COMPETITION POLICY AND LOCAL GOVERNMENT IN QUEENSLAND

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ABSTRACT

This Research Bulletin looks at the implications for Queensland local government of the implementation of the National Competition Policy (NCP). Principles of price oversight, competitive neutrality, reform of public monopolies, legislative review and third party access to services are each examined separately. It is a requirement under the Competition Principles Agreement that these Principles be applied to local government where appropriate. This Research Bulletin also considers the amendments that have recently been made to the Local Government Act 1993(Qld) by the Local Government Amendment Legislation Acts of 1996 and 1997 to accommodate NCP as well as the Queensland Competition Authority Act 1997. The Local Government Legislation Amendment Bill (No 3) 1997 is also considered.
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1. INTRODUCTION

The purpose of this Research Bulletin is to outline the application of the principles of the National Competition Policy resulting from the Report of the Independent Committee of Inquiry chaired by Professor Fred Hilmer in August 1993.¹

The objective of National Competition Policy (NCP) is to provide an environment to encourage a better use of the country’s resources - and hence provide a higher standard of living - through increasing competition.

The policy focuses on both the private and public sectors, in particular Government business enterprises and unincorporated businesses (including the professions), which have traditionally been protected from competition ... The policy is based on accepted reform principles aimed at providing a consistent approach to the dismantling of barriers to competition across State borders as well as legislation to ensure that the same competitive rules apply to all sectors of the economy, regardless of ownership.²

Clause 7 of the 1995 Competition Principles Agreement specifically stated that the principles were to apply to local government in all states and territories.

Application of the Principles to Local Government

7 (1) The principles set out in this agreement will apply to local government, even though local governments are not Parties to this agreement. Each State and Territory Party is responsible for applying those principles to local government.

(2) Subject to subclause (3) where clauses 3, 4 and 5 permit each Party to determine its own agenda for the implementation of the principles set out in those clauses, each State and Territory Party will publish a statement by June 1996:

(a) which is prepared in consultation with local government; and

(b) which specifies the application of the principles to particular local government activities and functions.³

¹ F G Hilmer, M R Rayner and G Q Taperall, National Competition Policy: Report by the Independent Committee of Inquiry, AGPS, Canberra, 1993.


³ Competition Principles Agreement.
The lack of discussion in the 1993 Hilmer Report on the consequences of implementation of Competition Policy Principles for local government did not go unrecognised.\(^4\) It has been argued that it was not until 1995 that there was any significant level of awareness on the part of federal and state officials as to the ramifications of the NCP for local government.\(^5\) Since April 1995 when the Council for Australian Governments adopted the National Competition Policy package, detailed policy statements have been prepared by the Queensland Government on implications for local government in Queensland as required by Clause 7 of the Competition Principles Agreement.\(^6\)

Local government in Queensland is different to that in other states in the scale and extent of local government services provided. In other states, significant services such as water and sewerage are generally delivered through State government authorities. Some activities of Queensland local government are clearly significant businesses in the context of the Queensland economy eg water supply, sewerage, and many larger local governments such as the Brisbane City Council are well advanced in implementing efficiency and competition related reforms by commercialisation of business units as well as participation in joint business ventures.\(^7\)

For the most part, however, application of National Competition Policy Principles to local government is going to constitute a new way of looking at organisational structure and provision of services by local authorities in Queensland. To create a “turn-a-round” from an accountability system based on elector expectations and demands, to one that is based on business principles will necessitate a change in the way in which local government approaches its constituency. This approach will be marked by a need for local government to ensure that its constituency is more


informed of the fact that business principles are to be given a higher priority. It will be a learning process for both local government officials and rate payers. Perhaps at a practical level NCP should be viewed as an opportunity for local government to examine its past and current performance in a critical way. Most local government officials would suggest that the biggest single constraint on their operations is a lack of financial resources to supply all the services they wish to supply at a level most desired. NCP will not change this. What the application of the NCP is intended to do is to introduce new ways of thinking about operations that will identify and allow the financial resources that are available, to be used more productively and efficiently. In short, the introduction of competitive neutrality reforms will assist in identifying where savings can be made in local government business activities to enable monies to be more effectively spent in other service areas, or more productively in the same area of activity.

2. THE NATIONAL COMPETITION POLICY FRAMEWORK AND QUEENSLAND LOCAL GOVERNMENT

The formalisation and implementation of the National Competition Policy occurred via a number of steps at Commonwealth and State level.

2.1 COMMONWEALTH

- Agreement at the March 1991 Premier’s Conference for a national approach to competition policy. This resulted in the establishment of the Hilmer inquiry in October 1992.
- The signing of the three inter-governmental agreements: the Conduct Code Agreement, the Competition Principles Agreement and the Agreement to Implement the NCP and Related Reforms. These were all entered into by the Commonwealth, the six states and the two territories, and signed by the respective heads of government, in April 1995.
- Competition Policy Reform Act 1995

This Act, by way of amendments to the Trade Practices Act 1974 (Cth) and the Prices Surveillance Act 1983 (Cth) created the National Competition Council and the Australian Competition and Consumer Commission; the latter resulting from an amalgamation of the former Trade Practices Commission and the former Prices Surveillance Authority. In order to apply prohibitions against anti-competitive behaviour to all businesses in Australia, complementary legislation was required at the state and territory level. The Act also established a legal regime to allow private sector (third party) access to the services of certain essential infrastructure facilities.
2.2 QUEENSLAND LEGISLATION AND POLICY

2.2.1 Competition Policy Reform (Queensland) Act 1996

The passing of this Act enabled the implementation in Queensland of the restrictive trade practices sections of the *Trade Practices Act 1974* (Cth) upon individuals and partnerships, as the jurisdiction of these does not fall within the constitutional power of the Commonwealth. (See Queensland Parliamentary Library Legislation Bulletin 6/95, *Extending the Hilmer Reforms to Queensland: The Competition Policy Reform (Queensland) Bill 1995*, and Background Information Brief No 30, *Competition Policy: Hilmer, Government and Business*, June 1995 for further analysis of and background to this Act).

