

# NCP

National Competition Policy Implementation in Queensland

## National Competition Policy and Queensland Local Government



QUEENSLAND GOVERNMENT

A QUEENSLAND GOVERNMENT  
POLICY STATEMENT  
JULY 1996

National  
Competition  
Policy  
and  
Queensland  
Local  
Government

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POLICY STATEMENT  
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## ABBREVIATIONS

The following abbreviations are used in this statement:

<b>ACCC</b>	Australian Competition and Consumer Commission
<b>COAG</b>	Council of Australian Governments
<b>CPA</b>	Competition Principles Agreement
<b>DLGP</b>	Department of Local Government and Planning
<b>LGAQ</b>	Local Government Association of Queensland
<b>NCC</b>	National Competition Council
<b>NCP</b>	National Competition Policy
<b>PFEs</b>	Public Financial Enterprises
<b>PTEs</b>	Public Trading Enterprises
<b>SBA</b>	Significant Business Activity
<b>TPA</b>	<i>Trade Practices Act 1974</i>

## FOREWORD

The Queensland Government is committed to the implementation of the National Competition Policy (NCP) and is bound by a number of inter-governmental agreements to fulfil certain obligations.

This paper outlines the application of the elements of the Competition Principles Agreement to Queensland Local Government and is based on two issues papers prepared by the joint State/Local Government NCP Working Group and feedback from councils and other major stakeholders. In effect, a process of extensive consultation with stakeholders was used to test the proposed approach to the implementation of NCP.

The Government remains committed to genuine consultation, as illustrated by the continuation of the State/Local Government NCP Working Group. The working group will continue to advise and assist the Government in the development of the final statement of application and in the preparation of legislation to give effect to NCP and other related initiatives.

In addition, the Government will ensure individual councils continue to be consulted and appropriate assistance and support is provided as implementation occurs.

The Government is exploring the possibility of providing financial support to councils undertaking NCP reforms. This process involves examining access to “competition payments” for those local governments participating in the reform process. In this respect, Cabinet has agreed, in principle to allocating a proportion of the Commonwealth’s competition payments to the State to those councils undertaking competition reforms. Financial assistance in this regard would be incentive-based and linked to both the size of the councils’ business operations and, in particular, the extent of genuine competition reform undertaken.

In implementing NCP, the Government has applied the flexibility of the Competition Principles Agreement to take account of the unique circumstances of local government in Queensland.

The Government is seeking to minimise any negative regional economic development impacts, in particular on the viability of rural communities. Additionally, the Government is committed to ensuring the social obligations of smaller local governments are not jeopardised.

In keeping with the focus of NCP on Significant Business Activities (SBAs), the Government’s approach is to concentrate on those business activities where the reforms are likely to gain the most. In terms of competitive neutrality, thresholds have been established to clearly identify which business activities will be affected. Whilst the resultant significant business activities involve a relatively small percentage of councils, they target the bulk, if not all, of the major business activities of local government.

Smaller local government business activities participating in competitive markets will be encouraged to adopt a proposed Code of Competitive Conduct, which will be based on competitive neutrality principles. How such a code might operate will be the subject of another issues paper later in the year. Whilst the code will be voluntary, the Government is exploring the provision of financial support to those local governments which adopt competition reforms.

Action has also been taken to clearly apply the provisions of Part IV of the *Trade Practices Act* to all council business activities within the terms of the Act, irrespective of the size of the council.

Model local laws and local laws made by individual councils will be subject to the legislation review process stipulated in the Competition Principles Agreement, along with all State legislation relevant to the local government system. In addition, the Government is currently considering State prices oversight and third party access arrangements which could apply to relevant local government activities and services.

## EXECUTIVE SUMMARY

The National Competition Policy (NCP) is a set of policy reforms being adopted by Governments throughout Australia. The objective is to encourage a better use of the country's resources — and hence provide a higher standard of living — through increasing competition.

In the past, the lack of competition in key markets has contributed to inefficiencies within organisations. Competition generally leads to better, more efficient organisations, giving consumers lower prices, greater choice and higher quality services.

NCP targets the public sector and certain unincorporated businesses which have historically been protected from competition. However, NCP has not been developed as a policy of “competition for competition's sake”. Rather, the underlying tenet is that competition is generally desirable, unless it can be demonstrated, on a case-by-case basis, that it will not deliver socially beneficial outcomes. As a result, flexibility exists in relation to how certain key aspects of the policy will be implemented. In particular, many of the reforms are to be implemented only if it can be demonstrated that the benefits of the reforms outweigh the associated costs to the community as a whole.

NCP is to apply to local governments throughout Australia. However, implementation at this level is only to occur after extensive consultation between the local and State Governments in each jurisdiction. This paper is the result of an extensive consultation process, centering around the deliberations of a joint State/Local Government NCP Working Group.

The main proposals outlined in this paper relate to two of the key policy elements of NCP; namely “competitive neutrality” (*i.e.* the removing of advantages and disadvantages that Government-owned businesses derive from their public ownership) and “legislation review” (*i.e.* the review and, where necessary, reform of Government legislation which restricts competition).

Other elements of NCP will also apply to Queensland's councils. However, the impacts of these on councils are either: (i) likely to be less significant at this stage (*e.g.* the introduction of structural reform) or; (ii) subject to further clarification (*e.g.* the implementation of third party access and prices oversight regimes and national reforms of urban water industry arrangements). In relation to the second category, the State/Local Government NCP Working Group will address the possible impacts on local governments as further developments occur later this year.

An additional issue is that from 21 July 1996, any uncertainty regarding the applicability of Part IV of the *Trade Practices Act* (TPA) to Councils will be resolved and that subsequently this part of the TPA will apply. Councils are therefore encouraged to adopt TPA compliance programs.

In relation to competitive neutrality, reforms are to concentrate on the “significant” business activities of councils, and not the non-business and non-profit activities of councils, such as social and regulatory activities. Roadworks under a council's control are also generally to be exempt from these reforms.

On this basis, the statement proposes that certain business undertakings of the State's largest 17 councils (mainly water, sewerage and garbage services) be assessed by the relevant councils for possible corporatisation, commercialisation<sup>1</sup> or, at the very least, ensuring that the prices charged for these services reflect the true cost of provision. Under each option, there would be a requirement for prices to include a component to cover the advantages which, by virtue of their Government ownership, councils have traditionally enjoyed through exemption from taxation and other imposts.

However, this should not necessarily mean that the prices of those councils' goods and services would need to increase. Rather, councils would be able to continue to subsidise activities, but only if the subsidies are fully costed and publicly reported (to allow for scrutiny of the extent of such subsidies).

The identified business activities of these 17 councils account for a very high proportion of the overall local government business activities in Queensland.

For smaller council business activities which are in direct competition with the private sector, a voluntary Code of Competitive Conduct is proposed. If adopted by a council, the code would require the council to, amongst other things, consider pricing practices which take account of the full costs of providing the services.

The competitive neutrality reforms are only to be introduced upon the councils demonstrating (in publicly available documents) that the benefits of undertaking the reforms are likely to exceed any associated costs. The assessments of costs and benefits would take place next financial year, with reforms to be introduced from 1997–98.

In relation to legislation review, all State Government legislation that might provide for anti-competitive activities to be undertaken by local governments (including the *Local Government Act* and the *City of Brisbane Act*) is to be reviewed as part of the State's NCP examination of its own Acts and Regulations over the next three and a half years. For council local laws (many of which also have potential anti-competitive impacts), it is proposed that the councils themselves review these over a similar timeframe, but pursuant to a methodology consistent with that used by the State Government.

In the future, all new State legislation and council local laws (or amendments) which are potentially anti-competitive will also be subject to review.

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<sup>1</sup> Corporatisation is a reform process for Government businesses which focuses on improved commercial performance, while allowing the Government (council), as owner, to continue to provide the broad direction for the organisation (e.g. setting key performance targets and community service obligations). Although the Government (council) maintains ownership of the business, it is removed from the day-to-day management of the business; this, instead, is the responsibility of a separate legal entity — the "corporation" — which has its own board of directors (as happens in the private sector). Under commercialisation, management of the business activity remains within a Government department/council, rather than with a separate organisation. Commercialisation is a reform process which is similar to — but less extensive than — corporatisation.



The assessment of existing anti-competitive local laws is proposed to complement each council's review of local laws as already required under the *Local Government Act*. The process for the subsequent review of new local laws is proposed to be as streamlined as possible, particularly for the smaller councils where the impacts are likely to be less significant.

In relation to many of the aspects of NCP, the Government proposes to issue further implementation policies later this year to assist councils in the adoption of NCP. This will include material to assist councils with undertaking NCP cost/benefit assessments (for both competitive neutrality and legislation review purposes), the proposed Code of Competitive Conduct and legislative proposals to give effect to corporatisation and commercialisation reforms.

The Government is also exploring the possibility of providing financial support to councils undertaking NCP reforms. This process involves examining access to "competition payments" for those councils participating in the reform process.

Overall, this paper proposes a pragmatic approach to the application of NCP to local government in Queensland. By limiting competitive neutrality (and certain aspects of the other NCP reforms) to the larger councils, those areas with the most potential for gain will be captured. At the same time, any additional administrative burden on the smaller councils (where potential gains to the overall economy are least) will be minimised.

## 1. INTRODUCTION

National Competition Policy (NCP) is arguably the most significant micro-economic reform initiative in the history of the nation to be jointly agreed by the Commonwealth, State and Territory Governments.

NCP is predicated on the principle that competition is the “engine room” of economic growth, employment and higher living standards. Given the globalisation of markets and the ever increasing competitiveness of the international economy, there is a need for Australia to “crash” through domestic barriers to competition if we are to sustain, and indeed improve living standards.

To achieve this, NCP consists of a number of separate reforms which, in aggregate, seek to deliver a widespread competitive revitalisation of the national economy over the next decade. The policy focuses on both the private and public sectors; in particular, Government business enterprises and unincorporated businesses (including the professions), which have traditionally been protected from competition.

