

1. The NCP Package and Progress to Date

1.1 The approach to National Competition Policy

The Commonwealth and all State and Territory governments adopted the NCP package in 1995. Because of the size of the package, implementation has been phased over several years. The National Competition Council plays a number of roles in the reform program, including assessing each government's progress in meeting its reform commitments at three stages of implementation: in July 1997, 1999 and 2001.

The Council has just finalised its first tranche assessments, and the progress to date has been positive. Most of the early activity focused on getting the policy agendas right, but a number of reforms have also been implemented, with some promising early results.

At the same time, recent public debate has revealed widespread confusion about competition policy and how it ties in with other government policies. For example, it has been suggested that the NCP agreements require certain policy actions such as repealing all anti-competitive legislation or privatising government businesses. Conversely, NCP is sometimes thought to preclude certain policy actions by governments, such as subsidising community services. More generally, there exists a concern that NCP is a form of 'economic rationalism' which focuses on money, markets and materialism with no regard for equity, the environment or the social fabric.

These concerns stem in part from limited awareness of the public interest safeguards built into the NCP processes. For example, when reviewing anti-competitive

legislation, governments must consider the effects of reform options on an array of public interest matters. These include the environment, employment, social welfare and consumer interests as well as business competitiveness and economic efficiency. These public interest matters must also be considered when assessing whether to apply competitive neutrality to particular government businesses and when reforming the structure of public monopolies (see Appendix 1).

The concerns about competition policy also stem from limited awareness of what the NCP program actually requires of governments. To clarify some of the most common misconceptions:

- NCP does not require the removal of all anti-competitive regulation, but ties reform directly to public interest safeguards (see section 1.5).
- NCP does not require the privatisation of any public entity (see section 1.6).
- NCP does not require reductions in government spending on important community services (see section 2.5).
- NCP is consistent with providing appropriate adjustment assistance when a reform measure adversely affects a particular section of the community (see section 2.2).
- Various NCP processes integrate economic and environmental considerations (see section 2.6).

1.2 The NCP reform package

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

Box 1 The NCP Agreements

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

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

The Council has published a compendium of the NCP agreements (NCC 1998b), which is available on the Council's website: www.ncc.gov.au

In summary, the NCP reforms agreed by governments in 1995 were to:

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

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

Sections 1.3 – 1.6 of this paper examine the reforms in more detail.

The Council’s Role

The National Competition Council was created in 1995 as an advisory body to governments on NCP implementation. While the Council is independent of the executive arm of any government, its work program is set by agreement of a majority of Australian governments.

In short, the Council has three key roles.

1. Assessment

The Council is required to assess each State and Territory government's progress in implementing NCP reform for the purpose of \$16 billion in competition payments from the Commonwealth over the period to 2005-06.

2. Functions related to specific NCP reforms

The Council plays a number of roles in relation to specific NCP reforms. To date, these roles relate principally to two areas:

- third party access to infrastructure. For example, the Council makes recommendations to governments on the effectiveness of State and Territory access regimes and on applications to declare significant monopoly infrastructure for third party access under the *Trade Practices Act*; and
- the review of anti-competitive legislation and regulation. For example, the Council recently conducted an inquiry into the *Australian Postal Corporation Act 1989*. The review was referred to the Council by the Commonwealth with the agreement of a majority of States and Territories.

3. Improving community understanding of NCP

The Council supports governments in explaining to the community the important relationships between competition reform, other aspects of government policy, and community objectives such as economic growth, full employment and social and environmental goals. The Council sees this role as particularly important, given that many of the reforms are complex and involve change – which can create conditions of uncertainty in the community. Three recent Parliamentary inquiries into the Council and the NCP program have emphasised the importance of community consultation and communication.¹

¹ House of Representatives Standing Committee on Financial Institutions and Public Administration (Hawker Committee) 1997, *Cultivating Competition: Inquiry into Aspects of the National Competition Policy Reform Package*, June; Joint Committee of Public Accounts and Audit 1998, *General and Specific Purpose Payments to the States*, Report no. 362, June; House of Representatives Standing Committee on Financial Institutions and Public Administration 1998, *Review of the National Competition Council Annual Report 1996-97*, June.

