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**COMPETITION POLICY: HILMER,  
GOVERNMENTS AND BUSINESS**

**BACKGROUND INFORMATION BRIEF NO 30**

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## **ABSTRACT**

*The Hilmer Report of August 1993 presented wide-ranging recommendations on the development of a National Competition Policy. The primary focus of the recommendations was to broaden the scope of competition policy to include all government and private businesses, including the professions, and to minimise exemptions. In April 1995, the Council of Australian Governments (COAG) adopted the general thrust of the recommendations and agreed on specific financial and co-operative arrangements between the Commonwealth and the States and Territories to facilitate the policy reforms.*

*This Information Brief describes the Hilmer reforms and the COAG agreements, and overviews the reactions to them. Predictions of the implications for various sectors of the Australian and Queensland economies are also presented.*

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## 1. INTRODUCTION

Competitiveness in the Australian economy has been enhanced by several major initiatives in recent years. The latest was at the meeting of the Council of Australian Governments (COAG) in Canberra in April 1995, which endorsed a package of reforms and agreements based on the recommendations of the "Hilmer Report" of August 1993. In the introduction to the Competition Policy Reform Bill, a key element of the reform package, the Commonwealth Government indicated the importance of the reforms as follows:

*Implementing this policy is the most important single development in micro-economic reform in recent years. Ultimately, the ability of the economy to grow, to provide jobs and an improved standard of living, depends upon how well the productive potential of the economy is employed and enhanced.<sup>1</sup>*

The communique of the COAG meeting was similarly positive about the economic outcomes of the reforms, but also highlighted broader benefits to the community and the Australian federation:

*In a spirit of co-operation Heads of Government have signed major agreements that will boost the competitiveness and growth prospects of the national economy and improve the effectiveness of public housing and health and community services so they better meet the needs of clients. As a result, the Australian federation will be economically stronger and more equitable as it approaches its centenary in 2001.<sup>2</sup>*

Press commentary after the COAG meeting largely reflected the optimism of the official statements.<sup>3</sup>

The reference to the federation is a reminder that the COAG decisions represent not just choices about competition policy, but also the evolving character of Australian federalism. The competition policy reform outcome provides an illustration of the interplay between the Commonwealth and the States and Territories, and to a lesser

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<sup>1</sup> Australia. Parliament. Senate. *Competition Policy Reform Bill, Second Reading Speech*, Canberra, 1995.

<sup>2</sup> Council of Australian Governments, *Communique*, COAG Meeting, 11 April 1995, Canberra.

<sup>3</sup> For example, Brook Turner and Tom Burton, 'Borderless nation', *Australian Financial Review*, 12 April 1995, pp.1,4; Tim Colebatch, 'Deal is done for era of competition', *Age*, 12 April 1995, p.1.

extent Local Government, on an issue which has national application and significance but considerable State responsibility and authority.

According to Glyn Davis, the current micro-economic reform agenda was initiated in response to the "banana republic" statement of the mid 1980s<sup>4</sup>. A more specific progenitor of the Hilmer inquiry was the Prime Minister's *One Nation* statement of February 1992. The statement called for continued reform to expose the Australian economy to greater competition, with emphasis on the aviation, electricity and finance industries.<sup>5</sup> Over the course of 1992, negotiations were conducted with the States to secure agreement for a broad inquiry into National Competition Policy. The inquiry was established in October 1992, chaired by Professor Fred Hilmer, Director of the Australian Graduate School of Management at the University of New South Wales. Although formal endorsement by the States was not secured<sup>6</sup>, four principles were agreed to, on which the inquiry was based (see Section 2.1).

As indicated above, the National Competition Policy envisaged in the Hilmer report and the agreements signed by COAG are predicted to have a substantial net positive impact on the Australian economy. Certain sectors of the economy that have until now been monopolistic or protected from competition in other ways should be extensively transformed. Key examples are government enterprises and the professions.

This Information Brief provides an overview of the issues of competition and competitiveness in Australia, with a focus on the recommendations of the Hilmer Report and the reform proposals adopted by COAG. Four main sections follow. Section 2 briefly outlines the conclusions and key recommendations of the Hilmer report. Section 3 reviews some of the reactions to and commentaries on the report. Section 4 describes the reform package agreed to by the Council of Australian Governments in April 1995, and reactions to that decision. Finally, Section 5 considers some of the specific implications for Queensland.

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<sup>4</sup> Glyn Davis, 'Introduction to the Competition Policy Reforms', Proceedings, *National Competition Policy Seminar*, Brisbane, 8 June 1995, p.1.

<sup>5</sup> Hon Paul Keating MP, *One Nation*, AGPS, Canberra, 1992.

<sup>6</sup> Rowley Spiers, 'Inquiry targets State cartels', *Australian Financial Review*, 5 October 1992, pp.1,2.

## 2. THE HILMER REPORT

The Hilmer Report, correctly titled *National Competition Policy: Report by the Independent Committee of Inquiry*<sup>7</sup>, was released in August 1993. The members of the Committee were Professor Fred Hilmer (Chairman), Mr Mark Rayner, a Director of CRA Ltd, and Mr Geoffrey Taperell, an international partner of the legal firm Baker and McKenzie.

### 2.1 TERMS OF REFERENCE

The Terms of Reference announced by the Prime Minister included five elements:

- a statement of four principles on which national competition policy was to be based (see below),
- a requirement to report on the means of applying the principles of national competition policy, particularly in relation to anti-competitive conduct, other market behaviour, and the *Trade Practices Act 1974* (Cth) (TPA),
- several matters to be considered by the Committee, including regulation of government business enterprises, interests of consumers, and the role of various provisions of the TPA,
- other matters to be taken into account, including aspects of government business enterprises, and procedural matters, and
- a deadline of May 1993, later extended to August 1993.

The full text of the Terms of Reference is included as Appendix A.

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<sup>7</sup> F.G. Hilmer, M.R. Rayner and G.Q. Taperell, *National Competition Policy: Report by the Independent Committee of Inquiry*, AGPS, Canberra, 1993.

The four principles provided to the inquiry in the terms of reference were as follows:

- *no participant in the market should be able to engage in anti-competitive conduct against the public interest,*
- *as far as possible, universal and uniformly applied rules of market conduct should apply to all market participants regardless of the form of business ownership,*
- *conduct with anti-competitive potential said to be in the public interest should be assessed by an appropriate transparent assessment process, with provision for review, to demonstrate the nature and incidence of the public costs and benefits claimed, and*
- *any changes to the coverage or nature of competition policy should be consistent with, and support, the general thrust of reforms:*
  - (i) *to develop an open, integrated domestic market for goods and services by removing unnecessary barriers to trade and competition; and*
  - (ii) *in recognition of the increasingly national operation of markets, to reduce complexity and eliminate administrative duplication.*

As required, the inquiry incorporated these principles in the conclusions and recommendations of their report.

## **2.2 DEFINITIONS: COMPETITION AND COMPETITION POLICY**

The Committee adopted a definition of **competition** originally proposed by F.G. Dennis: Competition is the *striving or potential striving of two or more persons or organisations against one another for the same or related objects*<sup>8</sup>. The reference to potential striving means that a firm is likely to act in a competitive way in a readily accessible market, even when there is no actual competition, because non-competitive behaviour will induce other firms to enter the market. Note also that the objects of competition do not have to be identical, only related. Thus competition will occur between firms who provide mixes of benefits and products which substitute for others, or which differ in such aspects as volume, quality, price, warranty, and/or associated advice or repair services.

The Committee noted that **competition policy** has traditionally been defined narrowly. Competition policy has been thought of as simply the formal rules governing the anti-

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<sup>8</sup> *National Competition Policy*, p.2.



competitive conduct of firms. In Australia's case, these are found primarily in Part IV of the TPA.

However the Committee adopted a broad view:

*In its broadest sense, competition policy encompasses all policy dealing with the extent and nature of competition in the economy. It permeates a large body of legislation and government actions that influence permissible competitive behaviour by firms, the capacity of firms to contest particular economic activities and differences in the regulatory regimes faced by firms competing in the one market.<sup>9</sup>*

In society, competition affects economic efficiency and other social goals. Competition policy is not simply the promotion of competition. There may be situations where economic efficiency and/or certain social goals are best served by specific limits on competitive freedoms.