All Governments have agreed that this reform is best undertaken on a national basis. The policy is therefore based on accepted reform principles aimed at providing a consistent approach to the dismantling of barriers to competition across State borders as well as legislation to ensure that the same competitive rules apply to all sectors of the economy, regardless of ownership.

While having a national focus, NCP offers significant economic and social benefits to Queensland.

In particular, NCP provides Queensland with a unique opportunity to establish a more competitive economy. It will boost economic development and make the State more attractive to major industry.

This will be achieved by ensuring that competition reform applies to those industry sectors which have most impact upon Queensland’s economy and the State’s attractiveness as an investment market, both nationally and internationally. Increased competitive pressure will facilitate higher levels of productivity and a narrowing of the performance gap between Queensland industry and world best practice. These gains will be reflected in lower prices and better service delivery for both consumers and industry.

A number of Queensland local government business activities are considered to be significant in this context. This paper outlines how NCP will apply to local government in general and to these significant business activities in particular.

Underlying the Government’s commitment to competition reforms through NCP is the recognition that the policy is about promoting efficient delivery of services within a broader social policy framework. As such, the State Government is keen to ensure that implementation of NCP will not compromise, but rather enhance, delivery of both State and local government social and essential service obligations.

## 2. WHAT IS NATIONAL COMPETITION POLICY?

National Competition Policy is a set of reform policies aimed at encouraging a better use of the country's resources — and hence provide a higher standard of living — through increasing competition. Commonwealth, State and Territory Governments at the 1992 Heads of Government Conference agreed to the appointment of an independent inquiry into competition in the Australian economy.

A Committee of Inquiry chaired by Professor Fred Hilmer was appointed in October 1992. Its purpose was to develop proposals for a national policy which would promote and maintain competitive forces to increase efficiency and community welfare, while accommodating other social goals.

This committee subsequently reported in August 1993.

In February 1994, the recommendations of the Hilmer Report were accepted in principle by the Council of Australian Governments (COAG).

A package of legislative and administrative arrangements reflecting many of the Hilmer Committee recommendations was endorsed by COAG in April 1995 in the form of the National Competition Policy. The policy appropriately gives the States and Territories considerably more latitude with regard to implementation of the competition reforms than was originally envisaged in the Hilmer Report.

### The National Competition Policy Inter-Governmental Agreements

At the 1995 COAG meeting, the Queensland Government became a signatory to three Agreements which comprise the National Competition Policy:

- the Conduct Code Agreement
- the Competition Principles Agreement (CPA)
- the Agreement to Implement National Competition Policy and Related Reforms.

#### Conduct Code Agreement

Under the Conduct Code Agreement, COAG agreed to extend the competitive conduct provisions of Part IV of the *Trade Practices Act* (TPA) to those activities previously not caught, *i.e.* Government business activities and the unincorporated sector (including the professions) which have to date only been subject to limited application of Part IV.

As a result of the Agreement, the Commonwealth and each State/Territory has or will enact legislation applying Part IV of the TPA to achieve a seamless coverage of the competitive conduct rules on a national basis.

This legislation also puts beyond doubt the application of Part IV to local government business activities.

Amendments to the TPA by the Commonwealth have already resulted in all State owned business activities being subject to Part IV from 21 July, 1996.

## Competition Principles Agreement

While the Conduct Code Agreement essentially deals with restrictions on competition arising from anti-competitive conduct, the Competition Principles Agreement establishes principles to address other forms of restriction on competition.

The agreement commits the parties to a suite of competition reforms impacting on all sectors of the economy. These are briefly outlined in Table 1.

**Table 1: Elements of the Competition Principles Agreement**

Policy Element	Purpose	Example
1. Third party access	to provide access, at “fair” prices and conditions, to facilities that are essential for competition to a “third party” ( <i>i.e.</i> someone other than the owner/supplier of the facility — <i>e.g.</i> a potential new user or existing user)	access by a third party to facilities such as telecommunication cables, gas pipelines and railway tracks
2. Prices oversight	to prevent the misuse of monopoly powers of Government business activities	introduction of arrangements similar to the Commonwealth Prices Surveillance Authority to State and local government business activities which exercise monopoly powers <sup>2</sup>
3. Structural reform	to reform the structure of Government-owned monopoly businesses where it is proposed to introduce competition	separation of vertically integrated electricity authorities into separate generation, distribution and transmission entities, to allow the potential for competition in electricity generation and retailing
4. Competitive neutrality	to remove benefits (and costs) which accrue to Government business activities as a result of their public ownership	<ul style="list-style-type: none"> <li>• requirement for Government business activities to pay taxes (or tax equivalents)</li> <li>• removal of regulations which provide special advantages for Government business activities when competing with the private sector</li> </ul>
5. Legislation review	to reform (or justify) Government regulation which restricts competition	<ul style="list-style-type: none"> <li>• (at a Commonwealth level) deregulation of domestic aviation and telecommunication arrangements</li> <li>• (at a State level) deregulation of various State agricultural statutory marketing arrangements has occurred; business regulations also reviewed</li> <li>• (at a local government level), integrated with the local law review process already established under the <i>Local Government Act</i></li> </ul>

<sup>2</sup> The Prices Surveillance Authority previously administered the *Prices Surveillance Act*. It had responsibility for examining the prices of particular goods and services in the Australian economy. The ACCC has taken over this responsibility and also promotes competitive pricing in markets.

## Agreement to Implement the National Competition Policy and Related Reforms

This agreement sets out the overall timetable for the implementation of the NCP reforms and related COAG Agreements governing reforms in specific industries — electricity, gas, road transport and water.

In the water industry, for example, cross-subsidies are to be made transparent and for urban water suppliers, two-part tariffs (constituting both an access and a consumption charge) are to be introduced, where cost effective. In addition, metropolitan bulk water suppliers are to charge on a volumetric basis, *i.e.* charges based on the volume of water used.

Under this agreement, the Commonwealth will make a series of “competition payments” to each State and Territory provided they meet the agreed timetable. The Commonwealth will also extend its guarantee to maintain Financial Assistance Grants to State and local governments in real per capita terms on a rolling three year basis from 1997/98.

## Application of the Competition Principles Agreement to Local Government

Under the Competition Principles Agreement, the principles of NCP are to apply to local government. Responsibility for application of the principles to local government lies with each State Government.

Each State, in consultation with local government, is required to publish a statement (by mid 1996) specifying how this is to be achieved. The statement must detail how the competitive neutrality, legislation review and structural reform principles of the CPA will apply to local government.

This paper forms the Queensland Government’s Local Government NCP statement in this regard.

### 3. NATIONAL COMPETITION POLICY AND LOCAL GOVERNMENT IN CONTEXT

Queensland’s local governments have annual expenditure of more than \$3 billion and control significant public infrastructure.

However, Queensland local government is highly decentralised and diverse in terms of population and service delivery capacity.

It ranges from the Brisbane City Council, Australia’s largest local government representing a population of 750,000, to Diamantina Shire, which serves a community of less than 300.

The complex variety of local government business activities in Queensland includes water and sewerage services, solid and liquid waste management, off-street car parking, land development, caravan parks, venues for entertainment, arts and sporting events, quarries, cattle saleyards and aerodromes.

The scale and extent of local government services in Queensland differs from other States, where significant services, particularly water and sewerage, are generally delivered through State Government authorities.

By contrast, local governments in Queensland generally provide domestic water and sewerage services. In the metropolitan area, the Brisbane City Council also provides public transport services (which are a State Government responsibility in other States).

Given the broad range of services they deliver, local government expenditure per capita in Queensland is the highest of the Australian states.

Some activities of Queensland local government are clearly significant businesses in the context of the Queensland economy.

For instance, Brisbane City Council's water and sewerage operation is the largest single business undertaking in local government in Australia, with current expenditure of some \$188m in 1995/96. Its public transport operations are also a major undertaking, with current expenditure of more than \$100m.

In essence, most of the business activity expenditure of Queensland local governments is by the larger metropolitan and provincial city councils, reflecting the way economic development and population growth have occurred.

Many local governments, especially the larger councils, are well advanced in implementing efficiency and competition related reforms.

For example, Brisbane City Council has embarked on the Brisbane City Enterprises project which in part relates to the commercialisation of business units as well as participation in joint ventures. The council also markets services to external clients in certain areas on a commercial basis; e.g. pavement sealing and the hire of specialist vehicles.

Some local governments are keen to corporatise certain activities and to have access to expanded powers in relation to the creation and operation of business units. Initiatives being taken under NCP will facilitate local governments achieving further improvements in service quality and efficiency.

These initiatives also build upon other local government reforms, especially those arising from the recent overhaul of the Local Government Act. The *Local Government Act 1993* replaced the prescriptive approach of the previous legislation with an expansive general competence power tempered with greatly broadened public accountability requirements. Other reforms under the Act include a requirement for local laws to be reviewed, accrual accounting introduced and development of corporate planning and annual reporting procedures.

## The Consultation Process

Following the Hilmer report, concerns about NCP were widely expressed by some Queensland councils. Smaller councils especially were concerned about the impact on their operations, and the potential to jeopardise their ability to deliver social obligations. In addition, a view was expressed by smaller councils that rigorous application of NCP would result in burdensome administration and unwarranted costs.

A joint State/Local Government Working Group was established in May 1995 to assist with the development of advice on implementation of NCP. The working group comprised senior State Government officers and representatives of the Local Government Association of Queensland (LGAQ) and the Brisbane City Council.

While consideration of the particular circumstances of Queensland local government has played a part in developing the proposals in this statement, the primary objective of the working group has been an outcome driven, pragmatic approach to competition reform.

The working group met regularly and developed a series of technical papers on implementation of competitive neutrality and NCP.

In addition, the group contributed to the development of two issues papers canvassing options for implementation of competition policy elements<sup>3</sup>.

