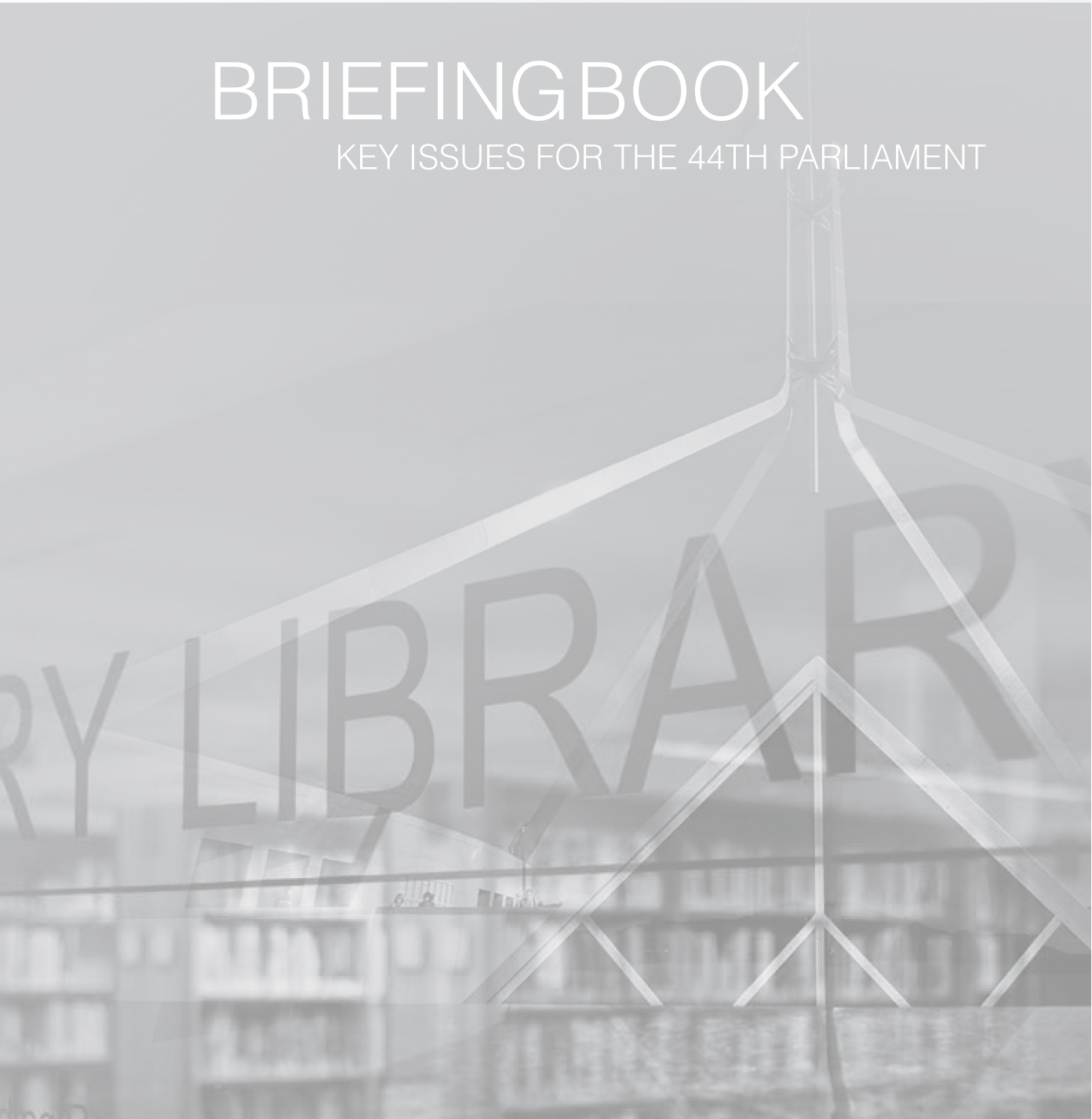


BRIEFING BOOK

KEY ISSUES FOR THE 44TH PARLIAMENT



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Foreword by the Parliamentary Librarian



Welcome to the 44th Parliament.

