular series of periodic reports, or particular extracts from each of the reports in that series, prepared by a carrier or a carriage service provider, in accordance with the record-keeping rules.

The report is to be disclosed to the public only if the disclosure would be likely to promote competition, or to facilitate the operation of Part XIB; or Part XIC; or Division 3 of Part 20 of the *Telecommunications Act 1997* (which deals with Rules of Conduct relating to dealings with international telecommunications operators); or Part 6 of the *Telstra Corporation Act 1991* (which deals with regulation of Telstra's charges).

REVIEW OF PART XIB OF THE TPA

According to Division 13 of Part XIB of the TPA, the Minister of Communications, Information Technology and the Arts will conduct a review of the operation of this Part of the TPA before 1 July 2000. The Terms of Reference for the Review have not been written, however, in conducting the review, consideration must be given to the question: whether any or all of the provisions of Part XIB should be repealed or amended? That is, the review will examine issues such as whether the current provisions in Part XIB are adequate in addressing anti-competitive conduct by carriers and carriage service providers, and/or whether broader ring-fencing arrangements are required.

EFFECTIVENESS OF A RING-FENCING REGIME

A ring-fencing regime may impose a significant cost burden both for the firm and for the regulatory authority. Ring-fencing arrangements do not remove, and are only intended to reduce, the incentive for a dominant carrier to act in an anti-competitive manner. If these arrangements are not implemented properly, then they will not achieve the desired objectives. In addition, there are still significant informational and other advantages associated with a vertically integrated structure which are not removed by a simple process of ring-fencing. For

example, a vertically integrated firm, such as Telstra, has detailed customer knowledge, a large customer base, customer reach and brand identity, which are sources of its market power. Other sources of market power are derived from the bargaining power that it has with its suppliers of inputs - which will impact significantly on its costs; and the control of key assets such as the transmission facilities.

3.4. A Structural Separation Model for the Telecommunications Industry

As discussed above, a ring-fencing regime will not remove the sources of market power and may not be an effective strategy to combat anti-competitive behaviour, which discourages real competition in the telecommunications industry. It has been almost 10 years since competition was introduced into the telecommunications industry in Australia (limited competition in early 1990s and full competition in 1997), and Telstra remains the dominant player, with significant market power, in the local telecommunications services market. Its major rival, Optus, has made little inroad into the local market.

Why should the telecommunications industry be treated differently from other infrastructure industries such as electricity, gas and railways, where there have been significant structural reforms, including horizontal and vertical unbundling? For example, the structural separation of the electricity industry in Victoria, separating generation, distribution and transmission facilities, has introduced real competition into the electricity market. As a result, consumers and industries have benefited immensely from the low prices. In addition, competition forces players in industry to choose the least cost method of production.

The consultant considers that the ring-fencing regime may not be an effective approach to bring out real competition in the local telecommunications market. Ring-fencing will not remove the key sources of Telstra's market power, and therefore, will not remove the incentive to engage in anti-competitive behaviour. The Consultant considers that the benefits of structural separation outweigh the costs. For example, in the US, the structural separation of AT&T into a long distance operation and a local loop operation, coupled with the recent introduction of competition into the local loop market, has lead to substantial benefits for customers and the general economy.

THE PROPOSED MODEL

There are many alternative models of structural separation of the local loop network. One possible model could be the separation of the Customer Access Network (CAN), the natural monopoly element of the network, from the transmission facilities i.e. from the CAN to trunk switches. Eventhough the costs of telecommunications technology have decreased significantly in recent years, the costs of duplicating the wires from a residential home to the local exchange may outweigh the benefits. The CAN may be operated by an independent telecommunications operator, under the supervisor of a regulator authority, such as the ACCC. The CAN operator provides access to fringe telecommunications operators. The telecommunications operators can then use their own transmission and switching facilities to transmit telecommunications services, such as a telephone call, from their network to the CAN operator's network. This model separates the natural monopoly element of the network and introduces real competition in the local loop market (Figure 13).

Figure 13: The Consultant's Proposed Structural Separation Model

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Appendix C NCP Contacts

Further information regarding NCP can be obtained by contacting the relevant Commonwealth, State or Territory competition policy unit or the National Competition Council.

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Email: info@ncc.gov.au
Website: http://www.ncc.gov.au

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New South Wales

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Regulatory Reform Branch
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