This discussion paper arises in the context of the Council's role in promoting community understanding and informed debate on NCP.

1.3 Extended coverage of Trade Practices Act

The scope of Part IV of the TPA has been expanded to cover virtually all private and public sector business activities.

Broadly speaking, Part IV prohibits a range of anti-competitive trade practices including:

- anti-competitive agreements;
- misuse of market power;
- exclusive dealing;
- resale price maintenance; and
- mergers which have the effect, or likely effect, of substantially lessening competition.

Constitutional limitations had previously prevented application of these provisions to unincorporated businesses, such as legal partnerships, operating solely in one State. Further, it was unclear whether the TPA covered State and Territory government businesses.

To rectify this, governments have enacted a modified version of Part IV, called the *Competition Code*, in each of their jurisdictions. All jurisdictions enacted this legislation in 1996.

1.4 Improving the performance of essential infrastructure

Services such as energy supply, transportation, communications and water supply play a vital role in the Australian economy. They are major business inputs, essential services for consumers, and the industries that supply these services are major resource users in their own right.

NCP takes a two-pronged approach to improving these essential service industries:

- specific National agreements for reforms in the electricity, gas, water and road transport sectors; and
- general 'access' regimes for all infrastructure services.

Energy

The NCP energy reforms are the furthest advanced. They seek to improve the efficiency of the electricity and gas industries, open these markets up to new businesses, and cut costs to energy users.

The *electricity* reforms are among the most ambitious in the NCP package, and aim to develop a national electricity market ultimately covering NSW, Victoria, Queensland, South Australia, Tasmania and the ACT.

A competitive market is currently evolving, with NSW, Victoria, South Australia and the ACT commencing interstate trade from May 1997. Queensland has introduced a parallel competitive market in preparation for interconnecting its power grid with NSW – expected by 2001 – and Tasmania has also announced its intention to interconnect. As part of the reform package, a National Electricity Code has been developed, including access arrangements covering the natural

monopoly transmission and distribution power grid. The ACCC granted approval of the code in October 1998, and the full operation of the national market rules commenced in December 1998 in all south-eastern mainland jurisdictions.

The reforms are creating a competitive wholesale market, in which generators bid for the right to supply the market, and customers compete for the right to buy. This has already occurred in the south-eastern mainland jurisdictions on an individual State basis. However, the introduction of interstate trade is creating more depth than is possible in the individual State markets – where the number of generators and major buyers is relatively small. As Box 2 indicates, the introduction of competition has already produced some significant price reductions, with indications that service standards are being maintained or improved. Given the importance of electricity in the cost structures of many businesses, the reforms are boosting the international competitiveness of Australian export and import-competing industries.

Interstate trade will also help address issues of deficient generating capacity in some States, and excess capacity in others – reducing the risk of overcapitalisation in new power stations.

Similar measures have been implemented in relation to *gas*. The central reform is a National Gas Pipelines Access Code developed by all jurisdictions, and implemented in most States and Territories by 30 June 1998.² The National Code creates a legally enforceable right for people to gain access to the services of natural gas pipelines at fair and reasonable prices. This is an important breakthrough in creating more competitive gas markets as it gives customers greater scope to negotiate with a range of gas suppliers, knowing that it is possible to access a pipeline to carry the gas to the required destination. The added competition is pushing down prices of both gas and gas haulage services (see Box 2).

Although it is still early days, these developments are helping to expand the market for natural gas, fuelling the development of new pipeline proposals to link key gas

² The exceptions are Western Australia, which expected to pass implementation legislation by 30 September 1998, and Tasmania, which does not have a natural gas industry at present.