As we do for each new Parliament, we present this volume of short, strategic level snapshots of some of the big issues affecting Australia which are expected to figure in the early months of the new Parliament.

The articles have been written to provide Senators and Members a high level perspective of key public policy issues; to give relevant background, context and legislative history, and to discuss possible new policy and legislative directions.

The volume is organised in themes, beginning with a chapter that shows in words and charts aspects of contemporary Australia. Subsequent chapters show how Australia is faring in its economy, its public finances, and in the welfare, health and rights of our citizens. It concludes with a chapter examining Australia's relationship with the wider world, our allies and our trading partners.

As this document illustrates, the world of public policy—and thus the Parliament—continues to be a crowded and busy place. In this environment, Senators and Members are deluged with information and opinions. The Library exists to provide a trusted, expert and impartial source of information. Importantly, our service is entirely confidential.

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Dr Dianne Heriot
Parliamentary Librarian

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 - » Director, Carol Ey (ph: 6277 2724)
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 - » Director, Sue Johnson (ph: 6277 2480)

The Central Enquiry Point (02 6277 2500) can direct you to the right researcher to assist with your request.

THE 44TH PARLIAMENT



Federal Election 2013

Brenton Holmes, Politics and Public Administration

KEY ISSUE

The federal election, held on 7 September 2013, brought to a conclusion what had been a tumultuous three years – largely animated by the tensions of a hung parliament, highly partisan parliamentary politics, leadership struggles within the Labor Party, and controversies associated with Speaker Peter Slipper. The demise of Australia's first female Prime Minister, Julia Gillard, and the return of Kevin Rudd to the Labor leadership intensified the electoral contest between the major parties. A record number of parties and candidates contested the election, which delivered a Coalition Government and a Senate comprising members of the two major parties, a mix of other parties and an independent.

Redistributions

Both Victoria and South Australia had redistributions prior to the election. In Victoria, the revised boundaries resulted in 374,807 electors, or 10.77% of electors, changing division. In South Australia 44,402 electors, or 4.01% of electors, changed division.

Voters, candidates and parties

A total of 14,712,799 people enrolled to vote in the 2013 federal election, an increase of over 624,000 since the last election. Despite a growth in youth enrolment of 25,000 since the 2010 election, an estimated 400,000 young voters failed to enrol. An estimated 1.22 million – the equivalent of 12 electorates – remained unenrolled across all age groups.

A record 1,717 candidates contested the election, compared to 1,198 in 2010—an increase of 43%. This national figure was comprised of 529 Senate candidates for the 40 Senate vacancies and 1,188 candidates for the 150 Representatives seats. There

were 470 female candidates and 1,247 male candidates. Altogether, 265 group voting tickets were accepted. The Australian Electoral Commission registered 54 unrelated parties plus 23 branches of the major parties.

The build-up to the election campaign

In January 2013, Julia Gillard had taken the unusual step of announcing a proposed election date of 14 September 2013. When Kevin Rudd replaced her as Prime Minister on 26 June, election date certainty evaporated. Opinion polls had consistently pointed to a substantial Coalition victory, but Rudd's return produced a resurgence of Labor's electoral prospects. Rudd began to move on several fronts: Labor Party reform, a faster transition to an emissions trading scheme, a major toughening of asylum seeker policy, and an Economic Statement that revealed ongoing deficits with a return to surplus in 2016–17. He then announced an election date of 7 September.

The campaign

The opening day of the campaign was notable for the strident headlines from some News Corporation mastheads calling for the defeat of Labor. Economic concerns quickly became the dominant campaign theme, and the major parties continued to trade blows over policy costings, alleged changes to the GST, and support for the motor vehicle and other industries. The Coalition had elected to use the Parliamentary Budget Office to verify its costings and to have these audited by an independent panel.

The numerous small parties on offer received little mainstream media attention—although occasional headlines highlighted the presence of parties led by Bob Katter, Clive Palmer and Wikileaks' Julian Assange.