Comments on the issues papers and a draft version of this paper were considered by the working group and taken into account in the development of this statement.

In addition, the LGAQ has initiated the networking of those councils it is anticipated will be most affected by NCP. These councils meet on a regular basis and share expertise and experience.

## 4. APPLICATION OF PART IV OF THE *TRADE PRACTICES ACT* TO LOCAL GOVERNMENT

A fundamental aspect of NCP is that all business activities should be subjected to the same competitive conduct rules. To achieve this the Commonwealth, State and Territory Governments have agreed that the anti-competitive provisions of Part IV of the *Trade Practices Act* (which deals with restrictive trade practices such as price fixing and anti-competitive exclusive dealings) will apply to those sections of the economy not previously exposed; primarily State Government business activities and unincorporated entities.

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<sup>3</sup> These were:  
“Local Government and National Competition Policy Issues Paper No. 1: Competitive Neutrality”; Queensland Department of Housing, Local Government and Planning, November 1995  
“Local Government and National Competition Policy: Issues Paper No. 2”; Queensland Department of Local Government and Planning, March 1996

These areas will be subject to the Part IV provisions from 21 July 1996, as a result of both Commonwealth and State/Territory legislation. This process will also remove any residual doubt that local government is subject to the TPA.

Beyond 21 July 1996, the only exempt local government business activities will be certain licensing activities and transactions between persons acting for the same local government.

If a local government determines its business conduct or administrative arrangements may be in breach of the provisions of Part IV, three possible remedies are available:

1. Cease the activity, or at least remove the anti-competitive aspects of the activity;
2. Seek authorisation of the Australian Competition and Consumer Commission (ACCC). Scope exists under the TPA for certain anti-competitive conduct to be authorised by the ACCC. Applications for authorisation are subject to a public benefit test. In certain circumstances, “notifications” can be lodged with the ACCC which, in effect, have a similar result; and
3. Seek statutory authorisation from the State Government. This option is also subject to a public benefit test and other conditions. Statutory authorisation is generally to be viewed as a last resort and is likely to be granted only in significant cases.

Proposals for either statutory authorisation or authorisation of the ACCC should be referred, in the first instance, to the Department of Local Government and Planning and Queensland Treasury.

Authorisations by the ACCC or State Governments of conduct otherwise in breach of the TPA hinge on demonstrating that benefits to the community as a whole exceed associated costs. Public interest assessment guidelines suitable for local government purposes are being developed by the State Government.

Prudent risk management by local government should include an examination of trading conduct in relation to the restrictive trade practices provisions of the TPA. The Local Government Association of Queensland has developed materials and processes to assist local government compliance in this respect.



## 5. APPLICATION OF COMPETITIVE NEUTRALITY

### What is Competitive Neutrality?

It is important for efficient resource allocation that Government business enterprises operate without any significant advantages or disadvantages as a result of Government ownership (*i.e.* they operate on a “competitively neutral” basis).

Currently, many Government business activities enjoy certain advantages that would not be available if these business activities were conducted by the private sector. For a start, virtually all Government businesses have traditionally been exempt from taxation. In many cases there is no requirement to pay dividends to the owner of the business (the State Government or local government) and/or the business has access to cheaper sources of finance (because of the Government’s higher credit rating and hence lower interest rate for borrowings). Also, some Government businesses are not subjected to the same business regulation as the private sector. Conversely, Government businesses may also suffer disadvantages which can affect their ability to compete on an equal footing; *e.g.* Government businesses are subject to public sector accountability legislation such as the *Freedom of Information Act*.

Where Government business activities have unfair advantages this can promote inefficient production and pricing practices which can result in an excess flow of resources to the public sector. This may limit resource availability to the private sector and can increase overall costs of service provision to the community. Efficient resource allocation requires that such distortions be removed.

Accordingly, the NCP requires the removal of advantages (and disadvantages) that significant Government businesses derive from their Government ownership and which prevent them from operating on a competitively neutral basis. The major focus of this section of the paper is to outline how competitive neutrality will apply at the local government level.

Competitive neutrality will make the true costs and level of performance of Government businesses transparent and will facilitate better decisions regarding their operation by both managers and Government owners alike. Competitive neutrality will also promote productivity gains which will flow to consumers and industry in the form of better service and lower prices.

The application of competitive neutrality to local government will also continue the process of reform established under the *Local Government Act*, the first objective of which is “to provide a legal framework for an effective, efficient and accountable system of local government in Queensland”.

## Requirements of the National Competition Policy

In essence, the NCP requires that, subject to a public benefit test, significant Government business activities should be either corporatised or placed on a “level playing field” basis in some other way such that major competitive advantages from their public ownership are removed.

The specific requirements of the policy are outlined in Clause 3 of the Competition Principles Agreement.

**Clause 3(4)** provides certain requirements will apply to business enterprises which are both “significant” and classified as Public Trading Enterprises (PTEs) or Public Financial Enterprises (PFEs) by the Australian Bureau of Statistics for the purposes of its Government Financial Statistics Classification.

These requirements are:

- (i) adoption of a corporatisation model where “appropriate”; or
- (ii) imposition of full Commonwealth, State and Territory tax equivalents, debt guarantee fees and regulations applying to private business.

**Clause 3(5)** provides for less stringent requirements to apply to activities other than PTEs or PFEs where these are conducted as part of a broader range of functions. While the measures prescribed under clause 3(4) are to be considered, the option exists to not undertake broader corporatisation or commercialisation structural reform, but rather to ensure that prices include a provision for costs as per (ii) above.

In summary, the clause requires that competitive neutrality be applied by either:

### **Method 1**

where appropriate, corporatising significant business activities [Clause 3(4)]; or

### **Method 2**

commercialising significant business activities [Clause 3(4)]; or

### **Method 3**

by adopting full cost pricing; *i.e.* prices should reflect the actual cost of providing the good or service [Clause 3(5)]<sup>4</sup>.

In the case of Methods 1 and 2, the business entity or unit is to be subject to tax equivalent payments, charged a debt guarantee fee and subjected to private sector business regulation. Method 3 requires that prices charged merely include a provision for these costs.

<sup>4</sup> This option, however, does not preclude councils from subsidising prices for business activities, provided certain criteria are met. This is discussed later in this chapter of the paper.

Further, the agreement provides for these reforms to apply only where the benefits from reform will exceed the costs.

## Principles Underlying Application of Competitive Neutrality

Five key principles underlie the Queensland Government's application of competitive neutrality reforms to local government.

1. Competitive neutrality reforms will only apply to what could be regarded as "business activities" of local government<sup>5</sup>. That is, it does not extend to the non-business, non-profit activities of local government such as regulatory activities or roadworks under a council's control. For an activity to be a business it must trade in goods or services to clients.
2. The reforms only apply to "significant business activities". In this respect, criteria have been set to clearly identify those business activities that are likely to be of a size which would justify the imposition of the reforms. The criteria are based on current expenditure thresholds. Below these thresholds, local government business activities will not be subject to the NCP competitive neutrality reform requirements. Nonetheless, councils will be encouraged to apply a related reform proposal (referred to as the Code of Competitive Conduct) to these activities. The Code is discussed later in this paper.
3. For those significant business activities which are targeted, the reforms need apply only to the extent it can be demonstrated the benefits of implementation of the reforms outweigh the costs. This evaluation will largely be the responsibility of the respective council, subject to the council's decision being made on the basis of processes which are transparent to their communities.
4. NCP will not require compulsory competitive tendering. Local governments have wide powers to decide what activities they want to make subject to a competitive tendering process. There are no State requirements for particular local government services to be subject to competitive tendering. Rather, the decision as to whether a council business activity should be subject to competitive tendering rests with each local government. Where, however, a competitive tender is sought, local government "in-house" bids should be made on a competitively neutral basis.
5. Where competitive neutrality is applied, it will not interfere with the capacity of a local government to subsidise the provision of goods or services to particular groups; again provided that where a Community Service Obligation payment is made, the level of payment is readily identified in public accounts.

National Competition Policy "*includes no mechanism or incentives to Governments to reduce their commitment to the effective delivery of their community service obligations*" (Second Reading Speech, 1994; Competition Reform Bill).

<sup>5</sup> In the case of most local governments, "business activities" would cover undertakings such as water and sewerage services, public transport, entertainment venues, off street parking and other activities which could reasonably be regarded as being able to be delivered by a private sector firm (for the purpose of earning profits), in the absence of the local government's involvement.

Overall, the Queensland Government is concerned that implementation of NCP does not jeopardise the social obligations of local governments to their local communities.

For smaller local governments in particular, the distinction between “business” and “social” activities is frequently blurred. Moreover, full imposition of competitive neutrality to activities of small local governments can potentially result in high transition and ongoing administrative costs. As a result, the public benefit from applying the full rigor of competitive reform at this level is highly questionable and may, indeed, be counter-productive, bearing in mind the small scale of the activities involved.

## Local Government Significant Business Activities

For the reasons outlined above, the focus of competitive neutrality reform of local government will be on those activities where the most gains can be made. Two types of business entities — referred to in this paper as Type 1 and Type 2 activities, have been categorised as “significant” and will be subjected to the clause 3(4) and 3(5) reforms.

Type 1 and Type 2 business activities are defined as follows<sup>6</sup>:

### *Type 1 business activities<sup>7</sup>*

The activity has a current expenditure, in the case of water and sewerage enterprises combined, greater than \$25m p.a. or, in the case of other enterprises, greater than \$15m p.a. in 1992/3 terms.

*Based on this criterion, the following activities would need to consider competitive neutrality reforms: Brisbane public transport; Brisbane and Gold Coast garbage; and Townsville, Logan, Ipswich, Gold Coast and Brisbane water and sewerage.*

### *Type 2 business activities*

The business activity has a current expenditure, in the case of water and sewerage enterprises combined, greater than \$7.5m p.a. or, in the case of other enterprises, greater than \$5m p.a. in 1992/3 terms.