Box 2 Some recent outcomes of energy reform

- A survey (ACM 1998) of businesses able to select their own electricity supplier under the national market found an average reduction in electricity bills of 30.6 percent in NSW and 23.2 percent in Victoria. While some of these gains were partly reversed late in 1998, those States most exposed to competition remained substantially cheaper electricity suppliers than other jurisdictions (*Australian Financial Review*, Sept 29, 98).
- A similar study of major businesses (Delloite 1998) found that 88 percent had achieved savings of more than 20 percent.
- The Victorian Government reported in June 1997 that from November 1992 to May 1997, a typical Victorian household gained a 9.2 percent real reduction in the cost of electricity; a typical household using electric hot water now spends \$66 less than it would have without the competitive industry. The Government also reported a 47 percent reduction in residential disconnections in the second half of 1996 compared with the same period in 1995.
- Victoria's Office of Regulator General (ORG) reported in 1997 that downtime from blackouts had fallen 50% since 1989-90, meaning that reliability of supply had risen by 50 percent. In 1998, the ORG reported that since privatisation, Victoria's electricity suppliers have generally improved or maintained their services to customers. While results varied between the five distributors, total downtime fell by 9 percent compared to the previous year, and affordability of supply and customer services had improved since 1996.
- After the commencement of the competitive wholesale market in Queensland in March 1998, wholesale electricity prices fell by around 23 percent (QERU 1998).

Box 2 ...cont

- In Western Australia, gas prices fell 50 percent for major industrial users after deregulation of the Pilbara market in 1995 (Barnett 1996); while transport tariffs on the pivotal Dampier-Bunbury pipeline will fall by around 26 percent between 1997 and 2000 under a transitional price path (Moran 1997, Farrant 1998).
- Gas distribution prices in New South Wales are to fall by up to 60 percent in real terms by 2000 under an AGL access undertaking accepted by the New South Wales regulator in 1997 (IPART 1997).

basins with major markets. Two of these proposals – the AGL-Chevron pipeline from Papua New Guinea to Queensland, and the Westcoast pipeline along the south-eastern seaboard – are now well advanced, with significant potential benefits for national and regional economic development.

Similarly, a \$50 million ‘interlink’ pipeline between New South Wales and Victoria was opened in 1998, allowing natural gas trades between the two states for the first time. The National Code was an important factor underlining the viability of the new pipeline, as it created an enforceable right for the pipeline owners and gas producers to access the distribution networks in major markets like Melbourne and Sydney. The pipeline played a vital role in September 1998, when Victorian gas supplies were suspended by the Longford disaster. The interlink allowed emergency supplies of gas to flow into Victoria from interstate throughout the crisis.

Governments are continuing their work with energy reform to ensure that the prospective benefits are reaped Australia-wide. For example:

- electricity price reductions should spread as competitive market arrangements expand to cover small business and households, and as more States join the national market; and

- with significant reform now accomplished or in train in relation to gas transportation, attention is now being given to the 'upstream' sector where there is scope for greater competition between and within gas basins. This can be a difficult issue due to the nature of long-term contracts between suppliers and major customers in many States. The Longford gas disaster illustrates the potential risks stemming from major gas markets relying exclusively on a single supplier. An intergovernmental working group examined 'upstream' issues in 1998 and was due to report to COAG and ANZMEC on reform options in December.

Water

Many of Australia's river systems are in crisis. Outbreaks of blue-green algae, excessive diversions of natural flows, increasing pollution and rising salinity are all taking their toll. Native fish populations, and wetlands and streams have been affected. There are salinity problems in many farming areas such as those in the Murray-Darling Basin,³ and water quality and reliability is at risk in some catchments. At the same time, water has been priced below cost, encouraging overconsumption and discouraging conservation. As the Australian Financial Review recently noted:

Australians are the world's second most voracious and wasteful consumers of water, despite living on the driest inhabited continent... Australians drink less than 5 per cent of the water they use, and nearly 30 per cent (of urban water) is used watering the lawn around the great Australian dream home. (*Australian Financial Review*, August 10 1998).