2.2.2 Queensland Government Policy Statement on Local Government and National Competition Policy 1996

Published in accordance with Clause 7 of the Competition Principles Agreement this policy establishes the government’s commitment to applying the elements of that agreement.\(^8\)

The policy statement gives an overview of the application of the five principles of the agreement as they apply to local government and they are discussed further in this Research Bulletin from Sections 3 to 8. In addition, the policy statement canvassed the introduction of a voluntary code of competitive conduct to be applied to the business activities of smaller councils. This issue is discussed at section 5.4.

2.2.3 Local Government Legislation Amendment Act 1996

This Act commenced the application of the NCP to local government. The Act formally designated 17 local authorities (see Appendix A of this Research Bulletin) as being obligated to conduct public benefit assessments in relation to significant business activities (Type 1 and Type 2) by 30 June 1997. The aim of these public benefit assessments is to ascertain the desirability of either corporatising or commercialising significant business activities which have a current expenditure level in excess of prescribed amounts as set out in the July 1996 Queensland Government Policy Statement *National Competition Policy and Queensland Local Government*.

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2.2.4 Queensland Competition Authority Act 1997

This Act established the Queensland Competition Authority which has responsibility for:

- reviewing the pricing regimes of monopoly and near monopoly government business activities; and
- receiving complaints relating to competitive neutrality and state government business activities and in some cases local government (see 2.2.6); and
- regulating third party access to infrastructure.

2.2.5 Local Government Legislation Amendment Act 1997

With respect to the involvement of local government with NCP this is the most significant Act that has been passed to date. One major aspect of the legislation is the establishment of a framework for the application of corporatisation, commercialisation, and full cost pricing to significant business activities of local authorities. The Act also introduces a detailed model of corporatisation of local government significant business activities. Smaller councils whose business activities do not cross the significant threshold will still be required to apply competitive neutrality principles to business activities that they undertake in competition with the private sector.

Further significant aspects of the Act are:

- the introduction of a voluntary code of competitive conduct;
- requirement to identify and assess anti-competitive provisions in local laws; and
- assessment of the cost effectiveness of introducing two phase water supply tariffs (ie connection charge & consumption charge).

2.2.6 Local Government Legislation Amendment Bill (No 3) 1997

The major focus of the Bill is to provide a mechanism in the Local Government Act 1993 for complaints about local government business activities which are not abiding by the competitive neutrality principles that apply to such activities.

It includes provision for an in-house complaints mechanism for the smaller type three business activities where a local government has chosen to apply the code of competitive conduct.

The approach taken is modelled on that of the Queensland Competition Authority which deals with complaints about competitive neutrality matters in respect of state government business activities. The Competition Authority has a role to play in
independently dealing with local government complaints. However the Bill provides for the complaints mechanism to be structured according to the size and significance of the business activities.\(^9\)

### 3. COMPETITION PRINCIPLES AND LOCAL GOVERNMENT

#### 3.1 COMPETITION PRINCIPLES AGREEMENT

Generally speaking, the Competition Principles Agreement obligates the Commonwealth, state and territory governments to apply the principles contained in the agreement to the business activities under their control, including those of local government. Clause 7 of the Agreement specifically stated that the NCP principles were to apply to local government.

The principles outlined in the Competition Principles Agreement were grouped under the following headings:

- Prices oversight of government business enterprises (Clause 2),
- Competitive neutrality policy and principles (Clause 3),
- Structural reform of public monopolies (Clause 4),
- Legislation review (Clause 5),
- Access to services provided by means of significant infrastructure facilities (Clause 6).

The objective of this Research Bulletin is to outline how the application of these competition principles will impact on the activities of local authorities.

### 4. PRICES OVERSIGHT OF LOCAL GOVERNMENT BUSINESS ENTERPRISES

Nationally, monopolies or near monopolies in the private sector have for some time been subject to pricing evaluations by an independent authority which was formerly known as the Prices Surveillance Authority, now part of the Australian Competition and Consumer Commission.

The rationale is that if a business (whether Commonwealth, state or local government owned) is corporatised or commercialised there should be some

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mechanism that takes away from government, as the owner, the absolute right to set pricing.\textsuperscript{10}

As the local government sector was not a direct signatory to the Competition Principles Agreement, the available options for ensuring that local government activities are incorporated fully into NCP with respect to pricing oversight, competitive neutrality and third party access are:

- firstly, that each local authority could make its own arrangements,
- secondly, that a single authoritative arrangement could be made to cover all local authorities, and
- thirdly, that an authoritative arrangement could be made to include local government business activities with those of state government business activities.\textsuperscript{11}

The consultancy report completed on behalf of the Australian Local Government Association concluded that the elements involved in the overseeing of prices would have minimal effect on local government. This conclusion was based on the following:

- that the overseeing of prices would only apply to local government business activities that are significant and are involved in the supply of goods and services to the community on a monopoly basis (e.g. water and sewerage services).

- the application of significance tests to business activities, although they may vary from state to state, will result in only a small number of local authorities being affected.\textsuperscript{12}

The Queensland Government policy statement on National Competition Policy and Queensland Local Government published in July 1996 specifically stated that monopoly and near-monopoly business activities at the local authority level would be subject to authoritative pricing oversight arrangements that may be implemented by the state government if a state based-regime was introduced. Water supply and sewerage were nominated in the policy document specifically in this regard.\textsuperscript{13}


The CPA required States to consider establishing independent sources of prices oversight for significant state-owned monopoly and near-monopoly businesses.\textsuperscript{14} Such a body was created early in 1997 being the Queensland Competition Authority. This body also has jurisdiction for pricing oversight of local government owned monopoly or near-monopoly significant businesses.\textsuperscript{15} The function of pricing oversight on the part of the Queensland Competition Authority will in effect place the Authority in the category of an accountability “watchdog”.