Economic efficiency enhances community welfare by increasing the productive base of the economy, and providing higher returns to producers and higher wages. Economic efficiency has three main components that are enhanced by competition:

- Technical or productive efficiency, through practices aimed at minimising the costs of producing goods and services. Examples include improvements in managerial performance, work practices, and the use of material inputs.
- Allocative efficiency, through modifying the use of resources to produce the greatest benefit relative to costs. Firms that can use particular resources more productively are able to capture them from other firms.
- Dynamic efficiency, through reform and innovation in products and processes. Examples include effective investment in research and development leading to new designs or products, and reforms in management structures and strategies.<sup>10</sup>

Competition may also enhance other, non-economic social goals. For example, firms may be keen to be known as non-discriminatory, non-polluting, or supportive of special community interests. On the other hand, competition policy may restrict competition in certain instances in order to fulfil social goals. For example, supply of services may be regulated so that those living in remote communities can receive services without being overwhelmed by the actual costs involved.

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<sup>9</sup> *National Competition Policy*, p.6.

<sup>10</sup> *National Competition Policy*, p.4.

The Committee's recommendations for a National Competition Policy were based on six key elements. These are listed in the table below and described more fully in Section 2.3.

**Table 1. The Six Recommended Elements of a National Competition Policy**

POLICY ELEMENT	EXAMPLES AND CURRENT APPROACHES <sup>a</sup>
1. Limiting anti-competitive conduct of firms	Competitive conduct rules in Part IV of the Trade Practices Act, but with numerous exemptions.
2. Reforming regulation which unjustifiably restricts competition	Reviews by individual governments without a systematic, national focus, eg deregulation of domestic aviation, egg marketing and telecommunications.
3. Reforming the structure of public monopolies to facilitate competition	Mostly examined on a case-by-case basis by individual governments, eg electricity utilities; recent inter-governmental work on electricity and rail.
4. Providing third-party access to certain facilities that are essential for effective competition	Some arrangements in place or being developed on an industry-specific basis (eg telecommunications); no general mechanism capable of effectively dealing with these issues across the economy.
5. Restraining monopoly pricing behaviour	Surveillance of declared firms' prices under the Prices Surveillance Act (Cth) with important exemptions; various mechanisms in the States and Territories.
6. Fostering "competitive neutrality" between government and private businesses when they compete	Largely addressed on an ad hoc basis by individual governments; increasing moves towards corporatisation but on disparate models. Examples include requirements for government businesses to make tax-equivalent payments.

a: That is, approaches current at the time the report was prepared.

Source: *National Competition Policy*, pp.xvii,7.

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## 2.3 KEY FINDINGS OF THE REPORT - SIX ELEMENTS OF COMPETITION POLICY

### 2.3.1 Competitive Conduct Rules

The "rules" governing competitive conduct are primarily the provisions of Part IV of the TPA. The Committee was asked to review the Act in relation to these provisions, including those relating to exemptions. The review of the rules occupied a major section (Part I) of the report. This section of the report is summarised here under four headings: the content of the rules, exemptions from the rules, the impact of the rules on specific sectors of the economy, and enforcement of the rules.

#### *Content of the Rules*

In broad terms, the rules prevent anti-competitive conduct in two ways: by either a blanket (*per se*) prohibition of certain conduct, or by disallowing conduct based on a test of whether or not its effect is sufficiently serious, for example if it "substantially lessens competition". The Committee recommended that the current rules be retained as the basis for the national competition policy, with some amendments to strengthen or standardise them. The primary areas of amendment recommended were<sup>11</sup>:

- Prohibiting price fixing arrangements for services, (currently prohibited for goods only), and removing other unjustified distinctions between goods and services,
- Relaxing the prohibition of "third-line forcing" (ie, requiring that a third party's product be bought in conjunction with the seller's product), so that it be disallowed only if it "substantially lessens competition", which would be consistent with the treatment of other forms of exclusive dealing (ie, tying sales of two or more products so that one may only be bought if others are also bought),
- Maintaining the prohibition of "resale price maintenance" (where a supplier requires retailers to sell at or above a minimum price), but allowing exceptions to be authorised when a net public benefit can be demonstrated, and
- Repealing the specific prohibition on price discrimination (selling like goods to different persons at different prices). For example, a bulk purchaser cannot be offered a discounted price. The provision provided a possible

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<sup>11</sup> *National Competition Policy*, p.xxiii.

protection to small business, but there was no evidence that it was effective in practice. The Committee considered the current provision to be vague (eg, the definition of "like" is unclear), and its benefits dubious. Some practices of this type may still be outlawed under existing provisions which prohibit the misuse of market power.

### ***Exemptions From the Rules***

The TPA contains several sources of exemptions to the competitive conduct rules. The Committee recommended retaining the following, with limitations on their use<sup>12</sup>:

- **Authorisations by the Trade Practices Commission (TPC) or its successor.** This should be the primary source of exemptions to the rules. To be approved, a public benefit must be demonstrated. Economic efficiency should be the primary consideration in assessing public benefit.
- **Specific Exemptions in the TPA.** The current limited exemptions for labour agreements, standards, restrictive covenants, export contracts and consumer boycotts should be retained, while those for intellectual property and overseas shipping should be reviewed separately by other bodies.
- **Other Commonwealth Legislation.** The TPA permits other Commonwealth legislation to specifically authorise conduct outlawed by the TPA. This authority should be limited to statutes only (not regulations).

The Committee recommended repealing or severely curtailing the other sources of exemptions:

- **Regulations made under the TPA.** None are currently in force and this power should only be used only for urgent, temporary protection.
- **State or Territory legislation.** The TPA permits State and Territory legislation to authorise conduct that would otherwise contravene the Act. The Committee did not think this appropriate in the context of a national policy. In practice, most State laws with anti-competitive effects do not operate by authorising conduct outlawed by the TPA, so repealing this provision will not have a large immediate impact.
- **Shield of the Crown Doctrine.** A statute will only bind the Crown by express words or necessary implication. The TPA binds Commonwealth agencies when they engage in business. State and Territory bodies are not specifically bound. The provision should be amended to apply to State and

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<sup>12</sup> *National Competition Policy*, p.120.

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Territory bodies, and to commercial transactions between government businesses which are in actual or potential competition with private firms.

- **Constitutional Limitations.** Currently, a non-corporate business operating in one state only may escape the operation of the TPA, because the constitution quarantines such businesses from the ambit of Commonwealth legislation on trade and commerce. Any national competition policy should be made to apply to such businesses.

### ***Impact on Specific Sectors***

The Report discusses the impact of its recommendations on 12 specific sectors of the economy. These are government-owned businesses, professions, other unincorporated businesses, agricultural marketing, overseas shipping, intellectual property, labour, approved standards, export contracts, restrictive covenants, consumer boycotts, and conduct or arrangements pursuant to international agreements. A brief summary of the comments in the report is provided here.

#### **(a) Government-Owned Businesses**

Commonwealth business units are already subject to the TPA, except for transactions between agencies. The Committee recommended that this distinction be removed. They noted that "This may require some Commonwealth entities to review their current business practices, but is not expected to involve any significant transitional arrangements"<sup>13</sup>.

The impact on State and Territory Government enterprises will be greater as they will come under the ambit of the TPA for the first time. The Committee noted that rail, electricity, gas and water utilities account for nearly 5% of national GDP. Efficiency measures could increase this by two percentage points, or \$8 billion per annum (an Industry Commission estimate), in part through the removal of regulatory arrangements that shield these businesses from competition.<sup>14</sup>

The Committee has not recommended a blanket removal of regulatory protections. A government may still protect community service obligations or other objectives by, for example, creating or maintaining a statutory monopoly with legislated exemptions from competition rules, such as for pricing arrangements. However such a move would have to be justified by a public interest test and in all other respects such businesses would be required to observe the national standards of competitive conduct.

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<sup>13</sup> *National Competition Policy*, p.126.

<sup>14</sup> *National Competition Policy*, p.129.

**(b) Professions**

The TPA does not contain a blanket exemption from its anti-competitive provisions for members of the professions, but most are not covered by the Act for various other reasons. These include being in non-corporate entities (eg, partnerships) and not trading across state borders or internationally, being exempted by State or Territory legislation, or having specific exemptions authorised by the TPC. Professions which have been granted authorisation by the TPC include pharmacists, architects, metallurgists, lawyers and doctors.

The Committee recommended that the application of the competitive conduct rules to the professions be extended by:

- extending the coverage of the TPA to all non-incorporated businesses, and
- discontinuing exemptions based on State and Territory laws.