The NCP water reforms are a direct response to the need to halt the degradation of this natural resource and seek to address both the economic viability and ecological

³ The Murray-Darling Basin covers four states and one territory (Queensland, NSW, Victoria, South Australia and the ACT), supports over 20 cities, has a population of 3 million, and is Australia's most important agricultural region. The Basin produces annual agricultural output exceeding \$10 billion or one-third of national rural output.

sustainability of the nation's water supply through the following measures:

- pricing reform based on principles of consumption-based pricing, full-cost recovery, and removal of cross-subsidies, with remaining subsidies made transparent – encouraging people to use water more wisely by basing their consumption decisions on prices reflecting the actual value of the water they use;
- water allocations or entitlements, including allocations for the environment, coupled with trading in water entitlements – allowing water to flow to those activities bringing maximum benefit to the community;
- improved water quality monitoring and catchment management policies and a renewed focus on landcare practices to protect rivers with high environmental value;
- future investment in dams and other water infrastructure being undertaken only after appraisal indicates it is economically viable and ecologically sustainable – addressing the need for cost-efficient investment with due regard to environmental concerns; and
- structural separation of the roles of service provision from water resource management, standard setting and regulatory enforcement.

The Council believes that the water reforms are among the most significant in the NCP package. Implementation is being phased in over five to seven years, to give people forward notice and time to adjust, and because of the sheer size and complexity of the package.

So far, the scope and pace of reform differs across Australia. Each government is taking a different approach to water reform, and rates of progress vary. New South Wales and Victoria are the furthest advanced. Other governments have implemented fewer reforms, or are still in the process of developing their approach to some areas. Some important recent reforms include:

- the NSW Government introduced water reforms in 1997 and 1998 that target explicit sharing of water between the environment and consumption. The

Government has identified a number of 'stressed rivers' and, for seven key rivers, announced that up to 10 percent of annual diversions would be reserved for the environment. Targets have also been set for 1998-99 to increase native fish breeding and migration, improve bird breeding in wetland areas, suppress algal blooms and provide greater long-term certainty of volumes and water quality for all water users;

- several States have begun the process of bringing water pricing into closer alignment with levels of consumption and the cost of supply. In Queensland, for example, consumers reduced their water use by around 20 per cent in the first year of the new pricing system, bringing significant environmental benefits. Pricing impacts will vary from State to State, depending on the extent of existing subsidies. In Victoria, where reform was already relatively advanced, the price of domestic water fell by 18 per cent in 1998. In NSW, however, prices for bulk water are set to rise over the next two years; and
- on 1 January 1998, a trial interstate water trading project began in the Mallee Region in NSW, Victoria and South Australia. The first permanent interstate trade in water occurred in September 1998. Interstate trading allows water to flow to areas where value-adding is highest, bringing benefits to rural communities (see section 3.5).

Road transport

The NCP program also covers road transport. There is already significant competition in the road transport industry itself, so the reforms are focussing on matters such as national licensing requirements for heavy vehicle operators, road pricing and vehicle standards.

However, progress to date has been slower than initially expected. National implementation has been hampered by difficulties with the 'template legislation' approach that was originally proposed, as well as by the lack of a concrete timetable for reform.

Access

The NCP package includes an ‘access’ regime allowing businesses to use essential infrastructure services at a fair and reasonable price, where this promotes competition in a related market. For example, a transport company may be able to gain access to a rail network and operate its own trains, in competition with the existing train operator.

The Commonwealth, States and Territories have already established access regimes for infrastructure services such as telecommunications networks, gas pipelines and shipping channels, and they are developing others. But for nationally significant infrastructure services not already covered by an access regime, the NCP package creates a generic national regime set out in Part IIIA of the Trade Practices Act.

The Council has a role in recommending the approval of State and Territory access regimes and handling applications from businesses that want to obtain access rights under the national regime. To date, most use of the national arrangements has been in relation to rail transport – the lack until recently of a national approach to rail reform has forced many freight businesses seeking to compete with existing government train operators to use the access provisions. Access to rail infrastructure will encourage greater competition between freight operators and cheaper rail freight charges, bringing significant benefits to rural communities in particular.

The Council has recommended that several services be ‘declared’ for access, although most of these matters have been appealed to the Australian Competition Tribunal. The Tribunal is yet to hand down a decision on a substantive matter.