Under the Queensland Government Policy Statement, the overlooking of the pricing of local government services would only apply to services that are conducted on a commercial basis. Services which are subsidised by Commonwealth or state or local government for the purposes of meeting a community service obligation would not be subject to prices oversight.\textsuperscript{16}

The Policy Statement further explained that in setting thresholds for those businesses to be subject to pricing oversight:

\begin{quote}
...a balance must be struck between the costs associated with prices oversight and the gains the process offers. Applying prices oversight to very small local government businesses even if they are monopolies, is unlikely to yield net benefits in a state or national context.\textsuperscript{17}
\end{quote}

The proposed threshold for overseeing of local government monopoly and near-monopoly activities would be based on businesses which \textit{accrue} more than $5m per year in 1992-93 terms in fees and charges, or $7.5m per year in 1992-93 terms in the case of water and sewerage activities combined.

Whilst the 1996 Policy Statement suggest that the Queensland Competition Authority will be the pricing oversight authority for local government significant business activities, this has not yet been provided for in legislation. Any legislation is not likely until early 1998.

\section{5. COMPETITIVE NEUTRALITY AND LOCAL GOVERNMENT}

Government business activities make up about 10\% of the national economy. The reform of government business activities so that they are more competitive has the potential to improve the efficiency of the whole economy because the goods and

\begin{flushleft}
\textsuperscript{14} Clause 2(3) of the Competition Principles Agreement.

\textsuperscript{15} s 18, \textit{Queensland Competition Authority Act 1997} (Qld).


\end{flushleft}
services they produce are important inputs to the production of other goods and services.

The Competition Principles Agreement states that the objective of competitive neutrality is the elimination of resource allocation distortions that exist in publicly owned entities engaged in significant business activities.\textsuperscript{18} These distortions may exist in the form of waste (inefficiency), over supply (spending too much on a good or service) or under supply (spending too little on a good or service).

The NCP reforms are intended to provide a regime whereby government business activities operate without any significant advantages or disadvantages as a result of government ownership ie they will become competitively neutral. Whilst some government businesses enjoy advantages in that they do not pay dividends and financing is cheap, others have disadvantages in that they need to meet a range of public sector accountability requirements including meeting community service obligations.

The principle is that the application of competitive neutrality identifies distortions in the market and then alleviates them through the operation of the price level that is best suited to the good or service concerned.\textsuperscript{19} However, there needs to be an organisational structure in place that is best suited to operate in a competitive environment.

The Competition Principles Agreement requires governments to consider three options in deciding whether or not to apply competitive neutrality:

\begin{itemize}
  \item[a)] full cost pricing,
  \item[b)] commercialisation,
  \item[c)] corporatisation.
\end{itemize}

Public corporations operating under an environment of competitive neutrality will be doing so with no preferential treatment from government ie in a competitive environment. This results in a similar situation to the relationship between private sector corporations and government. Hallmarks of this are:

\begin{itemize}
  \item the removal of government financial guarantees or, if this continues, the payment of a fee for this service,
  \item the imposition of taxation liabilities to the Commonwealth and state,
  \item the payment of government charges,
  \item the adoption of adequate returns in relation to the level of investment,
  \item receipt of government payments only in return for providing community service obligations.
\end{itemize}

\textsuperscript{18} Clause 3(1) of the Competition Principles Agreement.

Any business structure that results in either the payment of outgoings to higher levels of government or the accommodation of the value of such outgoings even if they do not actually occur, would require the generation of enough extra income to cover these financial obligations or at least the accommodation of them, when fixing prices. That is why under the Competition Principles Agreement the expectation of the achievement of competitive neutrality via corporatisation or commercialisation will not apply to non-business, non-profit activities of local authorities. They simply would not provide enough income (if at all).

Where competitive neutrality is applied in terms of full cost pricing, it will not interfere with the capacity of a local government to subsidise the provision of a good or service to particular groups; provided that where a community service obligation is made, the level of payment is readily identifiable in public accounts.

Competitive neutrality reforms will only apply to those activities where the most gains can be made ie what could be regarded as “significant business activities” of local government.

Two types of significant business activity have been defined and some examples have been supplied.

**Type 1 Business Activities.**- The activity has current expenditure, in the case of water and sewerage enterprises combined, greater than $25 m pa or, in the case of other enterprises, greater than $15m pa in 1992/93 terms. Activities under this category are: Brisbane public transport; Brisbane and Gold Coast garbage; and Townsville, Logan, Ipswich, Gold Coast and Brisbane water and sewerage.

**Type 2 Business Activities** - The business activity has a current expenditure in the case of water and sewerage enterprises combined, greater than $7.5 m pa or, in the case of other enterprises, greater than $5 m pa in 1992/93 terms. Activities under this category are garbage services of Cairns, Ipswich, Logan, Maroochy, Townsville; and water and sewerage services of Caboolture, Cairns, Hervey Bay, Caloundra, Mackay, Maroochy, Noosa, Pine Rivers, Redland, Rockhampton, Thuringowa and Toowoomba councils.

These are examples only and it has been suggested by Treasury that councils rely on their own audited statements for identifying Type 1 and Type 2 business activities discounted back to 1992-93 prices for the purposes of public benefit assessment.

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20 Clause 3(1) Competition Principles Agreement.


Chapter 7A of the Local Government Legislation Amendment Act 1996 No 81 requires the 17 largest councils in Queensland to carry out a **public benefit assessment** to ascertain whether competitive neutrality reforms should be applied to their water and sewerage services, garbage services, and in the case of Brisbane City Council as one of the 17, its public transport services. The main competitive neutrality reforms have been focussed on these 17 councils because they account for about 80% of all local government expenditure on these business activities.\(^{23}\) (See Appendix A for a table of business activities of the Councils specified in Chapter 7A s 458C of the Local Government Legislation Amendment Act 1996 No 81.)

There will be local authorities in Queensland which will have the potential of being subjected at some time in the future to public benefit assessment. The biggest single step that would bring them closer to the criteria threshold amounts would be amalgamations. Amalgamations result in an increase in the value of assets of business activities as well as an increase in overall annual expenditure to the one single authority that is created. The one single authority becomes far more likely to exceed the criteria threshold than the two previously independent smaller ones.

