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FINAL REPORT

NATIONAL COMPETITION POLICY

FIFTY-FOURTH REPORT

OF THE

ECONOMIC AND FINANCE COMMITTEE

Tabled in the House of Assembly and ordered to be published on 17 October 2005

Fourth Session, Fiftieth Parliament

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ECONOMIC AND FINANCE COMMITTEE

1.1 Membership

The Economic and Finance Committee is established under Section 4 of the *Parliamentary Committees Act 1991*. Section 5 states that the membership of the Committee is to comprise seven members of the House of Assembly. A Minister of the Crown is not eligible for appointment to the Committee.

The House of Assembly appointed the fourth Economic and Finance Committee on 7th May 2002 following the State Election, held 9th February 2002. At its first meeting, the Member for Reynell, Ms G Thompson, was appointed Presiding Member.

The following members comprise the Fourth Committee:

Ms G Thompson MP (Presiding Member)
Hon I F Evans MP
Hon G M Gunn MP
Mr J Rau MP
Mr J Snelling MP
Ms Karlene Maywald MP (until 23 July 2004)
Mr M Hamilton-Smith MP (as from 14 September 2004)
Mr M O'Brien MP (until 22 March 2005)
Hon P White (as from 4 April 2005)

Secretary to the Committee:
Dr Paul Lobban

Research Officer:
Mr Andrew Blue

Members of the Committee are appointed pursuant to Section 20, and cease to be members pursuant to Section 21 of the *Parliamentary Committees Act 1991*.

1.2 Functions

The functions of the Economic and Finance Committee are set out in Section 6 of the *Parliamentary Committees Act 1991*. They are:

(a) to inquire into, consider and report on such of the following matters as are referred to it under this Act:

(i) any matter concerned with finance or economic development;

(ii) any matter concerned with the structure, organisation and efficiency of any area of public sector operations or the way in which efficiency and service delivery might be enhanced in any area of public sector operations;

(iii) any matter concerned with the functions or operations of a particular public officer or a particular State instrumentality or

publicly funded body (other than a statutory authority) or whether a particular public office or a particular State instrumentality (other than a statutory authority) should continue to exist or whether changes should be made to improve efficiency and effectiveness in the area;

(iv) any matter concerned with regulation of business or other economic or financial activity or whether such regulation should be retained or modified in any area;

(b) to perform such functions as are imposed on the committee under this or any other Act or by resolution of both Houses.

1.3 References

Pursuant to Section 16 subsection (1) of the *Parliamentary Committees Act 1991*, any matter that is relevant to the functions of the Committee may be referred to the Committee-

(a) by resolution of the House of Assembly;

(b) by the Governor, by notice published in the Gazette;

(c) of the Committee's own motion.

Subsection (1) is in addition to and does not derogate from the provisions of any other Act under which a matter may be referred to the Committee.

1.4 Ministerial responses

Pursuant to Section 19 of the *Parliamentary Committees Act 1991*, if a report contains recommendations, the Minister with responsibility in the area concerned is required to respond within four months and include in the response statements as to –

which (if any) recommendations of the Committee will be carried out and the manner in which they will be carried out;

and

which (if any) recommendations will not be carried out and the reasons for not carrying them out.

The Minister must cause a copy of the response to a Committee's report to be laid before the Committee's appointing House within six sitting days after it is made.

2 SPECIFIC REFERENCE

On 9 June 2004:

On its own motion the Economic and Finance Committee (the Committee) resolved the following:

To inquire into the impact of National Competition in South Australia, and in particular, the withholding of National Competition payments by the Federal Government.

3 BACKGROUND TO THE INQUIRY

The Committee decided to undertake this inquiry into the impact of national competition policy as a part of its monitoring function pursuant to section 6(a)(iii) of the Parliamentary Committees Act 1991. This section empowers the Committee to inquire into any matter concerned with regulation of business or other economic or financial activity or whether such regulation should be retained or modified in any area.

The Committee initiated the inquiry in response to the foreshadowed withholding of national competition payments to South Australia in December 2003 by the National Competition Council (NCC).[1] Committee members were concerned that a strict application of NCC rules underpinning competition payment penalties due to a 'perceived' lack of progress on legislative reviews (notably those pertaining to liquor retailing, ownership restrictions in health professions and barley marketing) failed to appreciate the specific and significant issues faced by a small state such as South Australia.

Furthermore, anecdotal evidence suggested that the penalties recommended by the NCC were being applied without an adequate assessment of the implications of competition based legislative reform, especially in relation to the above mentioned areas. The Committee resolved therefore to obtain written submissions on National Competition Policy (NCP) from key stakeholders in these sectors, and approached the South Australian Hotels Association, the South Australian Farmers Federation and the South Australian Pharmacy Guild as a starting point.

In addition, the Committee approached the South Australian Milk Vendors Association to obtain their views on NCP as they had publicly expressed reservations about changes to milk distribution and in particular, the potential abuse of market power by larger supermarket chains.

The Committee reserved the right to call witnesses from these and any other industries, as well as relevant officials from State Government agencies so as to be more informed on NCP and to determine whether the impact of the proposed withholding of competition payments to South Australia could be justified.

[1] National Competition Council Media Release – 8 December 2003, NCC website - http://www.ncc.gov.au

4 NATIONAL COMPETITION POLICY OVERVIEW

In 1992, the Council of Australian Governments (CoAG), which comprises all nine State, Territory and Federal Governments, commissioned Professor Fred Hilmer to Chair an "Independent Committee of Inquiry into National Competition Policy". In 1995, acting on the Report's recommendations, a number of reforms were drawn together to form a package, agreed upon by all Australian Governments, called National Competition Policy (NCP).