Statutory restrictions on practice, for example through licensing requirements, would not be affected. Neither would any self-regulation of ethical or other standards. However any rules of professional associations that had the effect of substantially lessening competition would be prohibited under the TPA. Individual professional organisations wishing to retain any such rules would have to seek specific authorisation from the TPC and would have to demonstrate that the anti-competitive rule resulted in a net public benefit.

**(c) Other Unincorporated Businesses**

Because of constitutional limitations, the TPA does not reach unincorporated businesses such as partnerships that operate in a State and are not engaged in interstate or overseas trade, or do not supply the Commonwealth. The Committee argued that no business should be exempt from competitive conduct rules simply on the basis of its legal form.

**(d) Agricultural Marketing**

A broad range of statutory schemes for the marketing of agricultural products exists in Australia. These schemes may include such practices as price control, production controls, compulsory acquisition and monopoly marketing arrangements. The Committee argued that these schemes often lead to inefficient production (by world standards), higher prices to consumers, and restrictions on the development of value-added industries in Australia.

The recommendations covering removal of constitutional protection (for non-corporate, intra-state businesses), removal of Shield of the Crown exemptions, and discontinuance of exemptions based on State and Territory laws, all apply to agricultural marketing organisations, so that they will be required to comply with the competitive conduct rules. Statutory schemes will not be affected, but the number of these is expected to decrease over time. Specific conduct that requires exemption from the TPA may still be authorised by the TPC (or any replacement body), provided the public interest test can be satisfied.

**(e) Overseas Shipping**

International shipping enjoys various exemptions from competitive conduct rules under Part X of the TPA. The Committee did not make a recommendation on this topic because Part X was being reviewed separately. However they doubted that the exemptions could be justified, and suggested that the onus should be on those supporting their continuation to demonstrate that they would yield a net public benefit.

**(f) Intellectual Property**

The TPA provides a limited exemption which allows the owner of certain intellectual property rights to assign or licence those rights in order to retain control over them. Such restrictive assignment or licensing would otherwise contravene the Act. The scope of the exemption varies between forms of intellectual property such as patents, trademarks, designs, copyright and circuit layouts.

The Committee saw advantages and disadvantages in the principle of limited restrictions on the transfer of intellectual property rights. However they reached no definite conclusion and recommended that the question be considered by an expert committee.

**(g) Labour**

The TPA provides an exemption for any act or agreement relating to conditions of employment including remuneration, working hours and working conditions. These could be considered to be anti-competitive or even price-fixing, and thus contravene several provisions of the Act. This exemption could not be altered without a dramatic overhaul of the Australian industrial relations system and the Committee understandably recommended no changes.

**(h) Approved Standards**

The TPA provides an exemption which permits a contract or agreement to require the application of, or compliance with, a standard of the Standards Association of Australia or another prescribed body. Standards may enhance efficiency in several ways: by making products more substitutable, by facilitating development of service industries and/or by assisting consumers in their choices. On the other hand, standards could conceivably be used to reduce competition, by stipulating the use of particular products or technologies. The Committee was not informed of any anti-competitive use of standards in current practice, and on that basis recommended retention of the exemption.

**(i) Export Contracts**

The TPA exempts provisions of contracts relating to exports from Australia or the supply of services outside Australia. Full details must be provided to the TPC within 14 days of the making of the contract. The exemption does not cover export of goods by sea, which is covered by Part X of the TPA (see (e) above). The Committee recommended no change to this exemption.

**(j) Restrictive Covenants**

Restrictive covenants are provisions in agreements that limit a party from certain competitive conduct against another party. Usually the parties are or have been



contractually related in some way. In general, restrictive covenants are covered by common law. The TPA specifically permits three types of restrictive covenants: those restricting the work that a person may engage in during or after a contract; those restricting competition between partners during or after termination of a partnership; and those restricting the seller of a business from certain competition against the new owner. The Committee supported the retention of these provisions.

#### **(k) Consumer Boycotts**

The TPA exempts consumer boycotts against the suppliers of goods or services, providing they are not carried out in the course of trade and commerce. The Committee received no submissions on this topic and proposed no changes to the current provision.

#### **(l) Conduct or Arrangements Pursuant to International Agreements**

The TPA allows regulations to be made to exclude from the Act conduct or arrangements in agreements between the Governments of Australia and another country. No such regulations have ever been made and the Committee recommended repeal of this provision. If any requirement arises in the future, the Commonwealth could seek an authorisation from the TPC or its successor, or pass specific legislation.

#### ***Enforcement***

The enforcement provisions in the TPA include penalties, injunctions, orders for divestiture of assets or parts of a business, damages, declarations by a court concerning rules or practice, court orders, and orders relating to prices.

The Committee recommended that the current provisions continue to provide the basis for enforcement of the requirements of the national competition policy.

### 2.3.2 Regulatory Restrictions on Competition

The Committee report states bluntly that "The greatest impediment to enhanced competition in many key sectors of the economy are restrictions imposed by government regulation or through government ownership"<sup>15</sup>. The two broad forms of anti-competitive regulation are those that restrict market entry and those that restrict competitive conduct. The most obvious restriction to market entry is a statutory monopoly. Others include restrictions on the number of suppliers, the qualifications of suppliers, or the origin of goods or of service providers. Restrictions on competitive conduct can take many forms, and several examples have been given earlier.

The Committee recommended that regulatory restrictions on competition should only be allowed when there is a clearly demonstrated public benefit. This is a reversal of typical current practice, because the onus of proof now falls on those advocating the removal of regulatory controls which have built up over the years.

The Committee proposed four principles to govern the role of regulatory restrictions in national competition policy. These are presented in full in Appendix B. Briefly, these state that regulations which may restrict competition must be demonstrated to be in the public interest. Proposed benefits must be shown to outweigh the likely costs. All such existing regulations should be reviewed in a public process by an independent body. Any new regulation should be rigorously vindicated, and should have a sunset provision. In all cases, the economy-wide impact of regulations should be considered.

Having agreed to the principles, individual governments should be responsible for implementing them within their own jurisdiction. The Committee recommended that the Commonwealth should not have power to override offending state regulations, but that this option may be a fall-back position for the future if the co-operative approach failed. A proposed new body - the National Competition Council (NCC) - will undertake economy-wide reviews of regulatory issues, offer advice and assistance to state bodies, and seek to ensure national consistency. The proposed Australian Competition Commission (successor to the TPC) will also have a role in regulatory review in collaboration with the NCC (see Section 2.4).

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<sup>15</sup> *National Competition Policy*, p.184.

### 2.3.3 Structural Reform of Public Monopolies

Regulatory reform alone will not be sufficient to introduce a new era of competition into entrenched public monopolies. The Committee also recommended structural reform in three key areas:

- The separation of regulatory and commercial functions,
- The separation of natural monopoly and potentially competitive activities, and
- The separation of potentially competitive activities.

Many public agencies undertake a combination of regulatory and commercial functions. For example, an electricity authority may be responsible for formulating and supervising the regulations which control the industry, and may also be a provider of electricity under conditions stipulated by those regulations. It may be possible to avoid a regulator by replacing regulations with industry codes of practice. However if a regulator is necessary it should operate independently of any provider of goods or services, and of direct government control.

In relation to the second area, natural monopolies occur when an entire market is most economically serviced by a single organisation. An example is electricity distribution, because of the structure of the single grid. By contrast, electricity generation may be undertaken by multiple, competing organisations. Separating the two types of activity will enhance competition for two possible reasons. Firstly, when the two activities occur in the one organisation, returns from monopoly operations may be used to cross-subsidise potentially competitive activities. Secondly, control over access to the monopoly activity may be used to unfair advantage in the competitive activity.

The third area above, separation of potentially competitive activities, refers to the subdivision of organisations that conduct more than one commercial activity, into separate business entities. Fragmenting the market power of the combined organisation should facilitate the entry of new, smaller or more specialised firms. In practice, the justification for structural reform will vary on a case by case basis, depending on the balance between the potential costs and benefits of restructuring.

The Committee set out four principles to underpin national competition policy in relation to structural reform of public monopolies. These are reproduced in Appendix C. Briefly, these are that prior to the introduction of competition, regulatory responsibilities should be removed from the incumbent organisation, and that the costs and benefits of separating any potentially competitive activities or of privatisation should be examined in a "rigorous, open and independent study"<sup>16</sup>.

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<sup>16</sup> *National Competition Policy*, p.230.