Not only are amalgamations more likely to bring individual local government’s closer to the criteria threshold but it is also possible that the same could apply to two or more councils that cooperate by agreeing to create a single corporation based on a common business activity.\(^{24}\)

### 5.1 **Public Benefit Assessment**

Before any competitive neutrality reforms can be implemented they must be the subject of public benefit assessment designed to determine whether the benefits outweigh the costs of corporatising, commercialising or applying full cost pricing to the nominated activities. Only in cases where it has been identified that the benefits of implementation of reform outweigh the costs, will implementation go ahead. This in itself is a major task and it will require a rigorous approach to identifying the costs and benefits.

The 17 identified local authorities were required to carry out public benefit assessments by 30 June 1997. This was permitted to be extended to 30 September

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with the approval of the Minister for Local Government.\textsuperscript{25} They have until the end of December 1997 to pass a resolution as to whether any of the reforms should be implemented.

The corporatisation and commercialisation reforms will not be suitable for all business activities in any local authority in Queensland. They will only be suitable for some business activities in some councils. The essential “yardstick” that has been used in the application to local government is the size of annual financial current expenditure of the activity concerned.\textsuperscript{26} As was stated in the Commissin of Audit 1996 report, for Type 1 and Type 2 activities:

\begin{quote}
... if it is shown to be appropriate through a public benefit assessment, the local government is to implement a corporatisation model or a business unit model with an equivalent regime and the imposition of debt guarantee fees and regulation equivalent to that applied to the private sector.\textsuperscript{27}
\end{quote}

\section*{5.2 Corporatisation}

The 1990 Green Paper on Government Owned Enterprises\textsuperscript{28} stated that successful corporatisation depends heavily upon the imposition of the following:

\begin{itemize}
  \item the establishment of clear objectives of the corporation;
  \item the recognition that corporate management must have sufficient autonomy and authority to manage the corporation;
  \item that in line with managerial autonomy and authority, management must be held strictly accountable for performance of the corporation; and
  \item that government owned corporations are to operate on a basis of competitive neutrality without assistance from government that would in some way extend competitive advantages not available to the private sector.
\end{itemize}

Corporatisation for the purposes of the NCP and local government involves the restructuring of a local government business activity so that it operates on a commercial basis as a separate legal entity while remaining under local government ownership. The corporatisation of a business activity at the local government level will allow that corporation to concentrate solely on the supply of the good or

\textsuperscript{25} s 458L \textit{Local Government Act 1993} as inserted by \textit{Local Government Legislation Amendment Act 1996}.

\textsuperscript{26} s 458AC \textit{Local Government Act 1993}, as inserted by \textit{Local Government Legislation Amendment Act 1997}.


service. It entails the establishment of a corporate structure that separates the responsible provider entity from the accountable local authority but with the latter still retaining ownership and receiving dividends from the corporation if they are to be paid (the purchaser/provider model).

The decision to corporatise a local government business activity will be heavily dependent on the benefits to the community outweighing the costs determined by a public benefit assessment. Part of the cost will be the creation of a corporate structure itself. In this regard, only business activities that are capable of supporting a corporate structure can be reformed in this way. The *Local Government Act 1993* now details a model of corporatisation for significant local government business activities.\(^{29}\)

Part 6 of the *Local Government Act 1993* provides for the following:
- the establishment of corporations to carry on significant business activities;
- the preparation of corporatisation charters; and
- the operation of corporations.

The Act sets out a staged process for corporatisation involving:
- a local government proposing that a part of its significant business activity be acquired by a corporatised corporation;
- the nomination of that part as a candidate LGOC or a candidate subsidiary of an LGOC;
- the preparation and approval of a corporatisation charter for the candidate LGOC;
- the establishment of a significant business entity as a separate legal entity to acquire the relevant part of the significant business activity once it becomes a corporatised corporation; and
- the significant business activity entity becoming a corporatised corporation.\(^{30}\)

The last step is necessary so that the transfer of the business assets from the Council to the corporation is recognised for tax purposes.

At the top of any corporate structure sits a board of directors. Under the 1997 amendments to the *Local Government Act 1993*, elected councillors cease to be councillors if they are appointed as a director of a significant business activity board


in any capacity external to their elected council positions. However, local authorities will have the power to appoint two councillors as shareholder delegates (of the council) to the board of the corporatised entity without their positions as councillors being affected. Councillors cannot be employees of a significant business entity. (458FF LG Act).

Part 6 of the Local Government Act 1993 provides a model for local government owned corporations. The Act provides for councillors and council employees to be directors of an LGOC provided that such appointments are based on merit and are subject to checks and balances, eg no such appointments can be made to a subsidiary of an LGOC. As pointed out at the time the amending Bill was passing through Parliament:

*In effect greater separation and a more commercial focus can be achieved by a council creating only one LGOC as a holding company and having fully commercially focussed boards on the subsidiaries. The LGOC would monitor the performance of its subsidiaries and have input into their strategic direction.*

The checks and balances for councillors and council employees as directors of LGOCs include —

- restrictions on their number and a phasing out of their membership on boards other than where there is a pure holding company LGOC;
- a requirement that such directors must act in the best interests of the LGOC when attending board meetings; and
- making sure that a minimum number of the directors of an LGOC are not councillors, council employees or employees of the LGOC.

Whether or not councillors or council employees acting as directors is an appropriate approach in the long term will be reviewed on the basis of how this system operates over the next few years. The Bill specifically provides that the Minister must carry out such a review. As part of this review the desirability of having councillors potentially fulfilling both the roles of delegate shareholders and LGOC directors will also be assessed.

Board members would be subject to similar legal responsibilities and duties to those directors in private corporations. Under the corporate model, directors can be

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31 s 173A Local Government Act 1993 as inserted by Local Government Legislation Amendment Act 1997. See s 458FE also which provides for restrictions on councillors and employees being directors of a LGOC.

removed from the board just as in any private sector corporation with accountability for performance and results being a determining factor.

The corporate entity would be responsible for the provision of goods and services on a commercial basis. Local and or state government may pay the corporation subsidies for the provision of services that it would not otherwise provide for commercial reasons, such subsidies being dependent on the identification of community service obligations. These obligations, provided by government to the community generally, manifest themselves in either government directives to government owned enterprises to depart from what would otherwise be commercial decisions regarding the pricing and conditions of supply of services or as a result of a specific decision on the part of the LGOC board which meets the satisfaction of the shareholders.