The aim of NCP was to introduce reforms that enabled and encouraged competition. As stated on its website the NCC describes NCP as:

- The extension of 'Trade Practice' laws prohibiting anti-competitive activities (such as the abuse of market power and market-fixing) to all businesses – previously most government and some private businesses were exempt.
- The introduction of 'Competitive Neutrality' so that privately-owned businesses can compete with those owned by Government on an equal footing.
- The review and reform of all laws that restrict competition unless the benefits of the restriction to the community as a whole outweigh the costs.[2]

According to the NCC, NCP was designed to extend the Federal Government *Trade Practices Act 1974* to previously excluded State Government businesses with the objective of making them more commercially focussed and expose them to competitive pressure. More generally, NCP introduced regulatory arrangements with the aim of securing third-party access to infrastructure services and to guard against overcharging by monopoly service providers. NCP also introduced a process for reviewing, and where appropriate amending or rescinding, a wide range of State legislation which restricted competition.[3]

The NCP package is implemented through a number of intergovernmental agreements, which, amongst other things, provided for the creation of the Australian Competition and Consumer Commission (ACCC).[4] The CoAG Agreement also established the NCC as the body to manage the review process and to oversee the associated competition payment schedules and penalty system, which is now a central feature of NCP institutional frameworks.

Competition payments are paid by the Federal Government to the States and Territories as a mechanism to 'return' the fiscal dividend from their implementation of agreed reform commitments and progress on the Legislation Review Program (LRP). Competition payments recognise that while the States and Territories have responsibility for significant elements of the NCP reforms, much of the financial dividend from the economic growth arising from the NCP reforms accrues to the Commonwealth Government through the taxation system.

[2] http://www.ncc.gov.au/articleZone.asp?articleZoneID=16 1
[3] http://www.ncc.gov.au/articleZone.asp?articleZoneID=267#Article-127
[4] Note also as part of the NCP reforms the Trade Practices Act 1974 prohibits companies which are big enough to strongly influence a market from using their position to damage other businesses. It prevents a number of firms from banding together to control a market and raise prices and, regulates business mergers which would reduce competition whereas the Prices Surveillance Act 1983 enables the ACCC to make assessments as to whether proposed price increases are reasonable or not, and when a Government business has a monopoly or a very high degree of market power.

The payments are seen as a means, therefore, of distributing across the community the gains that arise from NCP reform. The NCC primarily assesses governments' progress against agreed NCP obligations and makes recommendations to the Commonwealth Treasurer on the distribution of NCP payments. The NCC has the authority to recommend that the Commonwealth Treasurer reduce or suspend NCP payments otherwise earmarked to any State and Territory if that State or Territory has been judged to have not invested in a timely manner in the LRP.

The LRP, it is reasonable to suggest, has resulted in an arduous process for all State and Territory Governments. When the NCP was first implemented, governments identified around 1700 pieces of legislation as containing competition restrictions that should be reviewed and, where warranted, reformed. Of these, the NCC considered that around 800 were priority areas - that is, areas in which restrictions had the greatest impact on competition.

Towards the end of 2003, the NCC completed an assessment of the performance of governments in meeting their priority review obligations. The decision to recommend penalties to a number of State and Territory Governments reflected the view of the NCC that after eight years, at least two previous 'deadlines' for completing LRP obligations and despite specific warnings in the 2002 NCP assessment, substantive obligations had not been met.[5]

5 SOUTH AUSTRALIAN LEGISLATIVE REVIEW PROGRAM

5.1 Legislative Review Program: Obligations, Task, Process

The responsibility for the LRP in South Australia rests primarily with the National Competition Policy Implementation Unit, Department of the Premier and Cabinet. The Committee received a briefing on the LRP from its Director, Mr Rod Williams, and in his appearance before the Committee, Mr Williams outlined South Australia's obligations and tasks under NCP as well as the processes his Unit had implemented thus far.

In summary, Mr Williams informed the Committee that:

- South Australia was obliged to remove competition restrictions if non-legislative alternatives existed or if the costs of restriction were greater than the public benefits.
- South Australia was obliged to retain competition restrictions if legislation is the only feasible option and if the public benefits were greater than the costs.
- The legislation covered by the LRP spans a wide range of areas, including: the professions and occupations; statutory marketing of agricultural products; fishing and forestry; retail trading; transport; communications; insurance and superannuation; child care; gambling; and planning and development services.
- The requirement for South Australia was to review and reform 178 Parliamentary Acts.
- A South Australian NCP Reference Group was established in February 1999 and its role was to:

[5] National Competition Council Media Release – 8 December 2003, NCC website - http://www.ncc.gov.au

- Clarify objectives of legislation
- Identify restrictions on competition
- Consider feasible alternatives to legislation
- Assess likely effects
- Assess costs & benefits
- Provide conclusions and recommendations

- The NCP Reference Group determined that restrictions on competition were evident in various forms, for example:
  - Entry barriers through registration, licensing, accreditation, qualifications, experience, bans & prohibitions.
  - Conduct limitations - multi disciplinary practices, discretionary powers, standards; and
  - Discrimination between competitors through professional privileges, exclusions, exclusive or sole provider or acquirer.
- The public benefit test as a guideline for the NCP Reference Group was built on the presumption that competitive markets were more likely to benefit consumers & business and therefore any exceptions must be justified by public interest reasons so as to retain restrictions.
- Examples of public benefit test include:
  - Ecologically sustainable development
  - Social welfare and equity including community service obligations
  - Occupational health & safety, industrial relations and access & equity
  - Economic & regional development
  - Interests of consumers
  - Competitiveness of Australian business
  - Efficient allocation of resources

In terms of the overall LRP requirements South Australia had 178 Parliamentary Acts to review of which his Unit had categorised as 29 as major and 149 as minor in nature. In terms of his personal assessment of the South Australian LRP experience, Mr Williams stated that in hindsight the list of legislation had been excessive and that limited resources, guidance and experience had delayed the commencement of some reviews. [6]

5.2 Competition Payment Schedule and Penalties Summary

Under the *Agreement to Implement the National Competition Policy and Related Reforms*, signed at the CoAG Meeting of 11 April 1995, the following schedule of payments was agreed upon.