### **2.3.4 Access to "Essential Facilities"**

Essential facilities are items of infrastructure that cannot be efficiently duplicated as a means of facilitating competition, usually because they are large or extensive. Most are or were originally in public ownership, for example electricity transmission grids, telephone exchange networks, railway networks and airports. These facilities are monopolies which give their owners potential anti-competitive advantages. Providing access to these facilities for competitors may therefore result in gains in efficiency. However, an important principle of business conduct is that firms are free to contract with whoever they choose and cannot be forced to make their facilities available to competitors. Exceptions to this principle should require a strong demonstration of public benefit.

The Committee recommended that legislated right of access to essential facilities should be available, subject to a test of public benefit. Access should be available only on a declaration by the responsible Commonwealth Minister. A declaration could only be made with the consent of the owner of the facility, or, in the absence of the owner's consent, on the recommendation of the NCC.

The NCC may only recommend that the Minister declare access if certain conditions are met. Conditions include that access to the facility must be essential to permit effective competition in a downstream or upstream activity, and that the declaration must be in the public interest, considering the significance of the industry nationally, and the expected impact of the competition engendered. The declaration must also protect the legitimate interests of the owner of the facility by establishing terms and conditions which are fair and reasonable, including the principles on which an access fee would be negotiated.

This proposal has implications for State and Territory Governments in relation to impacts on revenue, community service obligations, and sovereignty. The Committee concluded that transitional arrangements may be necessary to lessen the impact of revenue losses, and these should be reviewed by the NCC. However the loss of revenue was not expected to be large, unless revenue had been inflated by monopolistic practices, in which case there would be economy-wide advantages to its return to competitive levels.

In relation to community service obligations, the Committee recommended that alternative sources of funding be considered for these. Options include direct budget funding or levies on all market participants, perhaps as a condition of access to essential facilities. In relation to sovereignty, the Committee considered the situation where a state may be reluctant to allow access to an essential facility under its control. While a co-operative approach is always preferable, unilateral action by the Commonwealth to force an issue may be justified in circumstances of high national priority.

### **2.3.5 Monopoly Pricing**

Monopoly pricing refers to the situation where a firm takes advantage of a legislated or natural monopoly, or an otherwise poorly contestable market, to charge higher prices than would occur in a normal competitive situation. The Committee recommended that a prices oversight process be established as part of national competition policy.

The process would apply in specific monopoly pricing circumstances. It would be initiated by a declaration by the Commonwealth Minister in relation to a specific firm, but only if the firm agrees or if the declaration has been recommended by the NCC. Before making a recommendation, the NCC must determine that the firm has substantial market power in a substantial market in Australia, and must conduct a public inquiry.

Prices oversight should be conducted by the ACC and be limited to monitoring and surveillance. Monitoring requires the firm to provide cost and price data at regular intervals. Surveillance requires the firm to provide data and also to seek the ACC's non-binding recommendation on prices.

In principle, the process should apply equally to government and non-government businesses. In practice, state governments have the same concerns as outlined in Section 2.3.4 - revenue loss, funding of community service obligations, and sovereignty. Again, the Committee recommended voluntary controls and co-operation between governments as the preferred way of overcoming potential problems in this area.

### **2.3.6 Competitive Neutrality**

The issue here is that regulatory or other requirements may give particular firms competitive advantages that cannot be justified by any of the principles of competition policy. This applies most often to government-owned businesses, whose advantages may include tax exemption or immunities from compliance with statutory requirements. Government-owned businesses may also bear competitive disadvantages, such as accountability obligations (eg, Freedom of Information requirements), community service obligations, and centrally-regulated wage and superannuation levels.

The Committee proposed three principles for competitive neutrality issues in competition policy. These are presented in Appendix D. Briefly, they state that government-owned businesses should not enjoy any net competitive advantage because of their ownership, and any factors causing such an advantage should be neutralised. A transition period of a year should apply in traditional markets, but not in new markets. The preferred means of achieving competitive neutrality is corporatisation.

## **2.4 INSTITUTIONAL PROPOSALS**

The Committee recommended that two institutions be established to oversee and facilitate the implementation of its recommendations.

### **2.4.1 National Competition Council**

The proposed NCC is an independent analytical, advisory and co-ordinating body to be created jointly by Commonwealth, State and Territory Governments. It would consist of a full-time chairperson and up to four other members, supported by a small secretariat. The report lists six key characteristics of the proposed NCC. In summary, they are:

- its functions would be purely advisory (although the recommendation of the NCC would be required in cases of proposed unilateral action by a Commonwealth Minister),
- it would be independent of government,
- it would take an integrated, economy-wide view of competition policy matters, and could draw on industry-specific expertise when required,

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- it would take a pragmatic, business-like approach, focussing on specific practical reforms, and would consider transitional issues arising from its recommendations,
  - it would operate through open processes, with input from all affected parties, and
  - it would not duplicate the skills or resources of other agencies, and could contract analytical work to specialist agencies such as the Industry Commission.<sup>17</sup>

The key functions of the NCC in relation to specific aspects of competition reform are as follows:

- Regulatory restrictions on competition - to provide advice on the development and implementation of principles governing the review of regulatory restrictions, and, on request, undertake economy-wide reviews of particular restrictions.
- Structural reform of public monopolies - to provide advice on the development and implementation of principles governing the structural reform of public monopolies, undertake economy-wide reviews of structural reform issues on request, and on request from a particular government, investigate proposed privatisations that may involve the transfer of a significant public monopoly to the private sector.
- Declarations of access rights - to provide advice to the Commonwealth Minister on creation of a legislated right of access in particular circumstances, including recommendations of terms and conditions.
- Pricing matters - to provide support for the development of agreed pricing approaches for public monopolies, and advice to the Commonwealth Minister on whether a particular firm or market should be subject to the national prices oversight mechanism.
- Competitive neutrality - to provide advice on the development and implementation of principles.
- Transitional and other matters - to provide advice on the transition of public monopolies and regulated industries to a more competitive environment, and on request, on the development and implementation of the national competition policy.<sup>18</sup>

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<sup>17</sup> *National Competition Policy*, p.319.

<sup>18</sup> *National Competition Policy*, p.324.

## 2.4.2 Australian Competition Commission

The Committee's proposal is that the Trade Practices Commission be combined with the Prices Surveillance Authority and renamed the Australian Competition Commission (ACC). As such, the ACC would be the administrative body for the national competition policy, having a range of statutory functions. Key among those would be oversight of matters concerning the competitive conduct rules, including authorisations, declarations and enforcement.

Two other important functions would be the administration of access to essential facilities and of the national prices oversight mechanism. In both cases, the Committee considered the option of industry-specific regulation but rejected it in favour of an economy-wide regulator. The decision is most contentious in relation to access. The Committee concluded that there are sufficient common issues across industries to justify a common regulator, which would also have the advantage of having an economy-wide perspective and not being too intimately related to any one industry. Any specific technical issues would be considered by the NCC in the course of a public inquiry to determine its recommendations.

The key functions proposed for the ACC are as follows:

- Competitive conduct rules - to enforce and monitor compliance, administer the authorisation process (ie, authorisation of specific exemptions), and monitor and report annually on legislated and regulatory exemptions. The Commission will also administer other specified parts of the TPA.
- Regulation review - to undertake reviews of regulatory restrictions on competition.
- Access regime - to oversee the administration of the national access regime, provide arbitration facilities to parties subject to an access declaration, and oversee the implementation of any pro-competitive safeguards.
- Prices oversight - to administer the prices oversight function of the national policy.
- Competitive neutrality - to report on allegations of non-compliance with agreed principles to the relevant government and the NCC.
- Public education - to provide public education on the conduct rules and the role of competition in the community.<sup>19</sup>

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<sup>19</sup> *National Competition Policy*, p.332.



An important aspect of the role of the TPC is consumer protection, by virtue of parts V and VA of the TPA. In adopting the Hilmer-based reform package, the Council of Australian Governments expanded the name of the ACC to recognise its consumer protection role. It will be called the Australian Competition and Consumer Commission (ACCC) (see Section 4).

Appeals on decisions made by the ACCC would be considered by the proposed Australian Competition Tribunal, successor to the current Trade Practices Tribunal.

### **3. RESPONSES TO THE HILMER REPORT**

#### **3.1 INDUSTRY COMMISSION REPORT**

The Council of Australian Governments meeting in August 1994 requested the Industry Commission (IC) to assess the effects of "Hilmer and related reforms" on economic growth and revenue<sup>20</sup>. The expression "Hilmer and related reforms" refers to the recommendations in the Hilmer report and other specific reforms related to electricity, gas, water, road transport, mutual recognition, partially registered occupations and ports. The original deadline was for a draft report by 30 November and a final report by 20 January, in time for the next scheduled COAG meeting in February 1995. In the event, the COAG meeting was deferred to April 1995 and the report deadline to March 1995. Either way, the timing was frugal. The full terms of reference and a summary of the report's conclusions are reproduced as Appendix E.