The Prime Minister and Opposition Leader held their first debate at the National Press Club on 11 August. The economy dominated the exchange – although the issues of climate

change, asylum seeker policy, Sydney's second airport, aged care, and same-sex marriage were also addressed. Several debates were later held between key portfolio ministers and shadow ministers.

The publication of Treasury's Pre-election Economic and Fiscal Outlook prompted exchanges over the major parties' economic credentials, and the nature and timing of any return to a Budget surplus. Sexism also surfaced as an issue on the campaign trail and the Coalition's paid parental leave scheme became one of its most controversial policies. Asylum seeker policy continued to animate public discussion.

The Greens electoral prospects were somewhat undermined by the Coalition's decision to preference Labor, and Independent Senator Nick Xenophon's decision to run a split preference ticket.

A fortnight before polling day, a Fairfax-Neilsen poll showed Labor lagging behind the Coalition 47%–53% and indicated that 70% of voters were expecting a Coalition win.

A second leaders' debate in the style of a community forum was held in Brisbane on 21 August, and a third on 28 August at Rooty Hill in Sydney's western suburbs. The Opposition had by then released details of \$31 billion in savings, but had to weather constant criticism for not declaring its 'budget bottom line'.

The Coalition officially launched its campaign on 25 August, and Labor a week later. The final week of the campaign failed to improve Labor's position in the main opinion polls. The Coalition released more policy costings on Thursday 5 September, claiming it would improve the budget bottom line by over \$6 billion. The Coalition had indicated the possibility of a double dissolution if a victorious Coalition's key policies were to be frustrated in the Senate.

The outcome

The Coalition had a decisive win in the House of Representatives, with a two party preferred vote of 53.45% to Labor's 46.55%—a two-party swing of 3.65%. Labor's primary vote fell to 33.38%, its lowest in over 100 years.

Despite a national swing of 3.11% against the Australian Greens, deputy leader Adam Bandt retained his seat of Melbourne. Tasmanian

independent Andrew Wilkie was re-elected with an increased majority.

The Coalition won 90 seats, Labor 55 seats, with the remainder going to small parties (3)* and independents (2).

The Senate proved to be an interesting contest, with small parties winning six of the seats. The Coalition won 17 seats, Labor won 13 seats and the Greens three seats, with one independent returned.*

The Senate outcome prompted debate about the fairness of the Senate voting system, given that the distribution of preferences delivered Senate seats to parties with a very low primary vote. The Joint Standing Committee on Electoral Matters will examine the matter as part of its inquiry into the 2013 federal election. Senator Nick Xenophon (IND, SA) has announced his intention to introduce legislation to change the Senate voting system to optional preferential below the line.

Voter turnout in the House of Representatives was 93.34% (93.22% in 2010) and 94.00% in the Senate (93.83% in 2010).

It is perhaps surprising, given the size of many Senate ballot papers, that the rate of informal voting in the Senate was lower than at the previous election, and was also lower than the informal vote in the House of Representatives. The informal vote in the House of Representatives was 5.91% and 2.96% in the Senate, compared to the 2010 informal vote of 5.55% and 3.75% respectively.

Over 3.2 million Australians voted early (pre-poll or postal) for the 2013 federal election. This compares to around 2.5 million in 2010.

Over 1.3 million postal vote applications were received for the 2013 federal election. This compares to just over 950,000 in 2010.

* pending recounts in Fairfax and the WA senate.

Further reading

B Holmes and S Fernandes, 2010 Federal Election: a brief history, Research Paper, 8, 2011–12, Parliamentary Library, Canberra 2011.

Figures used in this brief were drawn from the Australian Electoral Commission's Virtual Tally Room as at 4 October 2013.

Composition of the 44th Parliament

Martin Lumb, Politics and Public Administration

KEY ISSUE

The 2013 election saw the retirement of 25 members of the House of Representatives and 7 senators, and the defeat of 17 members and 7 senators. The new component in the 44th Parliament will be sizeable: 37 members and 14 senators. The number of women in Parliament rises slightly.

Note: figures in this brief were drawn from the Australian Electoral Commission's Virtual Tally Room as at 2 October 2013.