At the local government level, community service obligations such as pensioner concessions in the form of rate rebates, the provision of some bus services, the supply of free public library services to the community, and the supply of free playground equipment are not hampered by NCP. The Competition Principles Agreement provides some direction about the delivery and funding of community service obligations through council business activities.

A recent House of Representatives Report concluded that there is no universal acceptance as to exactly what are community service obligations. Notwithstanding this, the House of Representatives Committee reported that the definition of community service obligations prepared by the Steering Committee of the National Performance Monitoring of Government Enterprises had been widely accepted, this definition being:

> A Community Service Obligation arises when a government specifically requires a public enterprise to carry out activities relating to outputs or inputs which it would not elect to do on a commercial basis, and which the government does not

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require other business in the public or private sectors to generally undertake, or which it would only do commercially at higher prices.  

The Local Government Amendment Act 1997 specifically defined community service obligation in the case of a corporatised local government corporation as obligations to do anything that the corporation’s board establishes to the satisfaction of the shareholder —

- are not in the commercial interests of the corporation to do; and
- arise because of a direction by the corporation’s local government to its LGOC; and
- do not arise because of the application of the principles of corporatisation being:
  
a) strict accountability; and
b) competitive neutrality.

5.2.1 The Commonwealth and State Tax Position for Local Government Owned Corporations (LGOCs)

The Queensland Government legislated in 1997 via the Local Government Legislation Amendment Act No 23 by inserting s 458JG into the Local Government Act 1993 to provide that councils will not be required to pay additional State taxes if their business activities are corporatised. The Commonwealth has not yet put in place such an arrangement for local government business activities. Although State owned government corporations are exempt from Commonwealth taxes, the position regarding local government corporations has not been determined. Intergovernmental discussions on this matter have been complicated by the consideration by the Commonwealth of more global reforms to taxation structures in Australia. Until this matter is resolved, it is likely that local governments will be cautious about making decisions as to corporatisation.

5.3 COMMERCIALISATION

Commercialisation is not so different from corporatisation in that the goals are still the same; the production or delivery of goods and services in a cost efficient

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manner for which the corporation can be held accountable. For local government commercialisation involves the operation of a business activity on a commercial basis as far as possible within the legal auspices of the local government. It also involves the application of full cost pricing.

Unlike the corporatisation process, the process of commercialisation does not create a structure responsible for the provision of the good or service separate from the local authority as a legal entity. Under a commercialised structure Commonwealth and state taxes and charges will not be imposed. This is because the business activity is still regarded as a direct arm of local government. However, there is an expectation that the level of such taxes and charges even though they are not being imposed are to be taken into account when determining the price structure of the good or service. On this basis, a commercial structure may possibly be more financially profitable to local authorities.

5.4. CODE OF COMPETITIVE CONDUCT AND TYPE 3 BUSINESS ACTIVITIES

Business activities that fall below the financial threshold for type 1 and 2 business activities ($25m and $7.5m respectively for water plus sewerage and $15m and $5m respectively for other activities) have been designated type 3 activities or Chapter 7B business activities. They are activities in goods and services that are undertaken by local government in direct competition with the private sector. Councils must decide whether or not to apply the Code of Competitive Conduct to these activities. The Code is designed to apply competitive neutrality principles by means of full cost pricing. Councils will need to make pricing decisions having regard to the full cost of providing goods or services through the business activity, including estimates for taxes that would be payable if the activity were carried out by the private sector.

The Code of Competitive Conduct is contained in the Local Government Finance Amendment (No 2) gazetted on 24 October 1997 (SL No 360 1997).

Clause 72, Application of full cost pricing, states:

In deciding charges to clients for goods and services provided in carrying on an activity, a local government must ensure the projected total revenue from carrying on the activity is enough to cover the

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40 Chapter 7B of the Local Government Act 1993 provides for the conduct of competitive business activities under the Code of Competitive Conduct.

projected total costs of carrying on the activity for the local government’s financial year or a longer period (not more than 5 years) decided by the local government.

The total costs of carrying on an activity include:

- operational costs incurred in carrying on the activity;
- administrative and overhead costs;
- cost of resources used in carrying on the activity;
- depreciation;
- equivalents for Commonwealth or State taxes the local government is not liable to pay because it is a local government;
- equivalents for the cost of funds advantage the local government obtains over commercial rates of interest because of State guarantees on borrowings;
- return on capital.\(^\text{42}\)

The types of Chapter 7B (Type 3) business activities include footpath construction and maintenance; some road construction and maintenance; off-street parking; and sporting and recreational facilities.\(^\text{43}\)

Roadworks to which the Competitive Code must apply are classified into three designated categories, being:

- roadworks on state controlled roads put out to tender; and
- roadworks on local authority roads that are put out to tender for which the local authority also tenders or another local authority tenders, as well as private sector tenders; and
- roadworks on another local authority’s roads, that are subject to a competitive tender to other local authorities and private contractors.

As from January 1998 all local authorities tendering for Main Road’s contracts will be required to have implemented the Code.\(^\text{44}\)

With respect to the other type 3 business activities (Chapter 7B business activities) the application of the Code will be voluntary, although once a council has resolved

\(^{42}\) Clause 74(1) Local Government Finance Amendment Standard (No 2), SL No 360 1997.

\(^{43}\) s 458MD Local Government Act 1993 (Qld).

to apply the Code to a business activity then it must do so. The initial decision needs to be made by 1 July 1998 and reviewed in each financial year after that. It is expected that any decision to apply or not to apply the Code to particular activities will be made after the completion of a public benefit assessment. Such an assessment is not expected to be as extensive as that required for type 1 and 2 business activities. Guideline for the undertaking of competitive neutrality cost-benefit assessment have been developed conjointly by the Department of Local Government and Planning and Queensland Treasury.

Chapter 7B of the Local Government Act 1993 and the Local Government Finance Amendment Standard (No 2) also set out the accountability requirements for business activities affected by the Code of Competitive Conduct. In applying the Code local authorities will be required to:

- Apply competitive neutrality by using cost pricing; and
- Establish a complaints and dispute resolution process; and
- Indicate in annual reports instances where the Code is being applied.