While delays of this nature are part and parcel of testing a new law, in several cases the threat of declaration appears to have forced the pace of change. For example, following its lodgement of a declaration application with the Council, Futuris was able to negotiate access to the AlintaGas high pressure gas distribution network in Western Australia. Similar outcomes have occurred following the lodgement of appeals.

1.5 Reviewing the merits of anti-competitive legislation

There are many pieces of legislation in Australia which contain provisions that restrict competition. They constrain peoples' choices of what they can buy and who they can buy from.

Often regulations perform a necessary function, such as addressing consumer protection, environmental, and public health and safety issues. But many restrictions have been around for years and often the circumstances of the industry have changed without any independent assessment as to whether the restrictions still serve any useful purpose.

As part of the NCP, governments have agreed to review and – where the restrictions are not in the public interest – reform their laws that constrain businesses from competing for customers. The program covers almost 2000 pieces of legislation. It also entails mechanisms to vet new or amended regulations to ensure that they do not unduly restrict competition.

The guiding principle for reviews is that legislation should not restrict competition *unless* it confers an overall community benefit and its objectives cannot be obtained in other ways.

There has been considerable confusion about this area of NCP in the community. It should be emphasised that NCP does *not* require removing all restrictions on competition. Instead, governments are reviewing laws that prevent businesses from competing freely to check whether they benefit the community as a whole rather than simply advantaging one group at the expense of others. If an independent review finds that a particular law does benefit the community as a whole, and there is no better way to do so, the law should be retained under NCP principles.

The NCP agreements list a range of public interest matters that government have agreed to take into account in assessing the benefits and costs of a restriction,

including the environment, employment, regional effects, consumer interests and the competitiveness of business (see Appendix 1).

Anti-competitive legislation can serve the public interest by, for example, setting appropriate accreditation standards for professional services. But in many cases, allowing more competition can protect consumers from unfair pricing by producers with monopoly power. This is because two or more producers competing for the same customers are more likely to find ways of offering consumers better products, cheaper prices, or both. For instance, after people other than lawyers were allowed to offer conveyancing services in NSW, conveyancing fees fell by 17%.

While the early work in this area of NCP reform revolved around developing review schedules and processes, the pace of undertaking reviews has picked up in the last year. The Council estimates that, as at July 1998, the States and Territories had completed more than 300 reviews with a similar number underway. Some key review areas in 1997-98 included agricultural marketing arrangements, regulation of the professions, restrictions on shop trading hours and liquor licensing and gambling legislation.

However, governments are yet to implement decisions in response to the recommendations of many of the recent reviews, and in cases where governments have implemented changes, there generally has been insufficient time to gauge their precise effects. Box 3 provides an indication of the type of outcomes which can be expected.

Box 3 Some outcomes of early legislation reviews

- Following a review of 250 business licenses in New South Wales that revealed significant overlap and unnecessary regulation, 72 licenses have been abolished (as at 1 January 1998), with a further 13 nominated for possible repeal. In one case, 44 categories have been collapsed into just three.
- In South Australia, a review found that while aspects of the Water Resources Act are restrictive, they generate net benefits by mitigating the risk of environmental degradation and disputes over water usage. It therefore recommended that they be retained.
- In Victoria, a 1997 review of physiotherapy regulations recommended the removal of restrictions on practice, the retention of registration requirements and the introduction of compulsory professional indemnity insurance.

Source: Jurisdictions (1998 legislation review schedule updates and information supplied to the Council).

1.6 Improving the competitiveness of government businesses

Improving the performance of government businesses has been an ongoing focus for all Australian governments since the late 1980s. Many studies and reviews provided widespread evidence of poor performance, including poor capital and labour productivity, overstaffing and excessive use of material inputs,

inappropriate management practices, poor quality goods and services, inappropriate pricing practices and poor financial performance.

Over the last decade, governments have been reforming their significant businesses in three ways:

- by restructuring them;
- by making them compete on an equal footing with private businesses, where this is in the public interest; and
- by monitoring their prices where the businesses retain monopoly power.