House of Representatives

The federal election on 7 September 2013 saw the retirement of 25 members of the House of Representatives. This is the highest number of departures at any one election – the previous highest was 21 at the 2007 election. Seventeen sitting members were defeated. There will be 37 new members of the House of Representatives, the highest new intake since 2007. The new component constitutes approximately 25% of the House of Representatives, compared with 20% in 2010 (29 new members) and 26% in 2007 (39 new members).

The House of Representatives also sees the return of two former members, Mal Brough (LP, Fisher, Qld) and Jason Wood (LP, La Trobe, Vic.). It also sees the arrival of three former senators who recently resigned to contest seats in the House of Representatives: David Feeney (ALP, Batman, Vic.), Barnaby Joyce (Nationals, New England, NSW) and Matt Thistlethwaite (ALP, Kingsford Smith, NSW).

Senate

Of the 40 senators up for re-election, 26 were re-elected. Seven did not contest the election and 7 were defeated. The 14 new Senators will comprise approximately 18% of the Senate as from 1 July 2014, equalling the previous highest intake following the 2007 election. This also compares with 12 new senators (16%) after the 2010 election.

Gender

Following the election, the number of women in the House of Representatives has risen from 37 (25%) to 39 (26%). When the new senators take up their places on 1 July 2014, the number of women in the Senate will decline from 30 (39%) to 29 (38%). Overall the number of women in Parliament will rise from 67 to 68 (30%).

Milestones

The election produced a number of notable results:

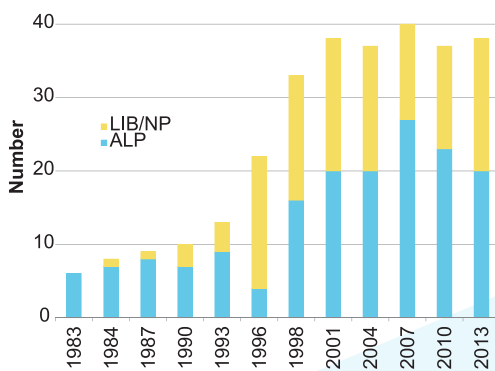
- Nova Peris (ALP, NT) becomes the first Indigenous woman elected to the federal Parliament.
- Cathy McGowan (IND, Indi, Vic.) becomes the first woman elected as an Independent to the House of Representatives. [Doris Blackburn (Bourke, Vic., 1946–49) was Independent Labor, and Pauline Hanson (Oxley, Qld, 1996–98) was a disendorsed Liberal Party candidate when elected, later forming the One Nation Party.]
- Pending a recount, the Palmer United Party looks to have secured one House of Representatives seat, its leader Clive Palmer elected to Fairfax in Queensland. Three Palmer United Party candidates were elected to the Senate: Glenn Lazarus (Qld), Jacqui Lambie (Tas.) and Zhenya Wang (WA).
- Katter's Australian Party did not secure any additional seats. Leader Bob Katter (KAP, Kennedy, Qld) retained his seat, despite a 16% swing against him.
- Candidates for three other small parties were elected to the Senate and will commence on 1 July 2014: Bob Day (Family First Party, SA), David Leyonhjelm (Liberal Democratic Party, NSW) and Ricky Muir (Australian Motoring Enthusiasts Party, Vic.). Only one of these parties has had a representative in Parliament before – the Family First Party's Steve Fielding (Vic.) was elected in 2004 and served a six-year term from 2005 to 2011.

Party representation in Parliament*

Party	House of Representatives		Senate	
	pre-election	post-election	before July 2014	after July 2014
Coalition	72	90	34	33
Liberal Party of Australia	44	58	24	23
The Nationals/Country Liberal Party	8	10	4	4
Liberal National Party	20	22	6	6
Australian Labor Party	71	55	31	26
Australian Greens	1	1	9	9
Australian Motoring Enthusiasts Party	–	–	–	1
Democratic Labour Party	–	–	1	1
Family First Party	–	–	–	1
Katter's Australian Party	1	1	–	–
Liberal Democratic Party	–	–	–	1
Palmer United Party	–	1	–	3
Independent	5	2	1	1
Total	150	150	76	76

*Pending recounts in Fairfax and the WA Senate.