> *"The per capita element was estimated to be an annual cost to the Commonwealth of $2.4 billion by 2005-06. There was to be three tranches of general-purpose payments in the form of a series of Competition Payments. The first tranche of Competition Payments commenced in July 1997 and was made quarterly thereafter. The annual payment from 1997-98 under the first tranche was projected to be $200 million in 1994-95 prices and was to be indexed annually to maintain its real value over time. Commencement of the first tranche of the Competition Payments and the per capita guarantee was subject to the States meeting the conditions in the CoAG Agreement.*

[6] Rod Williams, National Competition Policy Implementation Unit, Department of the Premier and Cabinet, PowerPoint Presentation, Economic and Finance Committee Meeting, Kingston Room, Old Parliament House, Adelaide, Wednesday 25 May 2005.

The second and third tranches of the Competition Payments would commence in 1999-2000 and 2001-02. The annual Competition Payments would be $400 million, in 1994-95 prices, from 1999-2000 and $600 million, in 1994-95 prices, from 2001-2002. These payments would also be indexed in real terms.

The Competition Payments to be made to the States in relation to the implementation of NCP and related reforms would be distributed to the States on a per capita basis. These Competition Payments would be quarantined from assessments by the Commonwealth Grants Commission. If a State had not undertaken the required action within the specified time its share of the per capita component of the Competition Payments pool would be retained by the Commonwealth. Prior to 1 July 1997, 1 July 1999, and 1 July 2001 the NCC would assess whether the conditions for payments to the States to commence on those dates had been met.[7]

Under the CoAG Agreement, governments agreed to the 30 June 2002 deadline for completing the LRP. However owing to the timing of its assessments, the NCC provided a further year's extension and notified all governments that the program had to be completed for the 2003 NCP assessment. All governments subsequently failed to complete their review and reform activity by the 2003 assessment, so the NCC recommended competition payment penalties.

In aggregate terms, by late 2003, around 70 per cent of governments' nominated legislation had been reviewed and, where appropriate, reformed. For priority legislation, the rate of compliance was substantially lower, at around 56 per cent. This rate compares with around 20 per cent in 2001 and nearly 40 per cent in 2002.[8]

As mentioned above, failure to expeditiously review the relevant Acts gives the NCC the authority to recommend that the Commonwealth Treasurer reduce or suspend NCP payments otherwise available to the States and Territories. In South Australia's case the legislative reviews being singled out for application of penalty payments (which attracted the attention of the Committee) were those related to barley export marketing, liquor retailing and certain health professions vis-à-vis ownership restrictions.

Each of these reviews 'drew' a $3 million penalty. There was also a further $3 million in payments placed in what is termed a suspension pool -i.e- pending further progress on other reviews and these included:

- Taxi licence & Tow truck licence caps
- Petroleum Products - limits on retail sites
- Fisheries – licences
- Employment agents
- Opal mining
- Shop trading hours (remaining limits)

As at the end of 2004 South Australia had completed 60% of its LRP and the competition payments paid to South Australia were as follows:

1997-98 - $34.3 M
1998-99 - $38.4 M

[7] http://www.coag.gov.au/meetings/110495/attachment_a.htm
[8] National Competition Council 2004, Annual Report 2003–2004, AusInfo, Canberra, p 45

1999-00 - $53.5 M
2000-01 - $35.9 M
2001-02 - $55.7 M
2002-03 - $56.1 M
2003-04 - $57.1 M

A further $58.1 M in 2004-05 and $59.8 M in 2005-06 is to be allocated to South Australia, unless the NCC rules otherwise. To date the competition penalties applied to South Australia are as follows;

2003-04 - $17.57 M
2004-05 - $11.9 M
2005-06 - $8 -10 M (estimated)[9]

National competition payments are the State's share in the dividends flowing from making markets more efficient and competitive, the funds are used for education, health, roads and other areas determined by the State and Territory Governments, and have never been tied to a purpose dictated by the Commonwealth. It was of concern therefore to the Committee that the penalties listed above are such a significant amount. Indeed, the potential to impact positively on the State Government's capacity to invest in the infrastructure and public service needs of the State is diminished by not accessing the full amount of competition payments available to the State.

6 INQUIRY FINDINGS

6.1 Written Submissions

The inquiry received written submissions from various organisations during the conduct of the inquiry. The written submissions assisted the Committee in reaching its final recommendations.

All of the written correspondence and tabled evidence is provided in Section 8 ('Attachments') of this report.

6.2 Hearings

This inquiry took evidence from the Executive Director of the Milk Vendors Association, an individual Milk Vendor and the Director, of the National Competition Policy Implementation Unit, during Committee Hearings.

Whilst the number of witnesses to appear before the Committee was comparatively low in terms of numbers, in conjunction with the written submissions (of which a synopsis is provided in 'The Deliberation of the Evidence' section of this chapter) their evidence confirmed the views of the Committee and assisted it in reaching its final recommendations.

[9] Rod Williams, National Competition Policy Implementation Unit, Department of the Premier and Cabinet, PowerPoint Presentation, Economic and Finance Committee Meeting, Kingston Room, Old Parliament House, Adelaide, Wednesday 25 May 2005.

1 December 2004 – Mr. Roger Prime, Executive Officer, Milk Vendors Association and Ms. Marilyn Hidvegi, Milk Vendor, National Foods.

At the outset Mr. Prime informed the Committee of three significant changes post industry deregulation (1 January 1995), which had impacted negatively on the milk distribution industry here in South Australia. One, processing companies chose to vary conditions and pricing unilaterally and Mr. Prime argued this meant.