The IC used a computer modelling approach which involved a range of assumptions and economic estimates, which are detailed in the report. The following points provide a brief summary of the IC's conclusions:

- The projected benefit of the reforms assessed was a gain in gross domestic product (GDP) of 5.5%, or \$23 billion per year. This should boost both real wages and job numbers, but they will counterbalance each other. One example given was a combination of a 3% increase in real wages and 30 000 extra jobs. If either increases more than those respective amounts, the other will increase less.
- The benefits should be widespread across industries. In most industries the projected gains are substantial.

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<sup>20</sup> Industry Commission, *The Growth and Revenue Implications of Hilmer and Related Reforms*, AGPS, Canberra, March 1995, Appendix D1.

- Commonwealth revenue should increase by \$5.9 billion annually, or 6.0%, and that of the States, Territories and local government should increase by \$3.0 billion annually, or 4.5%.
- Commonwealth reforms will contribute \$1.2 billion to Commonwealth revenue and \$0.4 billion to state and local revenue, and 1.0% to GDP. State, Territory and local government reforms will contribute \$2.6 billion to own revenue, \$4.7 billion to Commonwealth revenue, and 4.5% to GDP.<sup>21</sup>

The above figures do not include any transitional costs associated with the implementation of the reforms.

Some commentators have argued that the IC's predictions are unduly optimistic. Dr John Quiggin of James Cook University estimated that the net gain in GDP will be only 0.5%, not 5.5%<sup>22</sup>. Quiggin claims that the difference is due to the failure of the IC to adequately account for loss of employment associated with the Hilmer reforms, and to exaggerated predictions of gains in productivity and the stimulation of capital investment.

The results of an assessment by Dr John Madden of the Centre for Regional Economic Analysis at the University of Tasmania<sup>23</sup> were more comparable with those of the Industry Commission, although his analysis did not include all the reforms modelled by the IC. Overall, he estimated real increases of 3.4% in GDP and 4.0% in household consumption (higher than the IC). As with the IC, he predicted that the benefits of the reforms would be widespread, over all industry sectors and all States. Madden's simulations may be open to the same criticism to that made of the IC study by Quiggin, in that they involve the assumption that unemployment will not change as a result of the reforms.

Madden's predictions for the individual States and Territories are summarised in Table 3.1. Of the States, the greatest predicted impact of reforms is in Victoria, because the greatest amount of productivity improvement in both labour and capital is expected to occur there. The next highest impact is predicted for Western Australia, because of projected benefits for the mining industry, and the fact that WA has a high proportion of Australian mining output relative to its proportion of GDP. In Queensland, predicted growth in both GSP and household consumption is below the national average. This is at least partly due to the fact that in many of the industries studied (water, electricity,

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<sup>21</sup> Industry Commission, pp.83-84.

<sup>22</sup> John Quiggin, *The Growth Consequences of Hilmer and Related Reforms*, unpublished paper, 1995.

<sup>23</sup> John Madden, *The Impact of Implementing the Hilmer Report on the National and State Economies*, Report prepared for Australian Chamber of Commerce and Industry and other bodies (see Bibliography for full list), Centre for Regional Economic Analysis, University of Tasmania, 21 March 1995.

rail, and ports), Queensland appeared to start from a base of substantial prior improvements in productivity.

The relative impact of the mining industry also accounts for the high level of predicted GSP increase in the Northern Territory. By contrast, the low level in the ACT is because Commonwealth government consumption was assumed in the simulations to be static. However the ACT has relatively high personal income levels so should experience above average growth in household consumption.

**Table 3.1 Effects of Hilmer Reforms on Gross State Product and Household Consumption by State and Territory.**

STATE/TERRITORY	GSP <sup>a</sup>	RHC <sup>b</sup>
New South Wales	2.54	3.37
Victoria	4.28	4.92
Queensland	2.73	3.44
South Australia	2.51	3.63
Western Australia	4.27	5.16
Tasmania	2.56	4.04
Northern Territory	6.79	7.16
ACT	1.97	4.53
AUSTRALIA	3.37	4.03

a. Gross State Product, for Australia Gross Domestic Product

b. Real Household Consumption

Source: Madden, p.17.

### 3.2 THE BUSINESS COMMUNITY

Representatives of the business community are generally supportive of the recommendations of the Hilmer Report. After the inconclusive outcome of the August 1994 meeting of COAG, a joint press release was issued by business groups expressing commitment to the report's principles and calling for outstanding matters to be resolved at the next COAG meeting. Parties to the joint press release were the Business Council of Australia, the Australian Chamber of Commerce and Industry, the NSW Chamber of Manufacturers, the Metal Trades Industry Association, the Australian Chamber of Manufacturers, the Australian Mining Industry Council, the Queensland Mining Industry Council, the Steel Institute of Australia and the Victorian Farmers Federation<sup>24</sup>.

The position paper of the Business Council of Australia (BCA) published in July 1994 expressed strong support for the proposed national competition policy. It emphasised

<sup>24</sup> Tom Park, 'Why the Hilmer Report is important to business', *Business Council Bulletin*, no.115, December 1994, pp.44-48.

the need for competition policy to be national in focus, requiring consistency and co-operation between jurisdictions, particularly the states. Further, the business community did not want different competition rules for different jurisdictions or different industries<sup>25</sup>.

The rationale for the support given by the business community is twofold. The first reason relates to international trade. Competition improves productivity, and products sold on our domestic market are competing against imports which are becoming cheaper because the productivity of overseas manufacturers is increasing and our tariffs are declining. Also, our exports must be competitive in overseas markets. The second reason relates to investment by business. Investment creates jobs and enhances job security. For that investment to occur in Australia, profitability and competitiveness, by international standards, are required in Australia.<sup>26</sup>

### 3.3 UTILITIES AND OTHER GOVERNMENT BUSINESS ENTERPRISES

The Trade Practices Commission conducted a conference in March 1994 to examine reform issues in public utilities from a consumer perspective<sup>27</sup>. In general, speakers, including consumer representatives<sup>28</sup>, supported the thrust of reforms recommended by Hilmer, which in many cases continue trends already underway in various sectors.

David Borthwick of the Treasury presented comparisons of capital and labour productivity between Australia and the OECD average, for several sectors of the economy, between 1970 and 1985<sup>29</sup>. On the basis of these figures, the public utilities (electricity, gas and water) were by far the least productive sectors of the Australian economy in that period, relative to the OECD. Between 1984/85 and 1990/91, improvement was evident in that the utilities had one of the highest annual productivity growth rates in the economy, albeit from a low base. Borthwick concluded that the utilities had considerable potential to continue achieving productivity gains, in particular through the Hilmer reforms.

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<sup>25</sup> Business Council of Australia, 'Position paper on the Hilmer Report', *Business Council Bulletin*, no.110, July 1994, pp.6-15.

<sup>26</sup> Park, p.45.

<sup>27</sup> Trade Practices Commission, *Passing on the Benefits: Consumers and the reform of Australia's utilities*, TPC, March 1994.

<sup>28</sup> Phil Marchionni, Australian Consumers' Association, and Michael Delaney, Motor Trades Association of Australia.

<sup>29</sup> David Borthwick, 'The true consumer interest in utilities reform', *Passing on the Benefits: Consumers and the reform of Australia's utilities*, TPC, March 1994, pp.21-29.

Community service obligations, disclosure of information and prices are key issues in the impact of reforms on consumers. Community service obligations were defined by NSW Treasury as non-commercial activities of a government trading enterprise which the Government directs it to conduct because of a social benefit, and provides budget funding, but which would not be conducted under purely commercial considerations<sup>30</sup>. The advantages claimed for budget-sourced funding are transparency, accountability, clarity of management focus, equity, and efficiency in pricing. However consumers organisations were wary that the needs of some groups - "rural and remote consumers and other economically and socially disadvantaged groups" - may be undervalued<sup>31</sup>. Solutions proposed included guaranteed consultation by government on all decisions relating to public enterprises, preparation of consumer impact statements, and consumers' charters. A checklist for effective charters is reproduced in Appendix F.