6. STRUCTURAL REFORM OF MONOPOLIES AND THE ISSUE OF PRIVATISATION

Many local authorities in Queensland as in other states, do have a monopoly on the provision of some services. Water and sewerage services and refuse collection and disposal are the most recognisable. The Competition Principles Agreement addressed the issue of the introduction of competition into sectors that have traditionally operated under public monopolies. The Agreement recognised the possibility of the privatisation of public monopolies after the completion of a review that considered:

- the appropriate commercial objectives of the public monopoly
- the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly;
- the merits of separating potentially competitive elements of the public monopoly;

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45 s 458 MF Local Government Act 1993 (Qld).
• the most effective means of separating regulatory functions from commercial functions of the public monopoly;
• the most effective means of implementing the competitive neutrality principles set out in the agreement;
• the merits of any community service obligations undertaken by the public monopoly and the best means of funding and delivering any mandated community service obligations;
• the price and service regulations to be applied to the industry; and
• the appropriate financial relations between the owner of the public monopoly and the public monopoly, including the rate of return targets, dividends and capital structure.49

On the issue of privatisation there have been a number of statements made in both the national and state parliaments. For instance in the national parliament:

In particular the [competition policy] agreement, and indeed the package of reforms in total, does not compel, or even encourage, governments to privatise government business enterprises ... The package, as with the report of the Hilmer committee, is silent on the issue of public versus private ownership. The agreement sets out certain processes that should be followed where a government business enterprise is to be privatised or exposed to competition for the first time. The decision as to whether, and when, a government business enterprise might be privatised remains the exclusive responsibility of the owning government.50

In the Queensland parliament:

... the reforms should not be seen as a catalyst to privatisation. Nothing in the Bill compels any privatisation of Government functions. Accordingly, the Bill should not be viewed as one which threatens to dismantle any part of the public sector in this State.51

... the reforms do not involve privatisation or the compulsory tendering out of any local government activities.52

The issue of privatisation was also canvassed in the consultant’s report completed on behalf of the Australian Local Government Association. In relation to privatisation at the local authority level the report stated:

49 Clause 4(3), Competition Principles Agreement.
There is no information available to the consultants which would suggest that any state government has it in mind to privatise (ie transfer the ownership of) any business activities now owned or operated by local government, nor is there any reason to believe that such a development is likely in any significant respect. A similar comment applies in relation to the introduction of private sector services directly in competition with what are currently local government monopolies. If any changes of this kind were to be contemplated, the circumstances would be unusual and any analysis at this stage would be hypothetical and very unlikely to be of value.\(^{53}\)

From statements such as these, it seems clear that the National Competition Agreement is not being interpreted as a basis for the privatisation of public assets or functions.

7. TIMETABLE FOR REVIEW OF LOCAL GOVERNMENT LEGISLATION

The state government has the responsibility under the Competition Principles Agreement to review all state legislation for the purpose of identifying any existing anti-competitive provisions.\(^{54}\) This review process commenced in December 1995 and is being coordinated by the National Competition Unit within Queensland Treasury.\(^{55}\) The legislative review timetable produced by the National Competition Unit has allocated a rolling period between December 1995 and June 1999 to review all existing relevant legislation as of 30 June 1996 and subsequent to that date.\(^{56}\)

The pieces of legislation that are concerned with local government and fall within the administrative responsibility of the Department of Local Government and Planning will be reviewed between 1997 and 1999. This includes local government laws (by-laws) and the model local laws made under the authority of the Local

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\(^{54}\) Clause 5, *Competition Principles Agreement*.


Government Act 1993. The relevant legislation is listed below.

<table>
<thead>
<tr>
<th>Legislation</th>
<th>Proposed Review Time</th>
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<tbody>
<tr>
<td>City of Brisbane Act 1924</td>
<td>1997-1999</td>
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<tr>
<td>Local Laws (formerly by-laws) made under the authority of the</td>
<td>1997-1999</td>
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<tr>
<td>Local Government Act 1993 and the City of Brisbane Act 1924</td>
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<tr>
<td>Building Act 1975 and Regulations</td>
<td>1998-1999</td>
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</tbody>
</table>


Individual local governments will review their own specific local laws in accordance with a methodology which is agreed between Treasury and the Local Government Association of Queensland, the Department of Local Government and Planning and the Business Regulation Review Unit of the Department of Tourism, Small Business and Industry.

The consultant’s report to the Australian Local Government Association pointed to the complexity of such reviews as they would involve the consideration of competing objectives: the objective of the most efficient accountable allocation of resources and the objective of fulfilling community service obligations. The report further drew a distinction between “regulatory” and “anti-competitive” as it relates to local government. There are many regulations in relation to planning and building but they are not necessarily anti-competitive in the sense that they are not designed to determine the number of businesses or operators operating in a market. They are primarily concerned with standards of products and conduct applicable to those products (ie. workmanship).

The overall objective of the review of local laws should be to accommodate as far as possible the objective of minimising inefficiency in resource allocation with the traditional objective of local government of ensuring and providing a safe and livable natural and built environment in which community members can live and work. The

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central issue to the review of local laws is to identify those laws that are inhibiting the efficient allocation of resources in either the public or private sector and, once having identified them, to ascertain whether they do so with just reason.

Local authorities can conduct the reviews themselves by establishing a review group internally or they may choose to employ consultants to complete the process on their behalf. In either case there will need to be a final report containing recommendations for a final decision by council. As there is a continuing role for local government in reviewing existing and future local laws in relation to competitive restrictions the use of consultants to establish a framework for such an ongoing review may also be attractive to some councils.

7.1 **The Review Process - The Local Government Level**

The 17 local authorities that have been identified as having types 1 and 2 business activities were required to identify by July 1997, local laws that contain anti-competitive provisions. These councils are to complete their assessment of identified anti-competitive provisions by June 1999.

The process will also concern councils that do not operate type 1 and 2 business activities. These councils will be required to identify anti-competitive provisions within their local laws by January 1998 with the assessment due by June 1999.