> *They were able to transfer supermarkets, buying groups and large volume stores* [...] *and in doing so took 20 per cent of the margin of the vendor right off the top [...]. And that is still happening today: the larger stores are even now taken across to processor* [...] *and the vendor loses 20 per cent of his margin. Of course, he then loses business equity because his gross profit is not there as well.* (Hansard, 1 December 2004 p 2)

Two, milk rounds had been sold for between 150 and 200 times the average weekly gross profit, in the late 1980s. However by 1999, it had dropped to between 80 and 85 times average weekly gross profit on account of the major supermarket chains moving to a different distribution method. Mr. Prime suggested that by June 2005 if distribution to supermarkets is no longer through the milk vendor, 50 per cent of vendors in the State will be totally unviable. (Hansard, 1 December 2004 p 3)

Three, Mr. Prime raised concerns about the future contractual negotiations with National Foods, which it was suggested opposed the concept of milk vendor collective bargaining arrangements, an implication being that vendors would compete with other vendors for business, and it might be business that he (the vendor) already holds. (Hansard, 1 December 2004 p 4)

After an overview presentation of these changes, a question and answer session took place between Mr. Prime and Committee members. This session assisted the Committee in understanding more fully what was occurring in the milk distribution industry and it helped to draw out a proposal from the Milk Vendors Association for an industry rationalisation package as a means of overcoming these recent negative impacts on milk vendors.

> The Hon. I.F. Evans: *So, what we are really talking about is a claim about abuse of market power?*
>
> Mr. Prime: *Yes.*
>
> The Hon. I.F. Evans: *I assume the Milk Vendors Association or their agents have gone to the National Competition Council [...] and [...] what was their response?*
>
> Mr. Prime: *We have been down that path and [...]. our advice is that the facilitation of what Woolworths and Coles are doing by the processing company is a misuse of market power*
>
> The Hon. I.F. Evans: *Given that it is an abuse of market power circumstance, what do you want the state parliament to do? What exactly are you asking the committee to consider?*

Mr. Prime: *We are asking the committee to look into the situation* [...] *which would enable our members who wish to exit the industry to do so with some funding, to be able to go and do something else with their lives, not lose their home etc., and to rationalise our industry so that we may not go down that way.*

The Hon. I.F. Evans: *Have you come up with a model and a costing?*

Mr. Prime: *In our closest estimate between $9 million and $13 million.*

The Hon. I.F. Evans: *Over what period of time?*

Mr. Prime: *Over four years.*

The Hon. I.F. Evans: *How would that be funded?*

Mr. Prime: *It would be funded by those vendors remaining in the industry buying portions of the businesses of the vendors leaving the industry and/or getting new members coming in to the industry. We have said that 66 per cent would be retained by the vendor purchasing the business, and 33 per cent would go back into the fund until the fund is repaid.* (Hansard, 1 December 2004 p 7-8)

At this point in the hearing, Ms Hidvegi, as an individual milk vendor, endorsed the Milk Vendors Association rationalisation package proposal but from her perspective more funding than this would be required.

Ms Hidvegi: *That will not cover a loss of some $15 million worth of business that will be lost by supermarkets, so I do not like that scenario. I would rather see compensation for the supermarkets to the tune of $15 million, which is a big proportion, over 50 per cent of our business.*

The Hon. I.F. Evans: *So that we are clear, Marilyn - the $9 million to 13 million over four years does not cover the loss of business for supermarket trade?*

Ms Hidvegi: *We would need at least $24 million - $37 million altogether, I believe - and $12 million would come from vendors buying other rounds. So, $24 million would be required to cover it.*

In terms of the current contractual and regulatory arrangements vis-à-vis the impacts of national competition policy the Committee heard the following responses from Mr. Prime in various exchanges with Committee members - beginning with his response to the Presiding Member when she asked what process enables the existence of milk vendors.

Mr. Prime: *[...] It is very simple: you go to the Dairy Authority to obtain a licence which, at this stage, is only $20.*

The Presiding Member: *Woolies could get a licence to carry milk [...] So, the impact of national competition policy comes in when saying that a licence to carry milk should not be limited to a particular group of people, is it?*

Mr. Prime: *That is exactly right.*

The Presiding Member: *Effectively, is your argument that a particular licensing system was established to meet the historical needs in relation to the distribution of milk - to provide a service to the community and to make an important product safely distributed - and that many things have marched on, including the availability of refrigerated vans, etc., so that in a way milk vendors are an historical service? If you were looking at it today on a greenfields basis, there would be no need for milk vendors. However, given that the milk vendor industry provided this important service, and people bought their business on good faith, it should be treated similarly to prawn fishers, for instance.*

Mr. Prime: *Absolutely* [...] *I think there are some alignments, because our distribution sector is saying exactly the same thing. We believe that we have to rationalise our industry, otherwise it will not be 50 per cent going under, it might be 75 per cent. If a lot of those people who are not viable move from the industry, and are able to gain some compensation for doing so, they would be able to on sell their business to somebody remaining in the industry who may not be viable but would be if they were able to purchase extra business.* (Hansard, 1 December 2004 p 9-11)

Mr Hamilton-Smith: *Correct me if I am wrong, Mr Prime, but your argument seems to be that you are not so much the direct victims of deregulation and national competition policy but indirectly in that the big retailers and the big producers have grown so big that they are using their market power to cut you out of the market. Is that right?*

Mr. Prime: *It has been a slow, creeping process since deregulation.*

Mr Hamilton-Smith: [...] *So, isn't your argument* [...] *federal money that has been given to the state government over the last 10 years should have been used to ameliorate this effect that the national competition policy has had on your industry?* [...] *and you point to packages* [...] *provided by three other states.* (Hansard, 1 December 2004 p 12-15)

Mr. Prime: *That is right.*

In terms of deregulation and NCP, Ms Hidvegi added the following comments.

Ms Hidvegi: *Deregulation gave the processors the power to do what they have done. If deregulation had not been introduced - if the NCP had not been introduced - none of this would be here today. As far as the restructuring of the industry is concerned, it is only the processors moving the profit. As far as the industry is concerned, we would be quite a strong business had it not been for deregulation and the NCP payments, because that would not have given the processors the power to manipulate the system, and that is exactly what they have done. [...]*

The Committee also heard that competition payments have gone to help the dairy farmers rather than the milk vendors.