Some commentators have criticised Hilmer's emphasis on economic outcomes over other social objectives<sup>32 33</sup>. Two items of concern are universal access to essential services and environmental protection. In principle, universal access to such services as water, energy and telecommunications is implicit in the acknowledgment of community service obligations. However their inclusion in the annual budget process essentially exposes them to an annual test of affordability based on criteria subject to political and other pressures. The primacy of economic objectives may also lead to environmental exploitation. Maximising returns may lead entities to maximise usage of natural resources, complying only with minimum statutory requirements for environmental protection.

Writing in the BCA Bulletin, Haynes also argued for consumer involvement in the energy utilities<sup>34</sup>. Electricity users (perhaps industrial?) are represented on the National Grid Management Council and he urges a similar arrangement for gas. In fact, gas industry reform is lagging behind that of electricity in several respects, something which adoption of the Hilmer proposals should help to overcome.

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<sup>30</sup> Percy Allan, 'Community service obligations and the consumer interest', *Passing on the Benefits: Consumers and the reform of Australia's utilities*, TPC, March 1994, pp.122-125.

<sup>31</sup> Jenni Mack, 'Some solutions: Consumer impact assessments', *Passing on the Benefits: Consumers and the reform of Australia's utilities*, TPC, March 1994, pp.187-192.

<sup>32</sup> Liza Carver, 'The Hilmer report and competition policy: a consumer perspective', *Trade Practices Commission Bulletin*, no.80, February 1995, pp.8-10.

<sup>33</sup> Howard Guille, 'Market madness: the Hilmer Report', *WISER*, vol.1 no.2, pp.37-40.

<sup>34</sup> Warren Haynes, 'Competition in energy', *Business Council Bulletin*, no.117, March 1995, pp.38-42.

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Other commentators have been critical of the Hilmer proposals in relation to essential facilities and uniform application of competition rules. Pengilley argued against the Hilmer recommendation for decisions about access to essential facilities to be made by the Commonwealth Minister, because the resultant subjectivity and uncertainty will discourage investment.<sup>35</sup> He recommended a court-based decision process. He also presented a case for several industry-specific regulators, rather than a single body such as the proposed Australian Competition and Consumer Commission. The expertise and experience required for regulatory decisions differ between industries. Moreover, the very principle of competition suggests that monopoly decision-making by a single regulator greatly increases the likelihood and impact of serious consequences from a poor decision. Pengilley's conclusions are presented in Appendix G.

H.M. Kolsen also presented an economist's case in favour of industry-specific regulation<sup>36</sup>. He argued that a transition period will be necessary for government businesses to adopt the Hilmer reforms, which will in some cases require a fundamental re-evaluation of their basic approach. Therefore regulation will also have to evolve on an industry by industry basis during the transition period. Further, some industries will always remain cases where individual treatment is required, such as those primarily involved with international business, where overseas standards may overrule those in Australia.

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<sup>35</sup> Warren Pengilley, 'Hilmer and "Essential Facilities"', *University of New South Wales Law Journal*, vol.17 no.1, September 1994, pp.1-53.

<sup>36</sup> H.M. Kolsen, 'Industry policy and trade practices legislation in Australia', *Economic Analysis and Policy*, vol.24 no.2, September 1994, pp.116-129.

### 3.4 THE PROFESSIONS

Responses to Hilmer from the professions have varied from wary to hostile. Most concern has been with the proposed outlawing of anti-competitive aspects of the rules of professional associations, and the loss of exempt status under the TPA.

The Australian Council of Professions endorsed the principle of competition on the basis of merit for the provision of any specific service, but argued for a continuation of complete self-regulation<sup>37</sup>. However they suggested that the regulatory bodies should include community and government representatives. Arguments for self-regulation include that the regulator needs to have technical expertise and awareness of community needs in the profession concerned. The professions are a case where social objectives, eg maintaining quality standards, should be equivalent to economic efficiency in establishing competition policy.

The impact of the Hilmer proposals will vary between professions. Accountants are already deregulated to some degree, particularly in the important areas of fee regulation and advertising<sup>38</sup>. The impact on the legal profession will be much greater. Proposed changes will remove the distinctions between barristers and solicitors, remove restrictions on business structures, remove price controls, permit advertising, and enable non-lawyers to undertake some legal services<sup>39</sup>.

James Farmer QC argued strongly against the deregulation proposals for the legal profession, particularly the provision of legal services by non-lawyers and the removal of distinctions between barristers and solicitors<sup>40</sup>. He argued that the quality of legal services will decline because of the lowering of professional standards, and, that ultimately even the maintenance of the rule of law will suffer. John Graham, speaking for the medical profession, was even more belligerent<sup>41</sup>. He argued that the professions should be totally exempted from the Hilmer reforms and that there is no legitimate role in professional regulation for the Government at all. However he offered little discussion to support his opinions.

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<sup>37</sup> Australian Council of Professions, *Comments to COAG Working Group on Implementation of the Hilmer Report*, ACP, Canberra, May 1994.

<sup>38</sup> Janine Pascoe, 'Professional regulation after the Hilmer report', *Australian Accountant*, March 1994, pp.35-40.

<sup>39</sup> Trade Practices Commission, *Study of the Professions: Legal, Final Report*, TPC, March 1994.

<sup>40</sup> James Farmer, 'The application of competition principles to the organisation of the legal profession', *University of NSW Law Journal*, vol.17 no.1, September 1994, pp.285-297.

<sup>41</sup> John Graham, 'Professional competition leaves Hilmer for dead', *Australian Medicine*, vol.7 no.5, 20 March 1995, pp.16-17.



#### **4. IMPLEMENTATION OF HILMER - COAG, APRIL 1995**

The Council of Australian Governments meeting on 11 April 1995 endorsed a national competition reform package which was derived from the recommendations of the Hilmer report. At the meeting the Prime Minister, Premiers and Chief Ministers agreed to the legislative amendments in the Commonwealth's Competition Policy Reform Bill 1995, and signed three inter-governmental agreements which dealt with non-legislative matters (see below). Implementation of the national competition policy will be based on these initiatives.

The Premiers and Chief Ministers agreed to pass the required legislation to apply the Competition Code (based on Part IV and other relevant sections of the TPA) to State and Territory jurisdictions within 12 months of the Competition Policy Reform Bill receiving the Royal Assent. Subject to passage in the Commonwealth Parliament, the amendments to the competitive conduct rules will commence in July 1995. The new institutional arrangements and the access regime will commence in the second half of 1995 or early 1996.<sup>42</sup>

While the recommendations of the Hilmer report of 1993 largely became the competition policy reform package of 1995, there are certain salient differences. Most noticeably the States and Territories have secured more control over the development and implementation of competition policy than Hilmer recommended. In several key respects the agreements specify that the States and Territories are under no specific obligation to reform, and each is entitled to determine its own agenda. The States have also retained the right to authorise, by statute, conduct which would otherwise contravene the TPA, although such exemptions will be subject to disallowance by the Commonwealth if a net public benefit cannot be demonstrated. However despite these apparent concessions to the independence of the States and Territories, the agreements contain attractive financial incentives for them to comply with the reform proposals.

##### **4.1 COMPETITION POLICY REFORM BILL 1995**

The Bill contains the amendments to the TPA and other Commonwealth legislation required to implement the competition reform package. The amendments provide the legislative provisions for the National Competition Council and the Australian Competition and Consumer Commission, the amendments to the competition rules (primarily Part IV of the TPA), and the establishment of the Competition Code (including the schedule version of Part IV). New Section 2 of the TPA sets out the object of the Act as follows:

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<sup>42</sup> Council of Australian Governments, *Communique*, COAG meeting 11 April 1995, Canberra.

*The object of this Act is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection.*

## **4.2 CONDUCT CODE AGREEMENT**

This agreement sets out details of the conduct of the various parties in relation to competition laws. The States and Territories will legislate to apply the text of the Competition Code (the schedule version of Part IV of the TPA, and related sections and regulations) in their jurisdictions. The agreement also outlines the procedure for approval of appointments to the ACCC, and provides that the Commonwealth will be responsible for funding the ACCC.

The agreement sets out a procedure for consultation on any proposed modifications to the competition laws. Where a government enacts legislation which provides an exemption from the competition laws, notice of the exemption must be sent to the Australian Competition and Consumer Commission within 30 days. After four months, the Commonwealth may not table regulations to disallow the exemption unless they are accompanied by a report by the NCC on the impact of the exemption. Within three years, notice of all existing legislation which provides exemptions must also be given.

A copy of the agreement is included as Appendix H.