The elimination of anti-competitive provisions in local laws will only be required where it can be shown that the cost of such anti-competitiveness outweighs the benefits. The identification and assessment process entails the aspects of (i) identification of local laws to be reviewed, (ii) identification and clarification of the objectives of the local laws (iii) identification of the anti-competitive provisions, (iv) identification of the nature of the restriction, (v) analysis of the effect of the restriction on competition, (vi) analysis of the cost and benefits (vii) consideration of other means of achieving the stated objectives of the local laws.\(^{58}\)

**(i) Identification of local laws to be reviewed**

The objective of this stage is to eliminate irrelevant local laws allowing a schedule or list of the relevant local laws to be established that will be the subject of further action. For instance, local laws concerned with the control or management or running of caravan parks would have a relationship with a private sector activity whilst a local law forbidding the kicking of footballs within a specified distance of overhead electrical lines would not.

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(ii) Identification / clarification of objectives

The objective of this stage is to “highlight” the basic problem that the local laws that were included in stage (i) were designed to regulate.

A number of local laws may have more than one objective. For example a provision in a local law relating to a leaky awning or balcony over a road may have the twin objective of public safety as well as making a contribution to the amenity of the built environment.

Ideally, the provisions contained within a local law should be aimed at achieving the overall objective of the law. The correct identification of the objectives of local laws is also important because it again becomes the corner stone of complying with step (vii) of the process.

(iii) Preliminary identification of possible anti-competitive provisions

The objective of this stage is to establish which provisions of the local laws have the effect of restricting competition. However it is not necessary to analyse whether the restriction is good or bad, or justifiable.

The use of the term “anti-competitive,” gives a clue to the type and style of local law provisions that are most likely to fall within the category requiring review. They may have the following characteristics:

(a) they will be restrictive in nature
(b) they may create a monopoly
(c) they may establish standards
(d) they may allocate rights or quotas
(e) they may establish measures of preference.

In short, any provision that intrudes into the market place has a potential to be anti-competitive. At the local government level, the above attributes will encompass many local laws.

(iv) Identification of the nature of the restriction

The objective of this step is to identify what sort of restriction resides in the provision.

Does the provision prescribe that a particular behaviour is not to occur or does it prescribe particular behaviour that is to occur?

(v) Analysis of the effect of the restriction on competition
The objective of this step is to ascertain the effects that the restriction has on private sector participants.

One practical way is to consult with private sector participants through their relevant trade and professional associations. They would have particular views on the practical application of local laws from their perspective.

(vi) **Analysis of the cost and benefits**

The objective of this stage is to quantify as far as possible the cost of maintaining local laws as opposed to the perceived benefits that accrue.

This may be the hardest step in the process. For instance, the Business Regulation Review Unit initially planned in 1991 to require a cost-benefit analysis of each individual regime of business legislation and regulations from each government agency. However, this had to be abandoned due to the cost factor involved and the complexity of the task.\(^{59}\) There is every chance that local authorities will encounter this problem as well.

In practical terms many benefits will not be quantifiable in financial terms. For instance the preservation of natural beauty, wildlife, and community ties are all issues that are not quantifiable in financial terms. These sorts of issues may be directly or indirectly affected by restrictions in local law provisions.

(vii) **Consideration of alternate means of achieving local law objectives**

The object of this stage of the process is to consider alternate means that may be used to attain the objective of the local law provision.

This stage would apply to local law provisions that have been identified as having costs outweighing benefits. This brings up a number of alternatives ranging from implementing a strategy that lowers the cost but leaves the benefits unchanged, through to a strategy that may eliminate the restriction altogether.

Cost-effectiveness analysis asks the question that with a given objective, which is the least-cost way of achieving it? In relation to restrictions there would be two types of costs involved. Firstly, there would be an enforcement cost that falls on the local authority and secondly a cost that is incurred by the private sector in relation to compliance.

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7.2 **FINANCIAL ASSISTANCE FOR THE REVIEW PROCESS**

The States stand to gain significant financial assistance from the Commonwealth as a result of satisfactorily implementing the NCP. There is no provision for local government to necessarily share in the Competition payments which in Queensland’s case would amount to $756 million over the next 10 year period.\(^{60}\) The State Government has recognised there will be costs incurred by councils in the process of carrying out assessments. It has also acknowledged that there will be transitional costs associated with the application of full cost pricing, and the implementation of a commercial or corporate structure.

The state government has announced that it will financially assist councils. The Treasurer announced in April 1997 the allocation of $150 million over the next five years to assist local authorities in Queensland with the extra cost of complying with aspects of the NCP that are appropriate to local government. The announcement indicated that a percentage of the $150 million is earmarked to assist councils with reviews of business activities and local laws\(^{61}\) and was a response to a motion carried by the Local Government Association.\(^{62}\) The funding is drawn from the State’s competition payments of up to $756 million that it will receive from the Commonwealth. The Queensland Government has been described by the National Competition Council as being innovative in its approach to extending financial assistance to local authorities undertaking reforms.\(^{63}\)

8. **PROVIDING ACCESS TO THIRD PARTIES**

The Competition Principles Agreement allows for the possibility of access for third parties to services provided through “significant infrastructure facilities”. As the Under Treasurer has explained, the key characteristics of “significant infrastructure facilities” as they have been called in Part IIIA of the Trade Practices Act is that they cannot be economically duplicated and could be described as natural

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monopolies. The policy statement issued in July 1996 indicated that at that time it had not been decided as to whether local government infrastructure would be subject to Commonwealth or a proposed state third party access regime. At the local government level, water and sewerage infrastructure could be subject to third party access. However, for infrastructure facilities to be considered as candidates for third party access they are to be of a national significance with respect to their contribution to the national economy.

The 1996 Queensland Policy Statement discusses the possibility of third party access to local government infrastructure. The consultant’s report to the Australian Local Government Association concluded that the third party access clause would have minimal implications for local government if a reasonable test of significance were applied.