Mr. Prime: *Yes, that is right. They were given $1.68 billion to rationalise their side of the industry. They have since got another $272 million to continue with that rationalisation (federal money), and that is funded by an 11 cent per litre levy on milk throughout Australia, which we collect for the industry.* (Hansard, 1 December 2004 p 19)

25 May 2005, Mr. Rod Williams, Director, National Competition Policy Implementation Unit, Department of the Premier and Cabinet:

At the outset of this hearing Mr. Williams provided the Committee with an overview of NCP, a summary of which is described in Section Five of this report. Below is some more extensive coverage of the pertinent exchanges between Mr. Williams and the Committee members to compliment the summary above. As stated by Mr. Williams the State Government's obligation under NCP was:

> Mr. Williams [...] *reviewing legislation that contained restrictions on competition and that was to remove these, but a couple of tests were done. The restrictions could be retained if there was no alternative to legislation. So, the first task was to identify what the restrictions were and then to see whether there were any alternatives to legislation. In some cases codes of practice were feasible, but in a number of cases the legislative arrangements were put in place to deal with particular problems, and voluntary arrangements do not always fix them.*
>
> *The second test (and this is probably the one that has caused the biggest difficulty) was that the restrictions had to be removed if the cost of the restrictions exceeded any wider public benefits. In looking at this, there needed to be consideration not simply of the benefits to the parties that might be advantaged by the legislation but also the benefits that might exist for the wider community. [...] This really was the area of the greatest difficulty.* (Hansard, 25 May 2005, p 25)

In terms of the processes and experiences of the National Competition Policy Implementation Unit, Mr. Williams pointed out that when the process started:

> Mr. Williams: *We were obliged to provide a schedule of the legislation to be reviewed and this had to be done within four years. The reality is that we listed 178 acts. In hindsight, my view is that probably about 29 - perhaps more - of those were major pieces of legislation to be looked at; the rest were minor. So, in a sense, a lot of work and effort was undertaken for reviewing a lot of legislation that was retained unchanged.* [...] *One of the difficulties we experienced was that generally there was much greater emphasis given to economic factors as distinct from non economic factors. So, for example, social welfare and equity issues was one area where the South Australian government had some difficulties with the NCC in getting agreement on the way in which we assess things such as gambling legislation.* [...] *The deadline of four years to do this was extended for a further 18 months and there was provision for a transition period beyond 2000 if this was justified by public interest reasons. I think the experience and the hindsight on this is that, given the nature of the work and the difficulties with some of the reviews, this was quite an optimistic timetable.* (Hansard, 25 May 2005, p 26)

In addition Mr Williams pointed out the definitional difficulties when he stated:

> Mr. Williams: *One of the issues dealt with at one of the COAG meetings in November 2000 was an issue that the states had with the NCC that the NCC was arguing that, where there was a range of options when one looked at legislation, if one had to review it one had to choose the option that provided the greatest net public benefit. The argument the states put, which was eventually agreed to, was that providing an option provided a net public benefit, and the state could choose whichever one it preferred. This is certainly relevant in an area such as barley marketing where the NCC, for example, would argue that complete removal of the single desk was likely to provide a greater net public benefit and that should be chosen; whereas, if there were other alternatives which were available which did provide a net benefit - and the Western Australian arrangement is an example of something which put in a limited choice for barley growers - the NCC's argument would be that the complete removal was preferred* (Hansard, 25 May 2005, p 27)

At this point in the hearing Committee members became engaged in a rather robust question and answer session with Mr. Williams, with the key points highlighted below, beginning with a question from Mr. Rau, the Member for Enfield,

> Mr. Rau: *Can I say on that particular point, in regard to the application of the test - take the single desk - the ruler is run over the single desk by the characters who dictated the policy. They say the single desk is unsatisfactory because it is a restriction on trade or competition or whatever. You then have a review and, in the review, those factors that you threw up there (including, for example, the factor that the overwhelming number of people involved in the industry themselves thought that the current arrangements were superior to the proposed market arrangements) were thrown into the balance and dismissed in a sentence in the review in terms of, 'These are anecdotal things and it is very hard to manage and assess them so let's, in effect, ignore them.'* [...] (Hansard, 25 May 2005, p 27)

Mr. Williams replied:

> Mr. Williams: *Well, I think that has certainly been the experience here in South Australia, and I think part of the problem has come from the resources that will need to be put into those to undertake a review of the nature and extent that would be needed to demonstrate those. The economic issues tend to be much easier to identify and assess, particularly in terms of dollar value. In regard to the other factors, if you look at barley, for example, if you are arguing that there is a benefit because of the spin off benefit for regional areas, it is much more difficult to demonstrate the link and also to be able to quantify that, whether you do that in dollar terms or other terms.* [...]. *I think one of the difficulties with this is that the focus has often been on the economic factors and, if you do that without taking into account the non economic factors, the risk is that you may come to a conclusion that there is insufficient benefit to justify a restriction. If that is what has happened, the issue is the process of review is perhaps flawed or incomplete.* (Hansard, 25 May 2005, p 27)

On implementation of review difficulties, Mr. Williams also offered some comment on the contentious issue of shop trading hours:

> Mr. Williams: *If we look at the area of shop trading hours, this is one of the areas where South Australia had some significant differences of opinion with the NCC, and in 2002 the NCC chose a rather novel way of dealing with it by refusing to make any assessment of South Australia's progress in implementing the reforms required under the agreements. The net effect of this was that there was a suspension of all South Australia's competition payments. There were two arguments. One, the community was clearly seeking greater flexibility in shop trading hours. The counter argument, of course, is the likely effect that will have on retailers who may be disadvantaged by that.* (Hansard, 25 May 2005, p 29)

When challenged by Mr. Rau, the Member for Enfield, on which part of the community was clearly seeking a revision of shop trading hours, Mr. Williams responded by suggesting:

> Mr. Williams: *I simply used that example as one where, if you like, there are competing demands. The people who can take advantage of those trading hours are the ones who would clearly see that as a benefit; whereas the retailers, particularly the smaller retailers, who would be disadvantaged by that would take a contrary view. [...]* (Hansard, 25 May 2005, p 29)

When asked by the Hon. G.M. Gunn, the Member for Stuart, about the prospect of big supermarkets putting pharmacies in the supermarkets, Mr. Williams informed the Committee:

> Mr. Williams: *If that were to occur, that would result from changes to the commonwealth legislation which controls pharmacies. The removal of the ownership restrictions for pharmacies would certainly enable people such as Woolworths to acquire them. The review that was undertaken on pharmacies made one point (and I think it was a good one); that is, it distinguished pharmacies from most of the other professions. A fair amount of pharmacists' business is in the resale of various goods, drugs and other things. [...] Even before this issue of supermarkets came up, there was concern about the prospect of removing the ownership restriction on pharmacy and having pharmacy wholesalers buying chains. There has also been a longstanding concern about the wholesale chains providing finance to pharmacists to buy into businesses. So, the problems that came from ownership in an area like that were perhaps much higher than they were in the other professions.* [...] *There is a risk that if the ownership restrictions were removed, clearly other parties could acquire ownership.* (Hansard, 25 May 2005, p 29)

Another contentious issue was in relation to the public benefit test and the example of gambling was used. The Committee heard the following exchange:

> Mr. Williams: [...] *The NCC's argument has been that our licensing arrangements for lotteries, the casino and the other arrangements limiting gambling are anti competitive because they exclude people from the industry and they limit the number of gambling opportunities.*

Mr. Rau: *That just says it all, doesn't it? That's how clever these people are.*

Mr. Williams: *I am just giving you the position. Let me give you the reason why. The Productivity Commission did a review of gambling in, I think, 1999 as well. They came to the conclusion that gambling was a normal Australian recreational activity but they conceded that there were some difficulties with problem gamblers. My reading of the reports that have been done in South Australia and the parliamentary debates is that in South Australia generally the position has been taken that gambling intrinsically is an activity - I do not like to use the word 'evil' but certainly it is not necessarily seen to be a desirable activity for the community. However, recognising that a number of people will engage in it, the legislation has reluctantly conceded that it should permit it. These are fundamentally different views between what the Productivity Commission said, which the NCC picked up on, and what the South Australian government has been arguing consistently with its approach to gambling legislation. The reality has been that in the period from about 2002 ... the issue of problem gambling came to the fore. So, the NCC has backed off on its view and accepted the South Australia position because of the amount of published material that is available that demonstrated the nature and extent of problem gambling. It is certainly an issue that has been debated here pretty widely, but I think what that public debate demonstrated then was strong support for the view that South Australia is taking.*

At this point in proceedings the issue of community benefit became the focus of Committee members with Mr. Rau, the Member for Enfield questioning;

Mr. Rau: *[...] Where is the role for the community; where is the role for the people whom I and Mr. Gunn represent in our constituencies? The barley thing seems to be a classic example of where what you have described as self evident is transparently not self evident.*

To which Mr. Williams replied

Mr. Williams: *Some of the issues that you raise I suspect are probably beyond my brief to be able to respond to, because some of these things are quite right. My purpose here today is to try to explain to you the nature of the test that has been applied and the way that it has been applied. I do not see it as my position to debate some of these things with you.* (Hansard, 25 May 2005, p 31)

Pressed on this matter by the Hon P.L. White, the Member for Taylor, for a view on what exactly the State Government should do if the NCC takes a view there is a financial penalty to the state, Mr. Williams responded.

Mr. Williams: [...] *In terms of that, one of the difficulties we have had with all of this has partly been the time process, that there has been a limited amount of time to look at issues, and if we go back to have a look at say something like barley, if that had been looked at fairly early in the piece, it is quite feasible that the time that was available would have allowed a better consideration of this and certainly in terms of arguing the reasons for retaining the single export desk would have been much easier.*

One of the difficulties we have had with the NCC is that the pace in which these reviews were done, the NCC came to the conclusion by 2000-2001 that South Australia was dragging its heels and so therefore it was pressing for the change in a number of areas. It also looked at what some of the other jurisdictions had done and had come to the conclusion that if they had done it, South Australia should do it as well. So the difficulty we have had is that with a lot of these reviews they have been, while some of them are done by 2000, a lot of them were not completed until much later than that. So we have been in the position of having done reviews, not announced what the government's position is going to be, and then having the NCC draw the conclusion that we were dragging our heels, we did not want to put reforms in place where some of those reviews had recommended reforms. (Hansard, 25 May 2005, p 32)

In a further exchange between Committee members and Mr. Williams the rationale behind competition payments was explained:

Mr. Hamilton-Smith (the Member for Waite): *I am asking him to clarify what the payments are for.*

Mr. Rau: *In theory, as I understand it, these payments are based on the fiction that, because these reforms are introduced, the economy suddenly becomes productive to the tune of X per cent, which means increased government revenue is collected by the commonwealth on behalf of the community, because there is a measurable and notional amount of increased activity, which is then shared back to the states; and that is their dividend.*

Mr. Hamilton-Smith: *It was also envisaged there would be some restructuring costs to certain industries. Were the payments not perceived to be partly used to offset those restructuring consequences?*

Mr. Williams: *The short answer to that question is no. The payments were certainly intended to share the productivity gains and, to an extent, pick up on losses of revenue under government business enterprises, which would become subject to taxation. [..] In terms of providing compensation, that is always a separate issue. Certainly, the competition payments were never intended to be used for compensation. There have been some instances where other governments have made payments, but my understanding is that is in the nature of ex gratia payments to deal with specific issues. In terms of [...] milk vendors, in considering that difficulty there would be the length between the difficulties they are facing and whether in fact it was a consequence of any reform of legislation required under this process. The difficulty is separating out general structural change within various sectors from that which is caused directly by this. They are not the only ones that have run that argument. I think the length is more tenuous.* (Hansard, 25 May 2005, p 39-40)

6.3 Deliberation on the Evidence

It is the view of the Committee that notwithstanding the benefits of recent microeconomic reforms and increased competition, Australia has, in many ways, become a less competitive retailing market than before NCP. Committee Members are concerned that retailing is being concentrated in the hands of a few larger companies while small businesses such as milk vendors, grocers, butchers, bakers, florists, greengrocers, pharmacists, newsagents and liquor stores are the ones who feel the strain and continue to be vulnerable entities.

