

Further information regarding National Competition Policy and local government is available in the following reports:

Impact of Competition Policy Reforms on Rural and Regional Australia

<http://www.pc.gov.au/inquiry/compol/finalreport/index.html>

Senate Select Committee on the Socio-Economic Consequences of The National Competition Policy - Riding the Waves of Change

http://www.aph.gov.au/senate/committee/ncp_ctte/final/index.htm

The National Competition Council has produced a series of Community Information Papers that relate to competition reforms in specific industries.

National Competition Council's Community Information Papers currently available are as follows:

- Reforming the Professions
- Reform of the Legal Professions
- Reform of the Health Care Professions
- Securing the Future of Australian Agriculture: An Overview
- Securing the Future of Australian Agriculture: Barley
- Securing the Future of Australian Agriculture: Sugar
- National Competition Policy: An Overview
- Urban Water Reform
- Rural Water Reform
- Shop Trading Hours
- Improving our Taxes
- Road Transport Reform
- Local Government and National Competition Policy

Should you wish to receive copies of these papers, please call (03) 9285 7474 or email info@ncc.gov.au

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LOCAL GOVERNMENT AND NATIONAL COMPETITION POLICY

National Competition Council
Community Information
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In 1995, the Commonwealth, State and Territory governments agreed to implement a package of legislative and administrative reforms known as National Competition Policy.

National Competition Policy aims to promote effective competition in situations where it will enhance community welfare.

Across Australia local government authorities administer legislation and deliver services which have a marked impact on state economies, businesses and consumers. As such, reform at the local level is an important part of the competition policy process.

WHAT IS COMPETITION? & WHY DO WE NEED IT?

Between 1960 and 1992 Australia went from being the world's third richest developed country to being only the fifteenth. Our declining economic performance was largely due to the protection from competition of large sectors of the economy.

Without the disciplines imposed by competitive markets, businesses had little incentive to reduce costs and prices, produce new innovative products or use resources as efficiently as possible.

Competition is about choice, the freedom for consumers to choose between products and suppliers. When consumers have a choice between businesses offering similar products, prices tend to fall and quality improves.

National Competition Policy is a national package of market and economic reforms designed to stimulate growth and job creation.

The Productivity Commission estimates that in the five years since the inception of National Competition Policy it has provided a sustained increase in output from the Australian economy of 2.5% above what would have otherwise occurred in the absence of the reforms.

NATIONAL COMPETITION POLICY - IN A NUTSHELL

Broadly, the National Competition Policy reforms can be outlined as follows;

1. The extension of Trade Practices laws prohibiting anti-competitive activities (such as the abuse of market power and market-fixing) to all businesses, including government businesses.
2. The introduction of 'competitive neutrality' so that privately-owned businesses can compete on an equal footing with those owned by Government.
3. The review and reform of all laws that restrict competition.
4. The development of a national access regime to enable competing businesses to use nationally significant infrastructure.
5. Price monitoring for all significant government businesses that have a market monopoly (ie. Australia Post).
6. Specific reforms to the gas, electricity, water and road transport industries.

ENABLING FAIR COMPETITION

To enable fair competition between local government and private sector businesses, any advantages or disadvantages that the government businesses may experience, simply as a result of government ownership, must be neutralized. This is called 'competitive neutrality'.

Local governments conduct business activities ranging from the operation of recreation centres to the sale of photocopies. However, National Competition Policy only requires that competitive neutrality be introduced for 'significant' government businesses and, where the benefits of competitive neutrality outweigh the costs.

Whether a business is deemed to be significant or not depends on the size of the business and its importance in the particular market. Each State and Territory classifies significant businesses differently.

Competitive neutrality does not apply to the non-business, non-profit activities of government businesses. Nor does it extend to factors which are independent of ownership such as business size, skills or location.

INTRODUCING COMPETITION TO LOCAL SERVICES

Local governments are often providers of monopoly services such as water, sewerage and garbage collection.

Before introducing competition to a monopoly market it is important for local governments to:

- Separate the regulatory functions from the commercial activities of the business
For example, if a monopoly water supply business is responsible for developing regulation standards, then responsibility for those standards should be relocated or at least be subject to some other regulatory oversight.
- Review the business' structure to ensure that it can operate in a competitive environment
For example, if a government owned swimming centre is to compete effectively it cannot be subject to more onerous requirements than private swimming centres. For instance, it will need the freedom to make day to day business decisions and not need to rely on those decisions being made through the council process.

These issues are equally important when government owned businesses are to be privatised.





CHILDCARE: A COMPETITIVE NEUTRALITY CASE STUDY

A municipality has three childcare centres. One is run by the Council, and the other two centres are privately operated.

The Council childcare centre shares a building with the infant health centre. A National Competition Policy competitive neutrality review of childcare in the municipality examined both pricing and public interest issues. The review established that the Council centre had competitive advantages (it did not have to pay rates or land tax) but also that the childcare centre paid the electricity bill for the infant health centre from its local government ownership.