*Based on this criterion, the following activities would need to consider competitive neutrality reforms: Garbage services of Cairns, Ipswich, Logan, Maroochy and Townsville; and water and sewerage services of Caboolture, Cairns, Hervey Bay, Caloundra, Mackay, Maroochy, Noosa, Pine Rivers, Redland, Rockhampton, Thuringowa and Toowoomba councils.*

<sup>6</sup> These are examples only. Decisions will need to be made on the basis of more recent data (which is to be discounted to 1992/93 dollars). For example, recent Brisbane City Council data shows the Sleeman Sports Centre and the Brisbane Entertainment Centre would be Type 2 activities.

<sup>7</sup> Whilst the Competition Principles Agreement requires State Governments to base their list of significant business activities on the ABS list of PTEs and PFEs, this is not viewed as appropriate for local government in Queensland. The ABS local government list, for example, does not include garbage services of councils, or the Brisbane Entertainment Centre yet, on the other hand, includes a large number of insignificant business activities (in terms of size of operation). Instead of relying on ABS data, it is proposed that councils utilise their audited financial statements for identifying Type 1 and 2 business activities.

Due to the unavailability of reliable data at the State level, it is difficult to accurately estimate what portion of overall local government business activity would be targeted as Type 1 and Type 2 activities. As a guide, however, with regard to the water and sewerage sector, (which is the most common “business undertaking” across most Queensland local governments), they would account for approximately 80% of total current expenditure on water and sewerage by all Queensland councils and 84% of the annual revenue from water and sewerage fees and charges. (See Diagrams 1 and 2 on page 23)

Accordingly, whilst Type 1 and Type 2 activities relate to only around 15% of local governments in Queensland, it is envisaged they would cover a very high proportion of overall local government business activity and certainly those activities of regional and State-wide economic significance.

### Treatment of Roadworks

As indicated above, local government road construction and maintenance work on roads under a council’s control is not included as a significant business activity. However, if a local government enters into a contract with another local government to construct or maintain its roads, this would be regarded as a “Type 3” business activity (discussed below). The same would apply to a local government that opened up its road construction and maintenance works to competitive tender and submitted an “in-house” bid.

In recent years, road construction on State roads has been significantly opened to competition. Whilst there is a need to ensure that road construction and maintenance productivity continues to improve, it is important to ensure that increased efficiencies through increased competition do not negatively impact on the viability of rural communities. In this respect, the Government recognises the importance for some local governments to maintain an efficient, “right-sized” work force. In some cases this, in turn, requires continuity of work in the road construction and maintenance area.

Accordingly, the Government will be implementing new arrangements for the delivery of road infrastructure under the Roads Implementation Program. To promote efficiency in roadworks, it is proposed that contract work undertaken by local government on State-controlled roads (other than through a sole supplier arrangement) will need to comply with competitive neutrality requirements when competing in an open tendering process for construction or maintenance work on State controlled roads.

## Reforming Type 1 and Type 2 Businesses

Based on the criteria outlined in the previous section, local governments will have to identify any enterprises that are Type 1 and Type 2 business activities.

Subsequently, for the first five years, local governments will need to identify if any additional business activities meet the criteria for Type 1 and Type 2 business activities on an annual basis.

Legislation to give effect to these requirements will need to be enacted in the second half of 1996.

For Type 1 activities, if it is shown to be appropriate through a public benefit assessment, each respective local government is to implement:

- a corporatisation model<sup>8</sup>; and/or
- a tax equivalent regime for the business activity and the imposition of debt guarantee fees and regulation equivalent to that applied to the private sector.<sup>9</sup>

Corporatisation involves the establishment of a separate legal entity (with its own board of directors) to undertake the business activity on a commercial basis. A Government discussion paper detailing how a corporatisation framework could work in the local government arena is to be released in the near future. Legislation to enable local governments to establish such corporations is proposed to be enacted by the end of 1996.

A tax equivalent regime already operates at the State Government level, whereby State Government Owned Corporations and certain other business undertakings remit the equivalent of Commonwealth Government taxes to the State Government, rather than to the Commonwealth. It is proposed to establish a similar regime to apply at the local government level.

The State Government will not seek any financial transfer from local to State Government by way of tax equivalent payments. In other words, it is proposed that any tax equivalent payments by council business activities be made to its “parent” council, and not the State or Commonwealth Government.

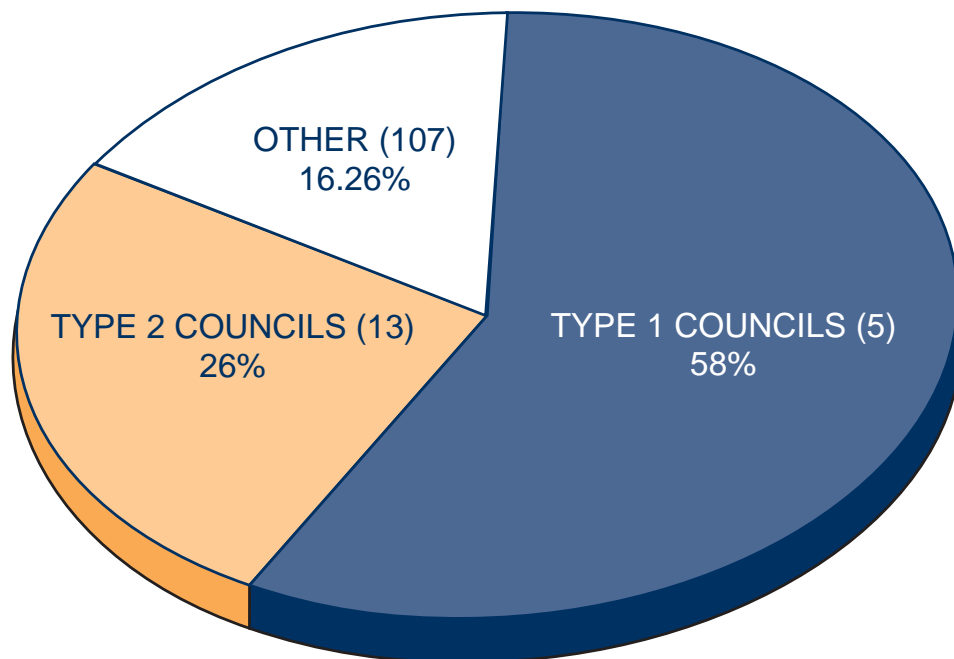
Proposed arrangements for the application of a tax equivalent regime at the local government level will be considered shortly by the working group.

With regard to regulatory powers, certain issues will need to be addressed not only by local governments themselves, but also by the Queensland Government as a part of the review of the *Local Government Act* (and other relevant legislation) during the legislation review component of NCP (discussed further in section 7 of this paper).

<sup>8</sup> Corporatisation automatically requires the application of tax equivalents, etc.

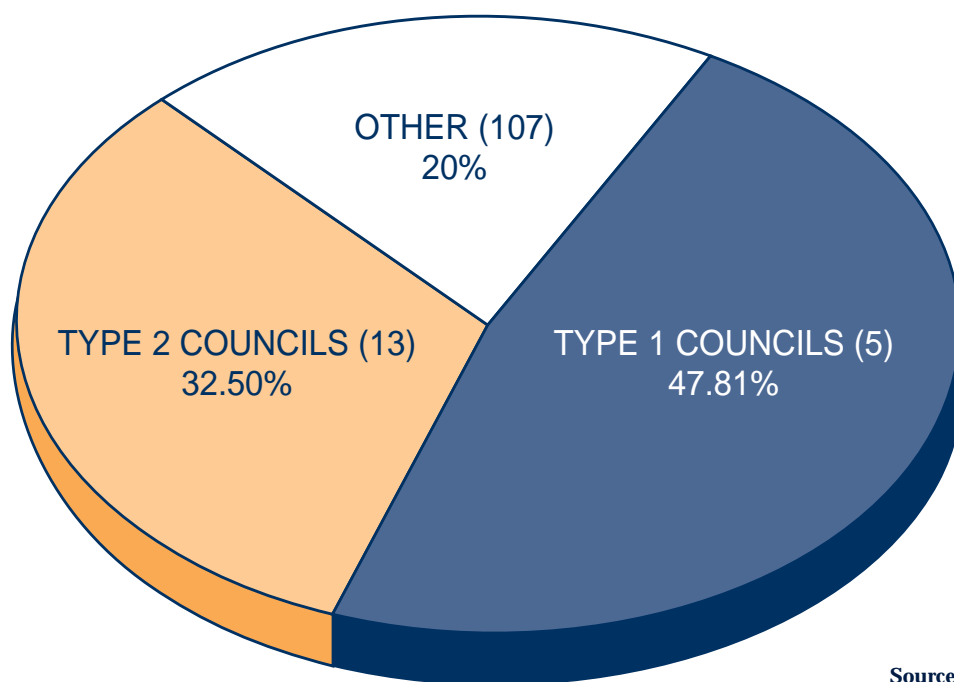
<sup>9</sup> In relation to competitive disadvantages that occur due to Government ownership, it is proposed that the respective Governments (state and local) remove these disadvantages, where justified.

**Diagram 1: Current annual revenue — fees and charges (\$m) water and sewerage (local government — State-wide 1993/94)**



Source ABS cat no. 5502.3

**Diagram 2: Current annual expenditure (\$m) water and sewerage (local government — State-wide 1993/94)**



Source ABS cat no. 5502.3

**For Type 2** activities, similar reforms are to be implemented where appropriate.

Again, the reforms are to be subjected to a public benefit assessment which will need to include the impacts of prices more accurately reflecting the full cost of providing the relevant goods or services.

Councils should note that full cost pricing will not prevent local governments from subsidising prices of goods and services, provided the subsidies are treated as explicit community service obligations which are separately funded by the parent local government with full disclosure in the council's annual report. In this manner, certain local government business undertakings may continue to be provided at less than the "full" cost of their production, but the difference will be made transparent (*i.e.* it will need to be accounted for, and published, in a manner which allows for public scrutiny).