The Committee was particularly concerned to hear evidence from the South Australian Milk Vendors Association that should distribution to supermarkets no longer be done through the milk vendor, a scenario that appears would best suit the needs of the larger supermarket chains and milk processing companies, then something like 50 per cent of vendors in this State would become totally unviable.

The Committee notes the difficulty in separating out general structural change within various sectors from that which is caused directly by NCP but nonetheless a major problem is that, whilst the benefits of NCP are generally longer-term and spread more widely amongst the community, the costs of change are often concentrated in a particular area and borne immediately, such as is the case with Milk Vendors, who argue they are being out muscled by the bigger supermarket and milk processing companies.

The Committee notes that it is ultimately how society compensates and supports those affected by NCP reforms which are the key issues yet to be satisfactorily resolved. Moreover, the mere fact that some States have the financial resources to fund milk vendor industry rationalisation packages and others do not is symptomatic of a flawed system. Certainly, the Committee was sympathetic to the views expressed by the Milk Vendors when they argued (on equity grounds) that three other States had provided industry rationalisation packages as a means of overcoming the negative impacts NCP had brought to the milk vendor industry.

This is especially the case when one considers that $1.68 billion of Federal Government money has been spent rationalising the wider dairy industry and currently an 11 cent per litre levy on milk is being collected throughout Australia towards further industry restructuring, yet milk vendors have been left out of any Federal rationalisation process.

The Committee further notes that it is not just milk vendors who are perplexed by the vagaries of NCP and/or industry rationalisation polices of the Federal Government. In written submissions to this Committee three very disparate industry groups all expressed similar angst regarding the imposition of the top-down driven policy imposition that is NCP.

For example correspondence from Mr John Lewis, General Manager of the Australian Hotels Association, SA Branch (AHASA), which included two specially commissioned reports for the AHASA, all took issue with the April 2003 Draft National Competition Review Report's finding that the restrictions on retail liquor licenses imposed under Sections 58 & 61 were anti-competitive. The view of the AHASA is that these sections have little practical impact on the degree of competition in the South Australian packaged liquor market.

The AHASA cites consumer surveys indicating a well informed market, evidence of price flexibility, consumer preferences as to how and where they purchase liquor and retail responsiveness to consumer demand and convenience. Furthermore, the AHASA advocates the current entry restrictions as a "light handed regulation" that acknowledges the product's potential social harm by preventing unlimited numbers of retailers into the market. It further asserts that competition in the industry is currently robust and unlimited entries could ultimately have anti-competitive results.

The AHASA commissioned independent reports also and these contained a survey document that assesses alcohol purchasing patterns amongst consumers, included findings that suggest:

- Proximity is an important element in purchasing patterns and loyalty to outlets;
- Some concern as to the availability of alcohol in supermarkets but a large majority indicating they would purchase alcohol in supermarkets if it was available;
- A general lack of concern regarding a decrease in the number of take away alcohol outlets;
- A perception that bottle shops would be more convenient than supermarkets.[10]

Intuitively, these findings and the views expressed by the AHASA should be taken into account by the NCC when making its rulings but it appears the NCP process is not an overly consultative one.

The South Australian Farmers Federation (SAFF) also provided a submission to the Committee. The essence of their submission was that the "public interest test" outlined in the April 2004 Productivity Commission Issues Paper is not applied to the rural sector in relation to NCP and it should be. The submission argues that a rigid application of competition rules fails to appreciate the specific and significant issues faced by rural producers, especially in a small market such as Australia, and especially South Australia.

SAFF go as far as to state that the effect of such inflexible applications of policy is essentially anti-competitive as concentration occurs and duopolies, or monopolies, result with both consumers and producers losing.[11]

The South Australian Pharmacy Guild (The Guild) is similarly critical of the rigidity with which NCP is enforced. The Guild believes a community benefit is derived from pharmacies being owned by pharmacists, a view also held by Federal and State Governments. The NCC opposes restrictions imposed by the SA Pharmacy Act limiting the number of pharmacies owned by individual pharmacists or friendly societies. The Guild supports the limitations and if any increases are to be allowed they should be minimal and reflect limitations in other states. The Guild is in favour of harmonising Pharmacy Acts across all states.

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[10] See Dr Dawes and Jonathan Hill, Marketing Science Centre, University of South Australia, "Australian Hotels Association Market Survey of Liquor Purchasing", Report No 2069301, September 2003 and the paper by Professor David Round and Dr John Dawes, entitled "An Economic Assessment of the Implications for Competition of the restrictions imposed by Sections 58 and 61 of the Liquor Licensing Act 1997", September 2003

[11] National Competition Policy Submission, The South Australian Farmers Federation, 9 July 2004.

The Guild opposes corporate chains operating pharmacies. The Guild believes the current community approach, mediated through the Guild, allows pharmacies to operate as a first line of the health system where corporate chains would not because of their purely financial imperatives. Corporate chains it is claimed would further disrupt the distribution system and place unbearable pressure on independent and rural pharmacies by bypassing wholesalers and buying direct from manufacturers.[12]

These submissions and the evidence provided to the Committee that arduous reviews of legislation with minimal competition impacts had taken up too much time, effort and administrative resources of the State Government with no real tangible benefits to show for such effort, was sufficient to confirm the suspicions of Committee members that the lack of consultation with industry groups by the NCC was a major concern.