## **4.3 COMPETITION PRINCIPLES AGREEMENT**

This agreement sets out several principles for the application of competition policy. A copy is included as Appendix I. Key features are:

### ***Relevant matters for assessments***

Any assessment of the costs, benefits, appropriateness or means of achieving a particular policy objective should take into account, where relevant:

- (a) legislation and policies on ecologically sustainable development,
- (b) social welfare and equity considerations including community service obligations,
- (c) industrial relations policies including occupational health and safety,
- (d) economic and regional development including employment and investment growth,
- (e) consumer interests,
- (f) business competitiveness, and
- (g) efficient allocation of resources.

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***Prices oversight of government business enterprises (GBEs)***

States and Territories are primarily responsible for prices oversight of GBEs that they own, and are to consider establishing "independent sources of price oversight advice". However a State or Territory may subject its GBEs to a prices oversight mechanism of the ACCC or of another jurisdiction, by agreement with the Commonwealth or the other jurisdiction.

A State or Territory GBE may be subjected by the Commonwealth to a prices oversight mechanism administered by the ACCC, without the consent of the State or Territory, but only under specified conditions and after extensive consultation and on the recommendation of the NCC.

***Competitive Neutrality policy and principles***

The objective of these principles is to remove any net competitive advantage that GBEs enjoy simply as a result of public sector ownership. Governments will corporatise all key GBEs<sup>43</sup>, imposing full taxes or tax equivalents, debt guarantee fees, and regulations equivalent to those imposed on private sector businesses. Such regulations may, for example, relate to environmental protection requirements or to planning and approval processes.

Similar conditions may be imposed on other GBEs where considered appropriate. In all cases, action is only required when the benefits are expected to outweigh the costs. Each Government will publish a policy statement on competitive neutrality by June 1996, and will publish an annual report on the implementation of competitive neutrality principles.

***Structural reform of public monopolies***

Each Government will review its public monopolies to determine the best way to privatise them. Among other things, the reviews will consider how to separate regulatory functions from commercial functions, and how to fund and deliver any community service obligations that are related to the monopolies and that are considered warranted.

***Legislation review***

The agreement provides the following guiding principle:

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<sup>43</sup> Defined as those classified as "Public Trading Enterprises" and "Public Financial Enterprises" under the Government Financial Statistics Classification.

*...that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:*

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

Each Government will review and reform anti-competitive legislation by the year 2000, and will prepare a review timetable by June 1996. When a Government believes a review should be a national review, it will consult other Governments and may request the NCC to conduct the review. Each Government and the NCC will report annually on progress. Any new legislation that restricts competition should comply with the guiding principle outlined above.

### ***Infrastructure access***

The Commonwealth will legislate to establish a regime for third party access to infrastructure facilities of national significance. State and Territory services should have their own access regime unless the national regime is more appropriate (for example, if a facility extends beyond one State or Territory). The agreement provides detailed principles for the operation of an access regime.

### ***Application of the principles to local government***

Each State and Territory will, in consultation with local government, apply the principles of the agreement to local government within their jurisdiction. Each State and Territory will publish a statement by June 1996 which specifies the application of the principles to particular local government activities and functions.

### ***The National Competition Council***

The Commonwealth will fund the NCC, and will consult the States and Territories on appointments to it. Governments will jointly prepare the work program of the NCC, and will review its operation after five years.

## **4.4 AGREEMENT TO IMPLEMENT THE NATIONAL COMPETITION POLICY AND RELATED REFORMS**

This agreement, between the Commonwealth and the States and Territories, sets out the financial assistance to be provided by the Commonwealth in relation to the competition policy reforms. The Commonwealth agreed to maintain the indexed per capita Financial

Assistance Grants, and to pay a series of Competition Payments to recompense the States for expected revenue losses from competition reforms.

The Competition Payments will be in three tranches (ie increments, commencing progressively). Total payments in current prices will be \$200 million annually from 1997/98, increasing to \$400 and \$600 million annually from 1999/2000 and 2001/02 respectively. They will be divided between the States on a per capita basis.

Payments to each state will be conditional on progress in implementing competition reforms. The actual conditions are reproduced in Appendix J. In summary, payment of the first tranche from July 1997 to a particular State or Territory will depend on:

- enactment of legislation to apply the Competition Code as a law of the state or Territory,
- complying with the Competition Policy Intergovernmental Agreements,
- where applicable<sup>44</sup>, implementation of COAG agreements on a national electricity market (by July 1995) and free and fair trade in gas (by July 1996), and
- observance of agreed road transport reforms.

Payment of the second tranche from July 1999 will depend on:

- continued compliance with the Competition Policy Intergovernmental Agreements, and with the Competition Policy Reform Bill as a fully participating jurisdiction,
- continued observance of agreed road transport reforms,
- where applicable, completion of the transition to a fully competitive National Electricity Market, and full implementation of free and fair trading in gas, and
- implementation of water industry reforms agreed to by COAG in February 1994.

Payment of the third tranche from July 2001 will depend on:

- actual compliance with the Competition Principles agreement, including review and reform of relevant legislation,

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<sup>44</sup> These reforms are not expected to apply to Western Australia, because of the logistical impracticalities of connecting to national grids.

- 
- continuing to be a fully participating jurisdiction under the Competition Policy Reform Bill,
  - continuing effective observance of reforms in electricity, gas, water and road transport, and
  - the setting of national standards in accordance with formal principles and guidelines.

The National Competition Council will decide whether the above conditions have been met by each jurisdiction before each tranche is due to commence.

#### 4.5 REACTIONS TO THE AGREEMENTS

Given the wide range of the Hilmer recommendations and of the decisions taken in response to them at the COAG meeting in April 1995, it is not surprising that reaction has been varied. Initial press comment was generally favourable and concentrated on the financial benefits predicted for the economy and the payments offered to the States and Territories by the Commonwealth<sup>45</sup>.

However several concerns were also expressed. Consumer groups predicted that prices of utilities to domestic consumers could rise rather than fall. Currently domestic charges for gas, electricity and water are cross-subsidised by higher charges to business consumers. Even though utility prices are expected to fall overall, the removal of the cross-subsidies will mean that domestic charges may rise or, at least, not fall as much as business charges.<sup>46</sup>

The Community and Public Sector Union criticised the potential privatisation of many public services including public transport, which they predicted would lead to downgrading of services, and price rises, especially through the loss of cross-subsidies on non-profitable services. They also said that the Industry Commission had not taken job losses into account in its calculations, which they claimed would decrease GDP by 0.5%.<sup>47</sup>

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<sup>45</sup> For example, Brook Turner and Tom Burton, 'Borderless nation', *Australian Financial Review*, 12 April 1995, p.1,4; Tim Colebatch, 'Deal is done for era of competition', *Age*, 12 April 1995, p.1.

<sup>46</sup> Anne Davies and Brad Norington, 'Prices may rise, warns consumer group', *Sydney Morning Herald*, 12 April 1995, p.

<sup>47</sup> Davies and Norington.

Mike Nahan of the Institute of Public Affairs criticised the Hilmer philosophy that competition policy and approaches should be as nationally uniform as possible<sup>48</sup>. He endorsed the COAG outcome that gave the States and Territories some freedom as to how they approach the reform package. Nahan also pointed out that some of the reforms which the Industry Commission included in its estimate of net benefit were already underway and would have occurred regardless of Hilmer.

The Australian Local Government Association, whose President attends COAG meetings, supported the thrust of the competition policy reforms, with reservations on particular issues<sup>49</sup>. The ALGA estimated that Local Government will receive an extra \$736 million in grants over the next decade, depending on progress in implementing the competition policy agenda. The first payment should be an extra \$14 million (spread over 770 local authorities) in 1997/98. However this money has not been directly allocated to Local Governments, but will come through State and Territory Governments.

The ALGA sought and obtained the requirement in the Competition Principles Agreement that States and Territories must negotiate the application of the Principles as they apply to local government activities and functions, with local government. The main concerns of the ALGA are that competition policy should not provide disincentives for regional development and should not lead to reduced community service obligations to rural and remote communities.

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<sup>48</sup> Mike Nahan, 'Reform not bound to competition policy', *Australian Financial Review*, 28 April 1995, p.24.

<sup>49</sup> Australian Local Government Association, *COAG - Good and not so Good Decisions*, ALGA News Release, 12 April 1995.