The review found that the price charged for childcare was ten per cent lower than the full cost of providing the service. It also found that there would be overall benefits from applying competitive neutrality principles.

The benefits included fairer competition between providers (and potential providers), the removal of a hidden subsidy to childcare users from ratepayers and, more transparent financial reporting by Council.

Therefore it was decided that competitive neutrality should be introduced by removing the advantages and disadvantages experienced by the Council's childcare centre. The childcare centre was to set prices as if it paid rates and land tax and the Council was to pay the electricity bill for the infant health centre.

Public interest considerations indicated that the Council wished to continue to subsidise childcare for low income residents. In order to achieve competitive neutrality and meet this social objective, the Council could either pay a subsidy to all childcare providers (and any potential providers) in the city, or, pay a subsidy directly to low income residents that use the Council childcare centre. Details of the subsidy are included in the Council's budget.

...HOW DOES COMPETITIVE NEUTRALITY WORK?

Competitive neutrality requires that the prices charged by local government businesses should aim to recover the full costs of a business activity.

Full costs should include:

- The direct cost of providing the goods or services and an appropriate proportion of indirect costs
Government businesses can sometimes underestimate their costs and omit to include expenses such as rent, payroll and personnel;
- All relevant taxes or tax equivalents
Sometimes government businesses are not required to pay tax or pay rates on their government owned premises;
- A commercial level of interest payments
Government businesses can often receive financial advantages, like low interest loans, as a result of government guarantees;
- A commercial rate of return (over a reasonable period)
Government businesses have not always been required to make a profit;

Government businesses should also be required to comply with all relevant government regulations (sometimes government businesses are exempt from laws relating to things like environmental protection, planning and approval processes).

Competitive neutrality does not apply to the non-business, non-profit activities of government businesses.

ANTI-COMPETITIVE LEGISLATION

National Competition Policy requires governments to review all new and existing anti-competitive regulations to determine whether;

- the benefits of the restriction on competition outweigh the costs; and
- restricting competition is the only way to achieve the benefits.

In assessing the costs and benefits of restrictions, governments need to apply a 'public interest test' and consider relevant factors including social welfare and equity, regional development, the environment, employment and business development.

...ARE PERMIT / LICENCE REQUIREMENTS 'ANTI-COMPETITIVE'?

Some local government permit/licence requirements can have anti-competitive consequences.

National Competition Policy requires that, where it is in the public interest, permits should be issued to all applicants that satisfy eligibility criteria such as health, safety and amenity.

Permit requirements should not be used to unnecessarily limit the number of sellers in a market.

LEGISLATION REVIEW: A CASE STUDY

Hypothetica City Council had required businesses wishing to place advertising signs on roads or footpaths to acquire a permit.

The Council's local law had specified that before issuing a permit, it must take into account the size and construction of the sign, the proposed placement of the sign (so as not to obstruct pedestrians or vehicles), and whether the appropriate fee had been paid. Shops on main business streets were allowed to have signs but shops in other areas, like side streets or arcades, were not permitted to have signs.

After hearing submissions from shoppers, businesses, the road authority and resident groups, the Council's National Competition Policy legislation review panel was able to assess the costs and benefits of the law. It recommended:

- retention of the provisions relating to the size, construction and placement of signs as they ensured public safety and amenity and did not discriminate between sellers.
- retention of the permit fee to cover administration, and enforcement costs.
- repeal of the provisions that prevented some businesses from displaying signage. These provisions restricted competition by disadvantaging some businesses without providing a net public benefit.

...DEALING WITH COMPLAINTS

Local governments should establish procedures to deal with complaints from people who believe that they are not getting a fair deal when they compete with a local government business.

In most States and Territories, a complainant's first point of contact will be the local government business owner. If the matter cannot be resolved, there is a capacity for the complainant to refer the matter to the state government complaints body or the local government department.

All States and Territories now have competitive neutrality complaints units that report annually to the National Competition Council regarding the types of complaints received and how they were dealt with.

COMPETITION PAYMENTS

National Competition Policy requires that the Commonwealth Government make annual 'competition payments' to the States and Territories.

The payments recognise that the economic growth brought about by competition reforms provide tangible financial dividends to the Commonwealth through increased taxation revenue.

Satisfactory progress in implementing the National Competition Policy reforms is a prerequisite for payment because, without reform, there would be no increased financial dividends.

The National Competition Council undertakes regular progress assessments and makes recommendations to the Commonwealth Treasurer on the level of payments.

It is entirely up to each government as to how the payments are spent and allocated. Queensland, Western Australia and Victoria grant a portion of their competition payments to local governments as an incentive to implement reform.

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National Competition Policy does not require governments to reduce their commitment to social objectives.

COMMUNITY SERVICE OBLIGATIONS

National Competition Policy does not require governments to reduce their commitment to social objectives. However, it does have implications for the manner in which those social objectives are identified, delivered and funded.