Whilst a state third party access regime has been established by the Queensland Competition Authority Act 10907 for state infrastructure, no final decision has been made as to whether local government in Queensland will be covered by this regime. At present local government is automatically caught by the Commonwealth regime established by the Competition Policy Reform Act 1995 (Cth).

9. COMPLAINTS MECHANISMS

9.1 TYPE 1 AND TYPE 2 SIGNIFICANT BUSINESS ACTIVITIES

The recently introduced Local Government Legislation Amendment Bill No 3 1997 provides for a mechanism for complaints about local government business activities which are not abiding by the competitive neutrality principles that apply to those activities. These include the Type 1 and 2 business activities of the largest 17 councils which have to be assessed for possible application of corporatisation, commercialisation or full cost pricing. The system is modelled on that of the

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64 McTaggart, p 21.
66 Clause 6, Competition Principles Agreement.
Queensland Competition Authority which deals with complaints about State owned government business activities.

There are two options:

- A less formal compliant process which places the primary onus on the local government to put in place a system to resolve complaints by appointing a referee and reporting to Council. Complainants will be able to refer a complaint to the Queensland Competition Authority if they are not satisfied by the outcome; or

- The local government could decide that the Queensland Competition Authority investigate the complaints and then the QCA would report to the local government.

If a business is accredited with the QCA then it does not require a complaints mechanism.

9.2 COMPLAINTS MECHANISM AND CODE OF COMPETITIVE CONDUCT

The Local Government Legislation Amendment Bill (No 3) 1997 provides that for business activities to which the Code of Competitive Conduct applies, a local government will be required to establish an in-house complaints mechanism. This will involve the appointment of a referee and report to Council. If accreditation of a Type 3 activity is obtained from the Queensland Competition Authority no complaints mechanism is required. Unlike with Type 1 and 2 business activities, there will be no scope for complaints to be referred to the Queensland Competition Authority if the complainant happens to be dissatisfied with the outcome of the process. The complaints mechanism must be in place by 1 January 1998.

10. COAG AGREEMENT ON WATER PRICING

As with the NCP, the Water Resource Policy developed from a report to the Council of Australian Governments (COAG) which agreed to the framework

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69 including any of its roads business activities ie where the local government lodges a tender for works on state roads, the roads of another local government or if it puts its own road works out to tender.

contained in the report. The COAG Communiqué of 1994 specified the following for urban water markets:

(i) the adoption, where cost effective, by no later than 1998 of charging based on a connection fee in conjunction with a consumption fee;

(ii) pricing regimes based on consumption, full cost recovery and removal of cross-subsidies not consistent with efficient and effective service. Continued cross-subsidies must be made transparent; and

(iii) volumetric-based charging for urban bulk water structured so as to recover all costs and earn a positive rate of return on assets.

In 1995, the achievement of water resource policy objectives as outlined in the 1994 communiqué were linked to Commonwealth payments attaching to the delivery of competition policy commitments.

Chapter 7C of the Local Government Act 1993 (as inserted by Local Government Legislation Amendment Act 1997) requires the 17 local government councils with Type 1 and Type 2 significant business activities to conduct an assessment of costs and benefits of charging for water by a two-part tariff (ie charges for access and charges for volume of water consumed) to be completed by 31 December 1998. If it is resolved that a two part tariff is to be applied then needs to be implemented by 1 July 2000 (Chapter 7C s 458NP).

As part of the water resource policy, councils other than the identified 17 will be encouraged through the use of financial incentives to introduce reforms over a five year period commencing in 1997/1998.

The focus of the reform is “on more responsible stewardship of water resources and a more commercial approach to the management of water resources”.

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11. CONCLUSION

The establishment of thresholds with respect to type 1 and type 2 business activities will initially ensure that the biggest reforms will take place in the 17 local authorities nominated in S 458C of the *Local Government Act 1993*.75 However, this is not to suggest that the remaining local authorities will be unaffected by NCP because all of these other authorities operate type 3 business activities that are also targeted for particular reforms.

There is some concern as to what the future holds for local government under NCP. Generally, the major concern is that local government stands to be transformed from an entity engaging in service delivery to one concerned with the monitoring of service delivery.76 Naturally enough, those who hold this perception have a fear that local government will lose control of service delivery which historically has been at the centre of its activities.

However, both the Commonwealth government and the state government have made it clear that they are not intent on pushing local government into re-arranging the management of their activities unless there are clear advantages to be gained. Corporatisation and commercialisation of business activities will only bring benefits when those business activities are large enough to support such re-structuring.

Some elected and appointed local government officials may feel that NCP has been “forced” upon them but with representation on the State / Local Government NCP Working Group, local government has the opportunity to influence the application of the NCP reforms.

The House of Representatives Standing Committee on Financial Institutions and Public Administration took evidence on the implications of NCP for local government. The Committee in its Report commented:

> The effects on local government generally are likely to be minimal from the principles of prices oversight of government business enterprises, structural reform of public monopolies and access to services provided by means of significant infrastructure facilities... The consensus is now that the direct and immediate implications of the Competition Principles Agreement for Local Government are likely to be more restricted in scope than many in Local Government had expected.77

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75 s 458C *Local Government Act 1993* as inserted by the *Local Government Legislation Amendment Act 1996*.


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**JOURNAL ARTICLES**


MINISTERIAL SPEECHES AND STATEMENTS


LEGISLATION

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• *Local Government Act 1993* (Qld).

• Local Government Finance Amendment Standard (No 2), SL No 360 1997.

• *Local Government Legislation Amendment Act (No 2) 1997 (No 42)* (Qld).

• *Local Government Legislation Amendment Act 1996 (No 81)* (Qld).

• *Local Government Legislation Amendment Act 1997 (No 23)* (Qld).

• Local Government Legislation Amendment Bill 1997 (Qld).

• *Queensland Competition Authority Act 1997* (Qld).
**APPENDIX A**

Source: Section 458C *Local Government Legislation Amendment Act (No 81) 1996.*

**List of local authorities designated as having Type 1 business activities**

<table>
<thead>
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<th>Local Authority</th>
<th>Water &amp; Sewerage</th>
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<th>Public Transport</th>
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**List of local authorities designated as having Type 2 business activities**

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