In 1995, these reforms were brought within the ambit of National Competition Policy. The early outcomes of reform are indicated in Box 4.

Box 4 Recent performance of government businesses

The Steering Committee on National Performance Monitoring of Government Trading Enterprises (1997) found improvements in the performance of government businesses over the four years to 1995-96. While the outcomes have varied between the enterprises studied, overall there were:

- improvements in labour productivity;
- a doubling of total payments to governments;
- average price reductions of around 15 percent; and
- some improvements in service quality.

The Steering Committee's October 1998 Report found that these trends were sustained over the period to 1996-97. The Report noted substantial price reductions for most Government Trading Enterprise (GTE) services, particularly electricity, port, telecommunications and air traffic services.

Box 4 ...cont

At the same time, the Report noted that the quality of services appears to have been maintained or increased for most GTEs in the period under review.

While significant price reductions occurred for residential services, some of the biggest reductions – for example in water and electricity – were experienced by business users. This is to be expected as some NCP reforms involve redressing previously existing cross-subsidies by reducing prices for business at a faster rate than those for household consumers. But these benefits to business also assist consumers – when reduced costs to firms are passed on to households through lower prices for goods and services.

Structural reform

Where a publicly owned business has developed into an integrated monopoly, there may not be sufficient incentives for the business to provide value for money services. One way to address this problem is for governments to consider structural reform of the monopoly. The NCP agreements call for a review of a public monopoly's structure whenever a government wishes to introduce competition to a market, or to privatise the monopoly. The review is aimed at determining the appropriate structure of the business to best serve the public interest, and takes account of a wide range of economic, social and environmental issues, including the best way of funding and delivering any mandated community service obligations.

It should be noted that NCP requires governments to examine structural reform only if a decision has already been made to introduce competition or to privatise a monopoly – but privatisation is not, in itself, required. The structural reform principles in NCP are neutral on the question of private versus public ownership.

Box 5 Privatisation

NCP does not require privatisation of any government business. The NCP agreements leave it to governments to determine whether privatisation is warranted in any particular circumstance. Where a government chooses to privatise a public monopoly, the NCP reforms require the government to undertake a review first to ensure, among other things, that the right competitive environment is in place for privatisation.

Hence, any decision by governments to privatise a public asset reflects a policy decision of the government in question — not a requirement of NCP.

That said, privatisation *is* one way (of several) by which governments can meet some of their obligations under the NCP agreements. For example, it can be one option for applying ‘competitive neutrality’ to significant government business activities (see below).

In addition, the Council recognises that NCP can sometimes result in governments giving stronger consideration to privatising certain businesses. For example, the introduction of competition may require a government business to undertake new investment to compete effectively in the market. In some cases, governments may have higher priorities for taxpayer funds. The high cost of upgrading the aircraft fleet, for instance, was one consideration underlying the privatisation of Qantas.

However, it is still up to individual governments to decide whether privatisation is warranted, and there will be cases in which it is unlikely to be. Privatising any particular publicly-owned business may or may not confer an overall community benefit. Consequently, the merits of privatising businesses need to be assessed on a case-by-case basis.

Structural reform of a public monopoly can advance the public interest for two reasons:

- some public monopolies have responsibilities for regulating technical aspects of an industry, as well as providing services that are subject to or affected by those regulations. In a competitive environment, such a dual role creates a potential conflict of interest.
- where privatisation of a public monopoly is contemplated, structural reform may be required to ensure that anti-competitive arrangements are not entrenched under private ownership.

Australian Governments have undertaken wide-ranging structural change of their big, monopolistic enterprises in the 1990s. As noted earlier, structural reform is an important part of the electricity, gas and water reforms. To quote other examples:

- New South Wales has broken up its State Rail Authority into seven smaller entities, each specialising in a particular facet of rail operations; and
- Victoria has restructured its port operations, putting responsibility for shipping channels in one body, and other wharf functions – which are amenable to competition from private businesses – elsewhere.