In order to maintain fair competition it is important that 'non-commercial' activities provided by local government businesses are identified, appropriately costed and directly paid for by the local government. Under National Competition Policy these activities are called 'Community Service Obligations'.

The provision of low cost water to schools and hospitals is an example of a Community Service Obligation.

In the past, government businesses tended to fund these obligations by charging other users higher prices. Governments would then ensure that their businesses were not undercut by restricting the potential entry of competitors.

If a government introduces competition without clearly identifying and determining funding mechanisms for Community Service Obligations the costs imposed on the government owned business will be much higher than those imposed on private providers and it will not be able to compete with them.

Or the government business will receive a subsidy not available to its competitors.

Without transparency as to what is and isn't subsidised it is impossible to have fair competition between government and private businesses.

Therefore it is important to:

- clearly identify any Community Service Obligations;
- accurately measure the full cost of provision;
- decide upon an appropriate funding mechanism; and
- fully disclose Community Service Obligations in policy statements, legislation and financial reporting.

COMPETITIVE TENDERING AND CONTRACTING

Compulsory competitive tendering and contracting are not requirements of National Competition Policy. However, in recent years local governments have increasingly been moving from being a 'provider' to being a 'purchaser' and using contracting and outsourcing to ensure that they receive the best value for ratepayers money.

For the potential benefits of competitive tendering to be fully realised, it is important that competitive neutrality principles are properly applied.

If an in-house bidder enjoys a competitive advantage, simply by virtue of its ownership, it may win a tender despite being a less efficient supplier than its rivals. Alternatively, the in-house bidder may lose because it must meet Community Service Obligations that are not applicable to a privately owned competitor.

In both cases, a less efficient supplier may win and the community's resources will not be put to their best use.

National Competition Policy does not prevent councils from considering factors other than price in choosing between in-house and external provision.

These factors may include;

- the quality of the service provided and the ability to provide low cost ongoing maintenance
- the value to the local economy of keeping workers employed in the region
- the potential convenience of having people readily available to provide a service
- the effect awarding a major contract may have on competition in the particular market.

WHAT NATIONAL COMPETITION POLICY DOES NOT REQUIRE:

- asset sales and privatisation
- cutting the size of the public sector
- compulsory competitive tendering
- local government amalgamations
- contracting out
- reductions in welfare and social services

National Competition Policy has delivered a sustained increase of 2.5% in output from the Australian economy.

THE PUBLIC INTEREST TEST

When governments are reviewing laws that restrict competition National Competition Policy requires that they consider a number of factors to determine what is in the public interest. These include;

- Laws and policies relating to the environment
- Social welfare and equity
- Laws and policies relating to matters such as occupational health and safety, industrial relations, 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.
- The efficient allocation of resources.

The list is open-ended, meaning that governments must also take into account any other matter relevant to determining the merits of the reform being examined.

When Governments are reviewing laws that restrict competition they must consider a number of factors to determine what is in the public interest.

COMPETITIVE TENDERING & PUBLIC INTEREST: A CASE STUDY

Local governments should consider public interest factors other than price when determining the result of competitive tenders.

In a submission to a recent Productivity Commission inquiry, the Shire of Yarra Ranges explained how it had let a road maintenance tender for each of the two regions in the Shire.

The initial evaluation had awarded both contracts to an external bidder. The Shire then applied a 'public interest' test which considered the potential for lost skills and knowledge of the area – critical for emergency management and planning within the shire. As a result, the external bidder was awarded one region and the in-house team awarded the other.



WATER REFORM

ECONOMICS & ENVIRONMENT

In 1994, all State and Territory Governments agreed to significantly reform water management and regulation to ensure water is used sustainably and efficiently. The water reforms were absorbed as part of National Competition Policy in 1995.

The reforms require that all governments;

- Review water pricing methodologies to determine if it is cost effective to introduce 'two-part tariffs' (including a fixed service charge and a variable charge based on the amount of water used).

If this is the case and the 'two-part tariffs' are introduced then people only pay for the water they use and are encouraged to use water conservatively.

- Ensure that prices reflect the actual cost of providing water (this includes the cost of building and maintaining dams, pipelines, and other water infrastructure).

- Consult with communities in setting prices, service standards and sustainable water use objectives.

The success and impetus for change is very often dictated by the quality and emphasis governments place on community information, education and involvement.

- Conduct rigorous appraisal of economic viability and environmental sustainability prior to investing in new or existing water supply schemes and dam construction.

Economic and environmental considerations carry equal weight for pre-construction appraisals.

- Minimise conflicts of interest.
Bodies with responsibility for water resource management, standard setting and regulatory enforcement must be substantially separate from those with responsibility for water service provision.

- Improve drinking water quality.

USEFUL WEB SITES

National Competition Council
www.ncc.gov.au

Productivity Commission
www.pc.gov.au

Australian Competition and Consumer Commission
www.accc.gov.au

All States and Territories have a formal policy statement which sets out the application of competition principles to their local governments. Some government websites also give examples of past competitive neutrality complaints.