A concern also for the Committee is that irrespective of whether the reviews or industry groups such as Milk Vendors, Pharmacists, Hoteliers and Farmers to name but a few, question the worth of increased competition or further deregulation, without competition reforms the State can seemingly be held to ransom and penalised a significant amount of money by way of competition penalty payments. For example, the Committee was alarmed that the State would forgo $3 million in competition payment allocations due to a 'perceived' lack of progress on deregulating barley marketing.

It was the considered view of the Committee that the push for deregulation of barley marketing overlooked the fact that much of the South Australian grains industry was a networked industry and despite recent commercialisation and privatisation of once publicly owned assets in the industry (eg ports, storage and handling and railways) it still operated as a set of connections built for the benefit of those connected, and by their nature they were still cooperative constructs which actually allowed them to obtain more of a scarce resource than they could obtain on their own through competitive interaction.

Moreover, as a major Transport SA policy discussion paper had recently confirmed the permanent nature of grains industry assets in South Australia often dictated that investment was on a long-term basis and generally required some cooperation and certainty about future operations. Thus the potential for capital exposure is high, should operations not be sustained. For example, the privately owned grain rail network on Eyre Peninsula covers large distances (670km of track), has low freight volume (0.7m to 1.2m tonnes p.a.), is self-contained and is dependent on one seasonal commodity (grain) for its long-term viability. This leaves rail operations on Eyre Peninsula highly exposed to the continued co-operation of producers, handlers and marketers of grain.[13]

The Committee also considers that the evidence presented to it by the coordinator of the National Competition Policy Implementation Unit here in South Australia, Mr. Rod Williams, whilst informative and illustrative merely highlighted the need for the State Government to be more proactive and to help steer a middle course between the excessive reliance on regulation that characterised industry policy for much of the post-war period and the naive faith in competition that motivates NCP.

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[12] National Competition Policy Submission, The Pharmacy Guild of Australia (S.A. Branch), 20 July 2004.
[13] Transport SA, Policy and Strategy Issues Paper: *Eyre Peninsula Grain Transport*, August 2002, p 15.

It is the view of the Committee therefore that it is critically important to recognise the possibility of a market solution, without assuming that market solutions will always be optimal. Furthermore, as the discussions above illustrate one critical aspect of the top-down nature of NCP is its lack of consultation. In the past, policies affecting particular sectors of the economy were normally formulated in consultation with the groups most directly concerned, including producers, workers and consumer organisations – such as Milk Vendors, sometimes collectively described as 'stakeholders'. However NCP has been undertaken in a way that precludes significant consultation and the Committee is of the view that the reforms involve a misunderstanding of the nature and role of competition in the economy. There is a danger that issues such as equity and industry sustainability are being neglected.

Approaches based on the dominance of a single objective such as the promotion of competition, must be rejected. Both the content of the NCP reforms and the nature of the reform process raise issues of concern for all members of the Committee. NCP fundamentally affects all aspects of South Australian life as indicated by the fact some 178 State Parliamentary Acts have been earmarked for review. As the Committee heard during hearings the arduous process and time, resource and experience limitations have hampered bureaucratic processes and by implication assisted to avoid public accountability.

A number of policy recommendations are put forward accordingly. First, the use of financial penalties to compel state governments to comply with the agreement is undemocratic and should be abandoned. The imposition of an agreement under which a national agency superintends a comprehensive review of all state legislation, and recommends the imposition of financial penalties if it is dissatisfied with the results, is inconsistent with the right of citizens of the Australian states to democratic self-government and should be renegotiated to remove the element of compulsion.

It is the view of this Committee that the NCC no longer be required to carry out legislative reviews; and that Governments, through CoAG, undertake to agree broad systems and processes for reviews, including mechanisms for proper consideration of the submissions and views of any and all interested parties. It is the view also of this Committee that other governments be provided the opportunity for input to each other's reviews as a way to contribute to impartial outcomes based on a national rather than state or regional perspective.

7 RECOMMENDATIONS

The Committee recommends that the Treasurer consider:

- **Proposing at the next CoAG Meeting that the use of financial penalties to compel state governments to comply with NCP is an abuse of Federal financial power and should be renegotiated to remove the element of compulsion.**

- **Proposing at the next CoAG Meeting that the NCC no longer be required to carry out legislative reviews; and that State Governments, through CoAG, undertake to agree broad systems and processes for reviews, including mechanisms for proper consideration of the submissions and views of any and all interested parties.**

- **That the effective presumption that the status quo is wrong arising from current NCP principles be reversed to put the onus on the advocates of change to make out their case.**

Gay Thompson

Gay Thompson MP
PRESIDING MEMBER
ECONOMIC AND FINANCE COMMITTEE

22/9/2005

8 ATTACHMENTS

8.1 Written submissions

- Correspondence from Mr John Lewis, General Manager, Australian Hotels Association, SA Branch, 29 June 2004 - including attachments of recent reports commission by the Australian Hotels Association:
    - A copy of a marketing survey report conducted by Dr Dawes and Jonathan Hill, Marketing Science Centre, University of South Australia, "Australian Hotels Association Market Survey of Liquor Purchasing", Report No 2069301, September 2003
    - A paper written by Professor David Round and Dr John Dawes, entitled "An Economic Assessment of the Implications for Competition of the restrictions imposed by Sections 58 and 61 of the Liquor Licensing Act 1997", September 2003

- National Competition Policy Submission, The South Australian Farmers Federation, 9 July 2004.

- National Competition Policy Submission, The Pharmacy Guild of Australia (S.A. Branch), 20 July 2004.

- National Competition Policy Submission, Milk Vendors Association S.A. Inc, 1 December 2004.

- National Competition Policy, Economic & Finance Committee Briefing, Rod Williams, Director, National Competition Policy Implementation Unit, Department of Premier & Cabinet, 25 May 2005