Competitive neutrality

‘Competitive neutrality’ measures seek to ensure that competition between public and private businesses happens on a fair basis, by making sure they face the same taxes, incentives and regulations. ‘Corporatisation’, ‘commercialization’ and ‘full cost pricing’ are some ways competitive neutrality can be introduced into government businesses. Under NCP, the application of competitive neutrality reforms to a particular government business is subject to a public interest test, taking into account relevant social, economic and environmental considerations (see Appendix 1).

Competitive neutrality reform can help governments and the community gain better value for money in service provision. Corporatisation or commercialisation can inject a government business with a sharper focus on customer needs and competitive pricing. Similarly, where governments provide services through competitive tendering, competitive neutrality helps ensure that the bids of each party are comparable. For example, without competitive neutrality, an 'in house' bidder could enjoy an unfair advantage over external contractors because of tax exemptions or access to various corporate overheads free of charge. Conversely, this 'bias' may favour external contractors in some cases. For example, an 'in house' bidder could be disadvantaged in a tender because of responsibilities to provide community service obligations.

But if competitive neutrality is applied, any advantages and disadvantages enjoyed by 'in house' bidders are made transparent and factored into the selection process to ensure that all tenders are considered on their merits. If this occurs, governments are in a better position to choose options that make the best use of taxpayers' money and deliver the best quality services.

To date, governments have corporatised or commercialised many of their businesses, and are progressively introducing pricing reforms to many others. Further, all governments have also established units to deal with any complaints about unfair advantages enjoyed by particular government businesses, as is required under the NCP agreements.

While the most significant benefits from competitive neutrality reform are likely to come from reforming the larger state-owned enterprises, local communities may also benefit from reforms which enable local governments to get better value for money from the rate base.

At the same time, there are often significant public interest considerations associated with local governments, particularly in remote locations. In these areas, regional development and employment factors can sometimes mean that the social and economic cost of introducing competitive neutrality may outweigh benefits arising from increased competition between public and private providers. This may sometimes point to reform being contrary to the public interest in rural and remote areas. But this is a matter which should be put to objective assessment

to determine the merits of the argument, rather than being the subject of an automatic exemption (see section 3.2).

Box 6 Competitive tendering and contracting out

Competitive tendering and contracting out are not requirements under NCP. As is the case with privatisation, any decision to provide government services through a tendering process is a policy decision for the government in question.

Many governments are choosing to provide a range of services through competitive tendering processes to improve value for money and quality of delivery. Where this occurs, it is important that the NCP requirement of competitive neutrality be first applied to ensure that the tender process is fair and delivers accurate signals to governments

It is important to note that competitive tendering does not necessarily mean contracting out – it can also be used as an approach to improve the quality of ‘in-house’ service provision. For example, prior to putting some of their functions to a competitive tendering process, some government bodies in Queensland and Victoria have provided training for their staff who undertook the relevant functions. This provided the staff with a better opportunity to win the work in open competition with the private sector or other government suppliers (see section 3.2).

Price monitoring

In some cases, reforms such as reviewing regulatory barriers to entry, competitive neutrality and structural reform may be insufficient to guarantee effective competition. This may occur, for example, where reforms need to be phased in over a period of time, or where important parts of the market remain largely dominated by a single firm.

Where government businesses retain monopoly power, the NCP calls on governments to consider subjecting them to independent prices oversight. All States and Territories, except Western Australia and the Northern Territory, have established independent prices oversight arrangements, and several government businesses are currently subject to prices oversight.

1.7 The broader policy mix

Competition policy can play a major role in enhancing the performance of the economy. Its strength lies in improving productivity and economic efficiency. This can directly improve people's material living standards and, in conjunction with other measures, enable the attainment of the community's social and environmental goals.

But while NCP is explicitly tailored to serve the public interest, competition policy should be seen as just one plank in a platform of policies to secure Australians' wellbeing and help us deal with our changing economic circumstances. Other policies – such as tax, social security, community services and labour market programs – also play a critical role in ensuring that the potential benefits of reform are realised in full and shared equitably.

The relationship between NCP and other areas of government policy is a theme examined more fully in the following sections of this paper.