Proposals on how cost reflective pricing may operate will be released over the coming months.

## Other Implementation Matters for Type 1 and Type 2 Activities

The introduction of tax equivalents, debt guarantee fee equivalents and private sector equivalent regulations is consistent with, and indeed is a significant part of, what are commonly referred to as commercialisation reforms. Under commercialisation, a Government business activity is restructured to become more commercial in its focus, whilst remaining within the Government department/council. It is a similar, but less extensive, process to corporatisation, as a separate legal entity is not established to undertake the business activities.

Some local governments have already contemplated introducing commercialisation reforms for their major business undertakings. For these and many others, it may be desirable to investigate implementing a more comprehensive commercialisation process at the time of investigating the benefits of introducing these other competitive neutrality reforms. For local governments interested in pursuing this option, Attachment 2 outlines the commercialisation model applied by the Queensland Government to its own departments. This will be used as a basis for developing proposals for a legislative framework for a local government commercialisation model.

Whilst councils will have the responsibility for undertaking cost benefit assessments, the decision on each assessment must be notified to the State Government.



## Reforming Type 3 Businesses

For those smaller business activities undertaken in direct competition with the private sector which are not Type 1 or Type 2 activities, a separate reform process is proposed. For these activities — referred to as Type 3 business activities — it is proposed that a voluntary Code of Competitive Conduct will apply.

The code is currently being considered by the State/Local Government NCP Working Group. Further details are included in Attachment 3.

Diagram 3 summarises the application of competitive neutrality to local government business activities.

## Complaints Mechanism

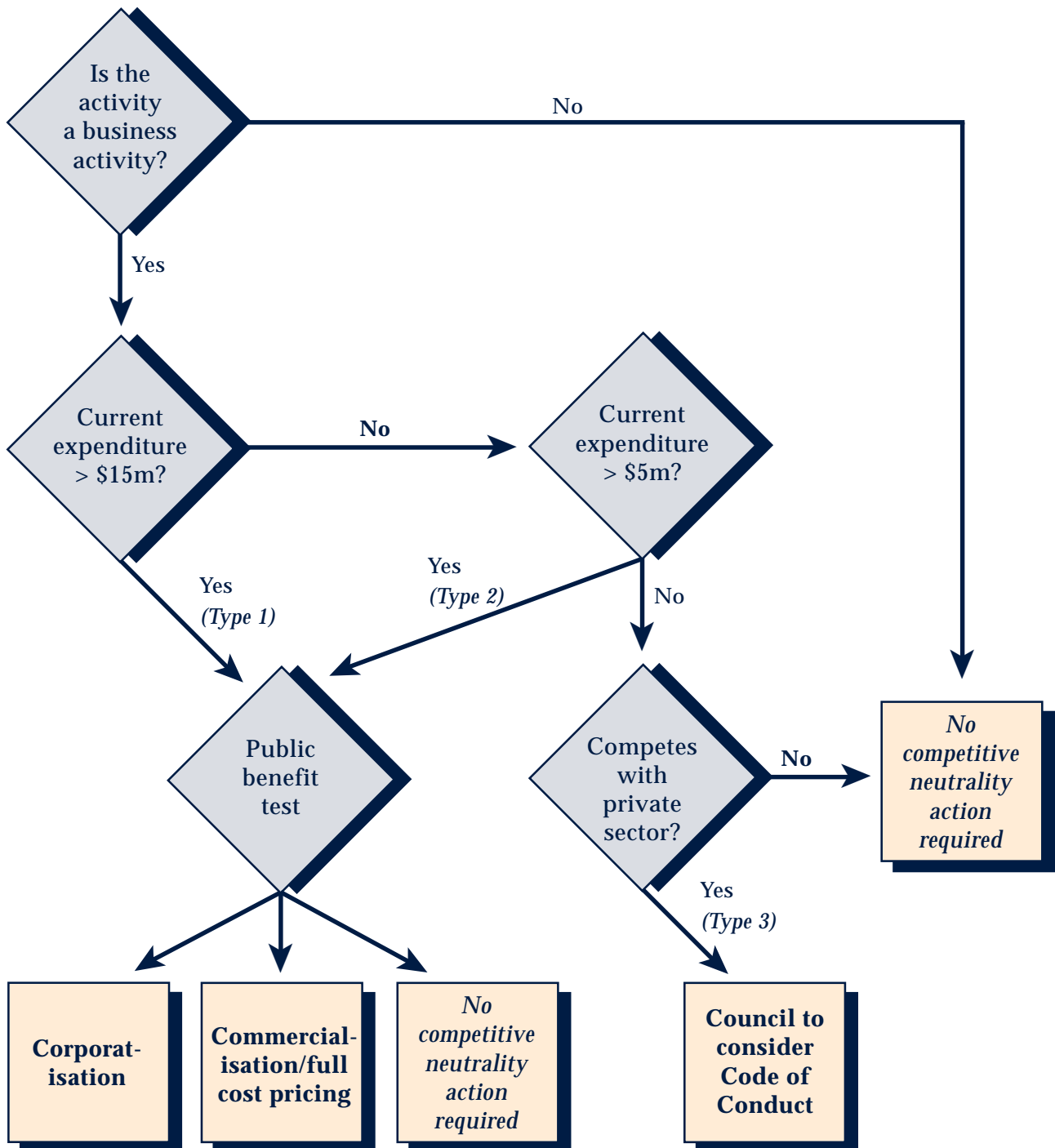
The Competition Principles Agreement (CPA) requires that a complaints mechanism be established in relation to competitive neutrality. The purpose of introducing a complaints mechanism is to ensure that Government significant business activities adhere to the principles of competitive neutrality as outlined in the CPA.

The Queensland Government will be establishing such a mechanism for its significant business activities. A similar process will need to be in place for local government Type 1 and Type 2 activities.

The main features of the proposed mechanism are:

- local governments will be responsible for establishing their own internal complaints mechanism in the first instance;
- if complaints are not resolved by the relevant local government, competitors will be able to approach the State body responsible for addressing NCP non-compliance matters;
- complaints are only to be lodged by genuinely disaffected parties; and
- the complaints may only be lodged against Type 1 or Type 2 business activities.

**Diagram 3: Application of Competitive Neutrality to Local Government Business Activities**



**Notes:**

1. Expenditure thresholds relate to 1992/93 data (current expenditure only)
2. \$15m threshold relates to individual business activities; \$25m is comparable figure for combined water/sewerage
3. \$5m threshold relates to individual business activities; \$7.5m is comparable figure for combined water/sewerage
4. Corporatisation and commercialisation/full cost pricing involve imputing tax equivalents, etc.

It is proposed that complaints be **limited** to those activities which, following a public benefit assessment, are subjected to competitive neutrality reform. The ground for complaint will be whether the activity is operating on a competitively neutral basis.

Details of the State Government complaints mechanism will be released with the Queensland Government Competitive Neutrality Statement.

## Public Benefit Assessment

Competitive neutrality reforms to Type 1 and 2 businesses under NCP will occur only where it can be demonstrated that benefits to the community from the reforms outweigh the associated costs. (It is expected that a similar process will be included in the voluntary Code of Competitive Conduct in relation to Type 3 business activities.)

Under the Competition Principles Agreement, matters which need to be considered in the public benefit assessment include:

- Government legislation relating to ecologically sustainable development;
- social welfare and equity considerations including community service obligations;
- Government legislation and policy relating to matters such as occupational health and safety, industrial relations and access and equity issues;
- economic and regional development, including employment and investment growth;
- the interests of consumers;
- the competitiveness of Australian business; and
- the efficient allocation of resources.

Results of the public benefit assessments by individual local governments are to be made publicly available. The Queensland Government will release guidelines for the undertaking of public benefit assessments during the second half of 1996, following the enactment of enabling legislation.

## Reporting Requirements for Competitive Neutrality

Local governments with Type 1 and 2 businesses are to advise the Department of Local Government and Planning annually on the implementation of competitive neutrality. This information will be included in the State Government's annual report on the introduction of competitive neutrality for its own entities. It is envisaged that these reporting arrangements will be phased out when most of the reform initiatives have been completed.

## Protection for Consumers

Consumers of Government goods and services have expressed concern that corporatisation or commercialisation of major utilities could provide incentives for price increases or service deterioration, or both. One means of safeguarding consumer interests is through the introduction of a prices oversight mechanism. This aspect is addressed later in this paper.

Another means of protecting the interests of consumers is for local governments with Type 1 and Type 2 businesses to consider the introduction of "Consumer Charters". Charters (or service guarantees) are published standards of service made by an organisation which consumers are entitled to expect and include mechanisms on what to do if the service provided does not meet the stated standard. Such charters are increasing in prominence both in the private sector and in Government Owned Corporations.

The Queensland Government is to release guidelines, for consideration by councils, on the development of consumer charters later this year.

## 6. APPLICATION OF STRUCTURAL REFORM

The Competition Principles Agreement requires examination and review of market structure where the introduction of competition into Government monopoly markets is being considered by the owner Government. Consequently, before competition is introduced in a local government monopoly market, the structure of the market and the incumbent monopoly supplier must be reviewed.

Matters to be considered as part of the review are:

- (i) the removal from the public monopoly business of responsibilities for industry regulation. This avoids potential for conflict of interest which may result in the public business being favoured over competitors;
- (ii) determining the appropriate commercial objectives of the public monopoly business;
- (iii) separation of "natural monopoly" elements from potentially competitive elements;
- (iv) separation of potentially competitive elements;
- (v) the introduction of competitive neutrality;
- (vi) assessing the merits of community service obligations; and
- (vii) the appropriate financial relationships between the owner of the public monopoly business (*i.e.* Government) and the business itself, including appropriate rate of return targets, dividends and capital structure.

In practice, structural reform considerations would normally be addressed during any major organisational reform exercise. In the case of the Queensland Government, these issues are addressed as part of the corporatisation and commercialisation process.