## 5. IMPACT OF COMPETITION POLICY IN QUEENSLAND

### 5.1 GOVERNMENT BUSINESS ENTERPRISES

Queensland is a signatory to the COAG agreements and is expected to remain a "fully-participating jurisdiction" in the competition policy reform process. The Queensland Government has established an Interdepartmental Steering Committee to oversee the implementation of national competition policy in government-related agencies. The Committee will consist of Directors-General or their nominees from central agencies and the most affected line departments. A National Competition Policy (NCP) Implementation Unit has been established within Treasury. The Steering Committee and the NCP Unit will oversee the implementation process by establishing policy guidelines, setting timetables, acting as a co-ordinating centre and providing specific assistance to departments<sup>50</sup>.

More specifically, Lennon has outlined the major components of the implementation program as follows:

1. *An extensive education program for legal, policy and administrative personnel across government, as well as the design of tailored compliance manuals for agencies involved in commercial transactions or service delivery.*

*This program must:*

- *generate a culture change in the way government officers conduct business*
  - *provide an understanding of the strict legal requirements of the TPA*
  - *provide an understanding of the policy framework within which future legislation must fit.*
2. *A comprehensive audit of all relevant government activities to identify:*
    - *existing areas of vulnerability (particularly in respect of contracts entered since 19 August 1994, and poorly drafted or non-existent authorisations) and*

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<sup>50</sup> Glyn Davis, 'Introduction to the Competition Policy Reforms', Proceedings, *National Competition Policy Seminar*, Brisbane, 8 June 1995, pp.3-4.



- *any appropriate remedial action.*
3. *Development of guidelines for the application of the cost-benefit test for anti-competitive legislation including section 51 authorisations.*
  4. *Ensuring compliance with the State's obligations under the Act and Agreements. This will include:*
    - *notification requirements (eg re section 51 authorisations)*
    - *publication of a competitive neutrality statement and development of a timetable for the 5 year legislation review by June 1996.*
  5. *Enactment of application legislation to apply the Code by June 1996.*
  6. *Establishment of a prices oversight regime and either a generic or industry specific access regimes - it is important that these are established as soon as possible if the Government does not wish to lose jurisdiction in these areas to the national bodies.*
  7. *Ensuring all proposed legislation is not inconsistent with the TPA and, if it is, whether this can be justified in terms of the cost-benefit test, and, if so, that an effective authorisation is in place.*
  8. *An examination of all existing section 51 authorisations within the transitional period (the next three years) to decide if they are to be retained and, if they are, to enact new authorisations where necessary to comply with the new section 51.*
  9. *By the year 2000, completion of a review of all anti-competitive legislation in accordance with the principles set down in the Competition Principles Agreement, and, thereafter, the conduct of similar reviews every 10 years.*<sup>51</sup>

All Queensland Government Business Enterprises and other agencies conducting business (such as the business units of the Administrative Services Department) will be affected by the requirements of the implementation program. New Section 2B of the TPA removes the protection of the shield of the crown from State and Territory agencies and authorities, "so far as the Crown carries on a business". This phrase is not defined, but Section 2C outlines several activities that do not amount to carrying on a business, including collecting fees, taxes and levies, and issuing licences for the supply of goods or services. In other words, most of the activities of GBEs will come under the ambit of the TPA.

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<sup>51</sup> Anna Lennon, 'An Overview of the Reforms', Proceedings, *National Competition Policy Seminar*, Brisbane, 8 June 1995, pp.9-10.

Sheahan argued that this will (or at least should) have a substantial impact on government agencies, because compliance with the TPA requires attention to considerable detail and the ramifications of non-compliance can be extremely serious. In many respects, a comprehensive culture change is required. In Sheahan's words,

*Having regard to the extent and nature of the litigation that has arisen under Part IV, and the important role played by state governments and their authorities in trade and commerce, it is not too pessimistic to say that it is not a question of whether, but when, the state will find itself a respondent to a part IV action. When that happens, success or failure may depend on the care and diligence with which existing practices are now scrutinised for compliance with the Act, and future conduct is guided by an understanding of the rules it imposes, and the philosophy which lies behind them. This last part is perhaps the greater challenge: it requires something close to a revolution in the way State governments think about the manner in which they try to achieve their social and economic goals and conduct their business affairs.<sup>52</sup>*

Legislative provision for many of the reforms has been prepared. For example, the Transport Infrastructure Amendment (Rail) Bill passed by the Parliament on 9 June 1995 amended the *Transport Infrastructure Act 1994* to provide for the corporatisation of Queensland Rail on 1 July 1995, and to provide a basis for the possible access by third parties to the railway system, in line with Hilmer recommendations and the COAG agreements. The *Electricity Act 1994* and the *Petroleum Act 1923* also include provisions to enable access to relevant facilities.

During the COAG negotiations, Queensland obtained the concession that access to rail facilities for the purpose of coal transport would not be possible for a five year transition period. This concession quarantines coal freight royalties, a major source of revenue to the Queensland Government, for that period.

The recent announcement that Queensland Rail was examining the possibility of constructing a rail link between Goondiwindi and Moree, to compete for export cotton and grain freight, is an example of the types of initiative that will become possible under the competition reforms.<sup>53</sup>

## 5.2 ANTICIPATED IMPACTS ON THE QUEENSLAND ECONOMY

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<sup>52</sup> John Sheahan, 'Part IV of the Trade Practices Act and the States: An Overview', Proceedings, *National Competition Policy Seminar*, Brisbane, 8 June 1995, p15.

<sup>53</sup> Peter Morley, 'State to cross border for rail trade', *Courier Mail*, 15 June 1995, p.1.

Queensland Government entities corporatised in 1994 included Queensland Industry Development Corporation, Queensland Investment Corporation, the Ports of Brisbane and Gladstone and the Ports corporation of Queensland. The electricity industry was corporatised and restructured from 1 January 1995, and corporatisation is planned during 1995 for the remaining port authorities, Queensland Rail and Suncorp. The Queensland Government's Economic Development Statement, *From Strength to Strength*<sup>54</sup>, indicated that benefits from the current corporatisation program would include:

- ongoing real reductions in electricity tariffs,
- reduction in pilotage and conservancy charges by port authorities of up to 50% during the next three years, and
- world best practice in coal haulage by the year 2000, and productivity sharing arrangements with coal suppliers.

The overall impact on Queensland of competition policy reforms, as estimated by John Madden of the Centre for Regional Economic Analysis, was described in Section 3.1. Further information from that report is provided in Table 5.1. Madden also estimated that proposed reforms to the legal services industry in Queensland would lead to productivity improvement of 12.0% in that industry<sup>55</sup>.

**Table 5.1 Projected Improvements in Labour and Capital Productivity as a result of Competition Policy Reform, Queensland and Australia.**

SECTOR	LABOUR PRODUCTIVITY		CAPITAL PRODUCTIVITY	
	Queensland	Australia	Queensland	Australia
Electricity	38	50	0	4
Water	0	15	0	6.7
Railways	3	25	4	25
Ports	0	9	15	9

Source: Madden.

<sup>54</sup> Hon Wayne Goss MLA, *From Strength to Strength: Queensland - Leading State*, Queensland Government Economic Development Statement, April 1995.

<sup>55</sup> Madden, p.7.

## 6. CONCLUSIONS

The Hilmer Report will probably be looked back on as one of the more prominent catalysts of micro economic reform in Australia in the latter part of this century. It should probably be viewed as continuing in the trend and philosophy of the reforms that preceded it, while seizing the opportunity to accelerate the process generally and initiate it in certain heretofore intractable areas. Given that the implementation process is only just getting underway, the areas of greatest innovation and impact are likely to be in government enterprises and in the professions. Reforms in the public utilities will almost certainly have major economic impact but will be viewed as inevitable in the flow of reform, parallel to the Hilmer process, promoted by it, but not a direct consequence of it.

Focussing on competition policy reform, the Hilmer report will be seen as the first stage in a long process whose outcome is by no means guaranteed. The next, equally important and arguably more difficult stage was the COAG negotiations to firstly accept the report in principle and secondly agree on its implementation in practice. The other stages remain primarily in the future, although there is no doubt considerable activity underway in government and professional bodies to influence and introduce the next tangible stage.

The nascent nature of the competition reform process and the challenge of the ensuing years was emphasised by Glyn Davis in his address to a recent seminar on the implementation of competition reform:

*It has taken at least a couple of years of difficult and intense intergovernmental work to get to this point, namely, a Bill which is currently being debated in the Federal Parliament, and two intergovernmental agreements. However this really only marks the beginning of implementation of national competition principles across Australia. The real challenges lie ahead, and will require commitment, understanding (not only of the strict letter of the law but also its intent), and a major culture change on the part of government.<sup>56</sup>*

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<sup>56</sup> Davis, p.3.

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