Initiatives by the State Government will provide support to councils for structural reform in the form of corporatisation or commercialisation. Considerable attention has been devoted to developing legislation to provide a local government corporatisation model which achieves suitable corporate governance standards while permitting appropriate levels of managerial autonomy.

Legislative options for commercialisation in local government are also being developed.

Monopoly rights conferred upon local government by State legislation will become subject to review under the legislation review exercise. If there is a need to remove monopoly rights as a consequence of any review, the structural reform process outlined above would need to be applied. In cases where the review of legislation results in the introduction of competition in markets which were previously subject to (local government) monopoly control, the relevant local government(s) will be required to comply with the structural reform principles as outlined in the Competition Principles Agreement.

## 7. APPLICATION OF LEGISLATION REVIEW

The Competition Principles Agreement requires all existing and proposed legislation to be reviewed with a view to reforming anti-competitive provisions where no net public benefit can be demonstrated or where the objectives of the provisions may be met in some other manner.

Specifically, each State/Territory government is to develop a timetable by June 1996 outlining a program for the review and, where appropriate, reform of legislation that restricts or may restrict competition. The review process must be completed and the implementation of any reform initiatives is to be commenced by the end of the year 2000.

“Anti-competitive provisions” for the purposes of legislation review are those imposing unnecessary cost, penalty or restriction on business, or creating or potentially creating barriers to entry to a market or barriers to competition within a market.

As part of the State’s legislation review exercise, the Department of Local Government and Planning will review State legislation relating to local government (principally the *Local Government Act* and the *City of Brisbane Act*). The department will also review model local laws made under the *Local Government Act*.

In addition, the local laws of every local government are subject to review.<sup>10</sup> It is proposed the review exercise will be coordinated, to the greatest extent possible, with each council's general review of local laws required under section 802 of the *Local Government Act*. Each council is required to review its existing local laws by March 1997. If reviews are not completed by this time, the local laws cease to have effect. The co-ordination of this review process with the NCP requirement is expected to involve amendments to extend the time allowed for the general review of local laws.

Thereafter, each local government must review all local laws at least once every ten years.

In general terms the review process must:

- (a) clarify the objectives of the legislation;
- (b) identify the nature of the restriction on competition;
- (c) analyse the likely effect of the restriction on competition and on the economy generally;
- (d) assess and balance the costs and benefits of the restriction; and
- (e) consider alternative means for achieving the objective of the legislation.

The matters to be taken into account in the legislation review process are shown in Attachment 1.

## Process for Review of Local Laws

The review process will first target local governments whose business activities are identified as Types 1 and 2 for competitive neutrality purposes. These local governments will be required initially to identify local laws containing provisions which may be anti-competitive.

It is proposed that this process be completed by July 1997. The formal assessment process, council consideration of the recommendations of the assessment, and subsequent decisions on reform must be completed by June 1999.

For other local governments, the initial identification of anti-competitive provisions should be performed by January 1998, although the assessment deadline would also be June 1999.

<sup>10</sup> At this stage, local governments will not be required to review planning schemes for actual or potential anti-competitive provisions. It is considered that a better approach would be to phase in NCP review requirements over time as part of the overall review process for local planning schemes (currently set out in the *Local Government (Planning and Environment) Act* i.e. local planning schemes can run for 10 years but have to be reviewed after seven years in accordance with the requirements of that Act). Review arrangements for local planning schemes will also be considered as part of the forthcoming review of the public submissions on the draft *Planning, Environment and Development Assessment (PEDA) Bill* commissioned by the Minister for Local Government and Planning. It may be appropriate for any revised PEDA legislation to set out the agreed process and timing for review of planning schemes to meet NCP requirements.

The methodology for the local law review will be determined by the State Government and legislation will need to be enacted in the second half of 1996. A balance will be struck between suitable rigour of process and additional obligations upon local governments, particularly in light of the limited resources available to local governments to undertake the review. It is proposed that the process be as simple and streamlined as possible, particularly for smaller and more remote local government areas where the impact of restrictions on competition may be minimal.

Local governments will be required to consult with the main parties affected by the local laws.

## Assessment of Proposed Local Laws

As indicated above, the Competition Principles Agreement requires proposed legislation to be assessed if it includes anti-competitive provisions.

This will need to be applied to proposed local laws and proposed amendments to existing local laws.

The process for this assessment would be similar to that for a review of existing local laws, as outlined above; *i.e.* it is to be as simple and streamlined as possible, particularly for smaller local governments.

## Implementation and Reporting

Legislation will need to be enacted in the second half of 1996 to set out the requirements for assessment of proposed local laws and proposed amendments to existing local laws.

The Department of Local Government and Planning will oversee the local law review exercise. Reviews will need to be timely, comply with the agreed methodology and exhibit integrity with regard to the objectives of the legislation review principle.

Under the Competition Principles Agreement, each party is to publish an annual report on its progress towards achieving the legislation review requirements. Progress in local government will be a component of the Queensland Government's annual report.

In the interests of consistency of treatment, the Department of Local Government and Planning will have responsibility for supervising the local law review exercise, including certification of the results of each local government review. Once completed, the consolidated results for local government will be presented to Queensland Treasury to be incorporated in the Queensland Government's Annual Report to the Commonwealth.

The application of legislation review to local laws is summarised in Table 2.

**Table 2: Application of Legislation Review to Local Laws**

Type of Local Law	1996–1999 Review	Subsequent 10 yearly review	Responsibility for review
Existing model local laws	Must be reviewed for anti-competitive provisions by 31/12/97.	yes	DLGP
New model local laws (laws which become operative after mid 1996)	Must be reviewed before introduction for anti-competitive provisions. DLGP to be satisfied that new model local law is not anti-competitive, or if anti-competitive, is justified in the public interest.	yes	DLGP
Existing local laws made by individual local governments	Must be reviewed for anti-competitive provisions by each local government. Councils to review all their local laws by June 1999.	yes	all local governments
New local laws and amendments to existing local laws made by individual local governments	Must be reviewed before introduction for anti-competitive provisions. Prior to introduction, council is to satisfy itself that the new local law is not anti-competitive, or if anti-competitive, is justified in the public interest.	yes	all local governments

## 8. TIMING OF APPLICATION OF COMPETITIVE NEUTRALITY, STRUCTURAL REFORM AND LEGISLATION REVIEW PRINCIPLES

The Queensland Government will need to introduce new/amended legislation over the coming financial year to give effect to many of these reform initiatives.

A provisional legislative timetable for competitive neutrality, structural reform and legislation review is illustrated at Table 3. Adequate time will be provided to enable local governments to assess and implement appropriate reforms, and therefore target completion dates may need to be adjusted.

The table highlights the need for the Queensland Government to introduce legislation — desirably by the end of 1996 — to address two issues; namely:



- (i) to set out requirements for identification and assessment of Type 1 and Type 2 business activities and for review of existing and proposed local laws; and
- (ii) to provide a legislative framework for the application of competitive neutrality through corporatisation, commercialisation or cost reflective pricing.

**Table 3: Timing of Application of Competitive Neutrality, Legislation Review and Structural Reform**

NCP Element	Target Completion Date
<p><b>Competitive Neutrality</b></p> <p>(a) Corporatisation and/or tax and debt guarantee fee equivalents, regulatory neutrality</p> <p>(b) Full cost pricing</p> <p>(c) Code of Competitive Conduct (note: this does not form part of NCP)</p>	<p>Legislation by end 1996. Public benefit assessment to be completed by July 1997. Implementation by July 1998.</p> <p>Legislation by end 1996. Public benefit assessment to be completed by July 1997. Implementation by July 1998.</p> <p>Note: Local governments with Type 1 and 2 businesses to report annually on introduction of competitive neutrality reforms.</p> <p>Development of a proposed code by end 1996. Consideration by council of adoption of code by July 1998.</p>
<p><b>Legislation Review</b></p>	<p>Legislation to provide for NCP review of local laws by end 1996. Review and assessment by Department of Local Government and Planning of model local laws by December 1997. For local governments with Type 1 and 2 businesses, identification of anti-competition provisions in local laws by July 1997 and assessment by June 1999. For other local governments, identification of anti-competition provisions in local laws by January 1998 and assessment by June 1999. Reporting: as appropriate to meet the requirements of the Competition Principles Agreement.</p>
<p><b>Structural Reform</b></p>	<p>Legislation (in relation to corporatisation) by end 1996. Implementation: ongoing.</p>

## 9. APPLICATION OF OTHER ELEMENTS OF NATIONAL COMPETITION POLICY

Although the terms of the Competition Principles Agreement require only the competitive neutrality, legislation review and structural reform principles to be addressed in the Local Government NCP Statement, the following section discusses current proposals with respect to other elements related to the Competition Principles Agreement and Competition Code Agreement.

### Prices Oversight

The Competition Principles Agreement requires State Governments to consider establishing independent sources of prices oversight for significant State-owned monopoly or near monopoly Government business activities. The objective of the prices oversight principle is to prevent the charging of excessive prices for goods and services supplied by business activities possessing significant market power.

If State Governments fail to establish effective prices oversight arrangements, there is scope for the Commonwealth Government, through the Australian Competition and Consumer Commission (ACCC), to assume responsibility for this role. The issue of which arrangements will apply for prices oversight regulation has not yet been determined by the State Government.

Local government monopoly or near monopoly business activities, *e.g.* water and sewerage, will be subject to State prices oversight arrangements, should the State Government decide in favour of State based regulation.

### Application to Local Government

The Competition Principles Agreement provides that prices oversight should apply to all significant Government businesses that are monopoly, or near monopoly, suppliers of goods and services.

In determining significance, a balance must be struck between the costs associated with prices oversight and benefits the process may offer. The application of prices oversight to smaller local government business activities is unlikely to yield appreciable net benefits.

Under State-based prices oversight regulation, it is considered local government monopoly or near monopoly businesses would be significant for the purposes of prices oversight if they accrue more than \$5M per year in 1992–93 terms in fees and charges, or \$7.5M per year in 1992–93

terms in the case of water and sewerage activities combined. Activities above these thresholds will be eligible for referral to an independent prices oversight body.<sup>11</sup>

However, prior to referral, the Minister responsible for prices oversight would consult with the Minister for Local Government and Planning and each affected local government.

Additionally, local governments may wish to refer business activities outside this scope for prices oversight (e.g. for an independent assessment of their pricing policies). In such cases, under a State regime, the Minister responsible for prices oversight will be obliged to make the referral.

It is not proposed that a State-based prices oversight regime would apply to local government goods or services which are substantially subsidised by any level of Government for the purpose of community service obligations. Prices oversight would apply only to service delivery conducted on a commercial basis.

In cases where prices of goods or services simply cover the costs of contracted service delivery, referral to prices oversight would be unlikely.

## Third Party Access to Essential Facilities

The objective of third party access is to provide a competitor with access on equitable terms and conditions to infrastructure facilities of national significance essential to competition in a related market and which cannot be economically duplicated.

The Commonwealth *Competition Policy Reform Act* establishes a national regime for third party access.

Under a third party access regime, the owner of “declared infrastructure” and an applicant for access are encouraged to reach an agreement. If agreement cannot be reached, legislation provides for dispute resolution by an independent agency. The terms of any ensuing agreement must protect the owner’s legitimate business interests.

The Competition Principles Agreement allows State Governments to establish their own access arrangements as long as they are consistent with the principles underlying the Commonwealth regime. The Commonwealth regime will not apply if an effective State system is in place.

The Queensland Government is considering the merits of establishing an access regime to apply particularly to Queensland Government infrastructure; *i.e.* in lieu of the Commonwealth arrangements applying.

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<sup>11</sup> In setting a threshold for prices oversight, a balance must be struck between the costs associated with prices oversight and the gains the process offers. Applying prices oversight to very small local government business activities, even if they are monopolies, is unlikely to yield net benefits in a state or national context. The threshold broadly corresponds with the threshold for the application of competitive neutrality to local government business activities except that, for prices oversight, the focus is on revenue rather than expenditure.

The State regime would have to comply with the principles of the Commonwealth regime, although this may be possible without the administrative and operational complexity of the Commonwealth system.

The issue remains as to whether local government infrastructure should be subject to the Commonwealth or, if it eventuates, a State-based regime. This matter will be further considered in the coming months during the finalisation of a State-based access regime proposal.

## Application of COAG Water Resource Policy to Local Government

In 1994, COAG adopted a set of water resource policy principles. These were, in the main, user-pays pricing policies to advance the objectives of recovering the full economic cost of water provision. Transparency or elimination of cross-subsidies was another important objective.

Specifically, in relation to urban water, the COAG Communiqué of 1994 specified for urban water markets:

- (i) the adoption, where cost-effective, by no later than 1998 of charging based on a connection fee in conjunction with a consumption fee;
- (ii) pricing regimes based on consumption, full cost recovery and removal of cross-subsidies not consistent with efficient and effective service. Continued cross-subsidies must be made transparent; and
- (iii) volumetric-based charging for urban bulk water structured so as to recover all costs and earn a positive rate of return on assets.

The State/Local Government Working Group is addressing these urban water issues and it is expected a discussion paper will be released in the near future.

Timetables were set at the 1994 COAG to achieve water resource policy objectives, and in 1995 these were linked to Commonwealth payments attaching to the delivery of competition policy commitments.

In Queensland, implementation of the principles will proceed on the basis of consultation with local government and other stakeholders. Proposals primarily affecting only urban water will be developed in conjunction with the State/Local Government Working Group so that water industry and NCP initiatives may be better integrated.

## 10. CONCLUSION

NCP provides Queensland with a unique opportunity to establish a more competitive economy, potentially boosting economic development and attractiveness of the State to major industry. It provides councils with the opportunity to participate in this process by reforming, where justified, certain aspects of their business operations. The State Government has agreed to provide financial incentives to councils to participate in the competition reform process.

However, in implementing the policy the Queensland Government seeks to ensure that the viability of rural communities is not compromised, and that there are no negative impacts on delivery of social obligations of councils.

Consistent with the focus of NCP on significant business activities of Government, this paper emphasises the application of competition policy to significant business activities of local government.

Further implementation policy and legislation for implementation will be developed over the coming months in consultation with the joint State/Local Government NCP Working Group and individual local governments.<sup>12</sup>

Table 4 summarises the proposed application of NCP to Queensland local governments.

<sup>12</sup> Specific details on the application to local governments of some of the elements of NCP have yet to be finalised. In most cases, it is proposed to issue further proposals by the end of 1996. Consultation will occur before these matters are finalised. A list of these matters is included as Attachment 4.

Table 4: Summary of proposed application of NCP to Local Government in Queensland

NCP Element	Proposed Extent of Application	Test	Arbitrator	Status of Policy Development	Timing of Application
Extension of coverage of Trade Practices Act	Most local government business activities, except certain licensing activities and transactions between persons within the same local government	Where the local government business activity breaches the Restrictive Trade Practices section (i.e. Part IV ) of the Act	ACCC	Finalised (Act has been amended)	Has probably always applied where local government was engaging in trading and/or financial activities, but definitely applies from 21 July 1996
Third Party Access	Final details to be clarified, but most likely to apply only to the larger local government business activities where substantial infrastructure is involved	“Significant” infrastructure facility unable to be duplicated economically	Subject to <b>either</b> the Commonwealth or State regime	Commonwealth: already applies State: being considered	Commonwealth: already applies State: considered for implementation by late 1996
Prices oversight	In the case of State-based regulation, monopoly or near monopoly business activities with annual current revenue in excess of \$5 million in 1992-93 terms. For combined water and sewerage services, \$7.5 million per annum. Generally corresponds with Type 1 and 2 activities as described in the statement	(re State-based regulation) revenue threshold plus monopoly or near monopoly government business activity	Either the ACCC or a State based body	State regime being considered by Government (although Commonwealth regime potentially already applies)	Commonwealth regime already applies; the merits of a State-based regime are currently being considered
Structural reform	Any local government considering the introduction of competition	Where competition is to be introduced into a monopoly market	Local government in conjunction with the DLGP	Principles established in the Competition Principles Agreement	Upon finalisation of Local Government NCP Statement

NCP Element	Proposed Extent of Application	Test	Arbitrator	Status of Policy Development	Timing of Application
<b>Competitive Neutrality</b> (a) corporatisation and/or tax equivalent regimes and payments involving guarantee fees; and full cost reflective pricing	Type 1 and Type 2 local government activities; with particular emphasis on Type 1 activities	(i) Exceeds Type 1 or 2 expenditure threshold limits, and (ii) Cost/benefit assessment	Local government (with oversight exercised by DLGP)	Policy outlined in draft statement legislation yet to be drafted	Proposed from July 1998
(b) Code of Competitive Conduct (Note: This does not form part of NCP)	Type 3 local government activities	Below Type 2 expenditure threshold (except for certain road construction and road maintenance works), operating in competitive market and cost/benefit assessment	Local government	Code to be developed by State/Local Government Working Group	Proposed from July 1998
<b>Legislation Review</b> State Government legislation	State Government legislation (including Local Government Act and City of Brisbane Act)	Legislation that restricts competition	Queensland Government, with annual reports to NCC	Public interest test guidelines being developed	Commencing mid 1996
Local laws	All Local Laws	Local laws that restrict competition	Local government, with DLGP oversight and annual reports to NCC	Public interest test guidelines being developed	Commencing mid 1996; to be coordinated with review of local laws (i.e. by mid 1999)
Model Local laws	Model Local Laws	Model local laws that restrict competition	Queensland Government with annual reports to NCC	Public interest test guidelines being developed	by December 1997
COAG water reforms	Yet to be resolved	Involved in urban water supply or metropolitan bulk water supply, although threshold limits yet to be resolved	Queensland Government	Application of reforms being addressed by State/Local Government Working Group	Varies, commencing from mid 1998 and possibly up to 2001

## ATTACHMENT 1: CRITERIA FOR IDENTIFYING LOCAL LAWS TO BE SUBJECT TO LEGISLATION REVIEW

Without limiting the matters to be taken into account, local law provisions to be reviewed are those that provide for:

- (i) an outright prohibition with regard to any particular business activity;
- (ii) a statutory monopoly;
- (iii) licensing or registration requirements for persons or bodies wishing to engage in a particular business activity and which operate on the basis of either limiting the number of participants or limiting participation to those persons or bodies that meet defined standards, qualifications or training or to those who hold membership of a particular occupational or professional organisation (an example would be the issuing of licences to roadside vendors);
- (iv) allocation of quantitative entitlements, quotas or franchises among participants engaging in a particular business activity;
- (v) requirements for prescribed quality or technical standards to be observed, or for specified equipment to be used, with regard to a particular business activity, other than those requirements that apply generally in regard to public/workplace health and safety;
- (vi) price control provisions, whether by way of setting, or prescribing a process for determining, the maximum/minimum prices or charges for a specified good or service or the maximum/minimum rates of commission, agency or fees for any good or service;
- (vii) restrictions on the conduct of a business relating to matters such as hours of operation, size of premises, provision of specified facilities, geographical area of operation, advertising or promotion, sector-specific operation (e.g., retail versus wholesale), type of good or service allowed to be offered for sale, *etc*;
- (viii) the nomination of a particular person or body as the sole or preferred customer or supplier in regard to a particular business activity;
- (ix) measures that have the effect of conferring a benefit on a particular person or body engaged in a particular business activity relative to other parties engaged in the same activity, including prescribing technical specifications or standards that can only be met by a particular operator, prescribing different requirements for public sector vis-a-vis private sector operators or making financial assistance available (including the waiver of various State or local government charges or fees as well as direct assistance measures such as a grant or subsidy) if a business is carried on at a particular place or in a particular manner;



- (x) the allocation of licences or other authorities which either allow the holder access to natural resources (including water, minerals, forests and fisheries)<sup>13</sup> or which create rights, or permit specified activities, denied to non-holders (for example, licences to collect and dispose of garbage and other waste material in a particular manner); and
- (xi) preferential purchasing arrangements.

The purpose of legislation review is not to develop a program for repeal, but to apply a review timetable and a workable review process. Legislation that restricts competition may be retained where benefits to the community can be shown to outweigh the costs.

<sup>13</sup> This criteria, however, is more relevant at a State Government level.

In relation to restrictions on access to natural resources, the following principles have been adopted at a State Government level in deciding if there is a restriction on competition, namely:

1. restrictions that exist only in Acts and regulations are to be considered in deciding if there is a restriction;
2. Crown ownership or control of the resource, and licensing schemes\* to regulate access to those resources are not restrictions per se;
3. limits on the number of licences issued, or on the amount of the resource attached to a licence, are restrictions, unless required for legitimate resource management purposes\*\*;
4. conditions imposed, or discrimination in the issuing, renewal or transfer of licences are restrictions unless for legitimate resource management purposes or for reasons associated with normal commercial dealings e.g. financial position and previous non-performance of applicants; and
5. non-licence conditions prescribed in legislation relating to harvesting and use of the resource (e.g. closed seasons, harvesting methods, etc.) are restrictions unless for legitimate resource management purposes.

\* "licence" includes permits, allocations and all other methods for controlling access to natural resources vested in, or under the control of, the Crown in the right of the State of Queensland.

\*\* "resource management purposes" means ensuring a natural resource is managed in an ecologically sustainable way in accordance with recognised scientific evaluations

## ATTACHMENT 2: COMMERCIALISATION OF BUSINESS ACTIVITIES

A reform option for Type 1 and 2 local government business activities has been loosely described as “commercialisation” of the activity. Specifically, this involves:

- (i) applying a tax equivalent regime for the business activity and establishing a regime involving payments equivalent to debt guarantee fees; and
- (ii) ensuring a level of regulation equivalent to that applied to the private sector.

However, these amount to only a part of what is generally regarded as necessary for commercialisation of a Government business activity. The following outlines major aspects of the State Government’s commercialisation model which are considered relevant for local governments undertaking this type of reform (*i.e.* in addition to requiring the implementation of (i) and (ii) as listed above).

### Queensland Government Commercialisation Model

Under this model, commercialisation is built around four key principles:

- competition with alternative providers on equal terms;
- clear specification of objectives;
- an appropriate level of management responsibility and autonomy; and
- strict accountability for performance.

Relevant components of this are listed below.

### Untying of Clients

- Business activities will be placed on a more commercial footing and, in many cases, required to compete for public sector business, rather than simply being allocated that business.

### Commercial Operating Framework

- Major stand-alone activities will be established as separate business units.
- Policy and regulatory roles will be separated from commercial activities within the portfolio department.

- Accrual accounting will be adopted and management information systems will be enhanced to facilitate performance monitoring.
- Commercial disciplines will be applied (e.g. dividend policy; commercial pricing arrangements; performance monitoring; taxation; capital structure).

## **Implementation Issues**

- Implementation by the Government will be on a case by case basis to ensure that detailed arrangements suit the particular circumstances.

## **Management Autonomy and Accountability for Performance**

- The portfolio minister will set strategic policy directions for the business unit, but will not be involved in day to day operations.
- The Treasurer would have a key policy role in relation to financial and economic performance and, with the portfolio minister would monitor performance.
- An annual performance contract will specify the objectives, nature and scope of the unit's main activities, target performance indicators, agreed CSO activities, target dividends and budget and other financial requirements.
- Business unit management will be responsible for commercial operations subject to Government policy.
- Continued management autonomy would depend on sound performance. Otherwise, tighter external controls would be imposed and, ultimately, more efficient private sector alternatives considered.

## **Performance Monitoring**

- Monitoring would encompass broad based economic, financial and non-financial indicators, balance sheets, profit and loss statements and cash flow forecasts.

## **Pricing Policies**

- Prices will be governed by competitive market forces.
- Invoicing and recovery of unpaid accounts will be on commercial terms.

## Capital Structure

- The mix of commercial debt and equity will be determined with reference to comparable private sector benchmarks and stability of cash flows.
- Debt/equity swaps and, in some cases, transfer of assets from/to the State Government's Budget may be required to adjust current capitalisation.
- The funding mix for major new capital investment will depend on the availability of Government funding and the ability of cash flows at that time to service debt *etc.*

## Dividend Policy

- Dividends will be negotiated annually. The starting point will be the target return on assets, less interest and tax equivalents. Other factors taken into account will include the level of profits generated, the need to retain earnings for re-investment in the business and the level of dividends paid in comparable private sector entities.

## Assets

- Assets required by the business will generally be vested in the business unit on commercialisation at current value.
- Surplus assets will be disposed of, with no automatic right of compensation.
- Assets will be valued in accordance with the Treasury policy document "*Recording and Valuation of Non-Current Physical Assets in the Queensland Public Sector*" (this is based on the deprival methodology for asset valuation). Comprehensive revaluations are to be undertaken every five years, with annual indexation in intervening periods.
- Detailed asset registers must be maintained.

## Taxation

- Under Commonwealth–States agreement, all State business enterprises are to make payments to the State in lieu of Commonwealth income tax and sales tax.
- As a general principle, the taxation arrangement to apply to fully commercial business units would mirror those applying to corporatised entities.

## Community Service Obligations (CSOs)

- CSOs are non-commercial activities which the Government has directed the business unit to undertake.
- A CSO must result from a specific, material and binding Government directive, satisfy a clearly defined policy objective and not be a normal cost of carrying on a business.
- CSOs would specifically exclude:
  - conditions applicable across the broad public service;
  - compliance with regulations;
  - activities which, although non-viable on a stand-alone basis, enhance business; and
  - activities which, if undertaken more efficiently, would be commercially viable.
- Funding of a CSO will be considered within the context of the Budget process, generally on the basis of the same principles as applying for CSO funding under corporatisation.

## ATTACHMENT 3: CODE OF COMPETITIVE CONDUCT

It is recognised that local governments undertake a multitude of smaller business activities participating in competitive markets (*e.g.* sport and recreation venues, quarries, offstreet car parking, caravan parks, cemeteries and crematoria, and land development activities). In most instances, these would not constitute Type 1 or Type 2 business activities (*i.e.* on the basis of size).

Generally, these are businesses which are not sufficiently significant to have economic impact at the State or regional levels, but are trading goods and services in a local or regional market in direct competition with the private sector.

Because of their smaller scale, these “Type 3” business activities are proposed to be dealt with separately from National Competition Policy. However, the proposed approach is consistent with the intent of competition policy reforms.

For these types of small business activities, it is proposed that local governments would be encouraged to adopt a voluntary Code of Competitive Conduct embodying principles of, at least, full cost pricing.

Again, the reforms are to be subjected to a public benefit assessment which will need to include the impacts of prices more accurately reflecting the full cost of providing the relevant goods or services. As with the other larger council business activities, cost reflective pricing will not prevent local governments from subsidising prices of goods and services, provided the subsidies are treated as explicit Community Service Obligations which are separately funded by the parent local government with full disclosure in the council’s annual report.

The code is also likely to address other commercial principles such as accountability and transparency.

The code, which will be developed in consultation with local government, would be most applicable in situations where a local government:

1. is engaged in competition with a private sector provider; or
2. elects to seek outside bids for service delivery and the council business activity is, itself, submitting a tender; or
3. enters into contracts with other local governments to undertake construction or maintenance works on local government roads, opens its road construction and maintenance works to competitive tender and submits an “in-house” bid, or contracts to undertake work on State-controlled roads (other than through a sole supplier arrangement).

While it is proposed, at this stage, that the code be voluntary, there are a number of process issues with which councils may need to comply. In particular, the finalisation of the code will need to consider whether a process such as the following be prescribed by legislation:

1. annual identification of the council's Type 3 business activities; and
2. publication of this list in councils' annual reports, particularly highlighting those activities which councils have determined should not be subject to the code (along with reasons supporting the decision).

This issue will be addressed in further detail when the draft code is released for public comment later in 1996.

## ATTACHMENT 4: NCP LOCAL GOVERNMENT ISSUES TO BE COMPLETED BY DECEMBER 1996

Issue	Purpose	Relevance
Amendments to legislation	development of legislation for identification and assessment of Type 1 and Type 2 activities and for reviews of local laws	Type 1 and Type 2 re business activities; all councils re review of laws
Corporatisation/ Commercialisation Legislation Discussion Paper	consultation on corporatisation and commercialisation models and legislation	Types 1 & 2
Public Benefit Assessment Guidelines	competitive neutrality assessments (corporatisation, commercialisation), <i>etc.</i>	Types 1 & 2
State Government Complaints Mechanism Regime	local government to link in with State regime	Types 1 & 2
Full Cost Pricing Guidelines	competitive neutrality	Types 1 and 2 (although may also be included in the Code)
Tax Equivalent Regime Manual	to provide Tax Equivalent Regime	Types 1 & 2
Code of Competitive Conduct	competitive neutrality, <i>etc.</i>	Type 3
Public Interest Test Guidelines	review of local laws (also to be used for authorisations for exemption from Part IV of the TPA)	all councils
(In the event of government introducing State-based regulation), State Government Prices Oversight Discussion Paper/Legislation	local government to link in with State regime (if State-based regulation to apply)	Types 1 & 2 (under a State-based regime)
State Government Third Party Access Discussion Paper/ Legislation	local government to link in with State regime	Types 1 & 2
COAG Water Discussion Papers, <i>etc.</i>	to meet COAG requirements	all councils
<i>Trade Practices Act</i> Audit/ Compliance Manual	to minimise TPA exposure	all councils