Number of women in the House of Representatives 1983–2013



Source: Parliamentary Library.

Further reading

Parliamentary handbook of the Commonwealth of Australia, Parliamentary Library, Canberra.

Parliamentary Library. Politics and Public Administration Section, Composition of Australian parliaments by party and gender, as at 26 June 2013, Parliamentary Library, Canberra, 2013.

M Lumb, The 43rd Parliament: traits and trends, Research paper, 2013–14, Parliamentary Library, Canberra, 2013.

The Senate voting system: issues and suggestions for reform

Rob Lundie and Deirdre McKeown, Politics and Public Administration

KEY ISSUE

Election to the Senate of candidates from small parties with a very low primary vote.

Small party success

The Senate result at the 2013 election ignited debate about the fairness of the voting system, given that the distribution of preferences delivered Senate seats to parties with a very low primary vote. This has been attributed to the fact that most people chose to vote above-the-line, resulting in their preferences being distributed according to a pre-determined Group Voting Ticket, which is lodged by the parties with the Australian Electoral Commission (AEC) before polling day. Group Voting Tickets are published on the AEC website.

Through a complex series of preference deals, about which most voters were unaware or did not understand, candidates from a number of small parties were elected.

A similar situation occurred at the 2004 federal election when Family First's Steve Fielding (Vic) was elected to the Senate with 1.9% of the primary vote and in 2010 when DLP Senator John Madigan (Vic) was elected with 2.33%.

Size of ballot paper

Large numbers of candidates stood for the Senate (for example, over 100 candidates in NSW). This resulted in very large ballot papers that voters found difficult to manage in polling booths. Furthermore, the size of the print required polling officials to provide magnifiers so that the names could be read.

Low informal vote

The 2013 election saw a lower level of Senate informal votes than at the 2010 election, 2.96% and 3.75% respectively. It is possible that

the size of the Senate ballot paper and the requirement that people voting below-the-line number every box, encouraged most electors to simply vote '1' above-the-line, thereby reducing the chance of informality.

Confusing party name and ballot paper position

Commentators have suggested that the Liberal Democrats may have benefitted from the so-called 'donkey vote' it received by being the first party listed on the NSW Senate ballot paper. There were also reports that a number of voters had confused the name of the party with the Liberal Party.

Proposals for reform

A range of solutions have been suggested by psephologists, commentators and academics (such as Antony Green, Brian Costar and George Williams) along with former Senator Bob Brown and current Senators Lee Rhiannon (AG, NSW) and Nick Xenophon (IND, SA).

The proposals for reform can be grouped into two main approaches:

Taking the power to allocate preferences away from the parties and giving it to the voters.

The most common method advocated for returning the power of allocating preferences to voters is optional preferential voting above or below the line. Above-the-line voters would have the choice of voting for as many parties as they wished. The preferences would flow down the list of the candidates of the party they first chose and then move on to the list of candidates of the party of their second choice, and so on. This would weaken the power of Group Voting Tickets as the voter, not the party, would have the power to allocate preferences.

Alternatively, the voter could vote below the line for a limited number of candidates (six for a half-Senate election; 12 for a double dissolution). Voters would not be required to fill

in every box and would have greater control of the flow of preferences.

Optional Preferential Voting was adopted for the NSW Legislative Council after it confronted a similar situation in 1999 (250 candidates and the election of a candidate who obtained only 0.2% of the primary vote).

Reducing the number of small parties and their influence on the result.

The number of small parties could be reduced by tightening the party registration criteria and/or requiring small parties to obtain a certain level of voter support as indicated by their primary vote.

The proponents of new party registration requirements suggest such things as: each party would be required to have a larger number of members than the present 500; no person could be a member of two parties at the same time; each party would be required to pay a larger registration fee than the current \$500; each party would be required to have a constitution, hold meetings and provide minutes of those meetings; each party would have to register at least a year before the election was due and party names could not be so similar to the names of other parties as to be likely to cause confusion amongst voters.

The effect of small parties' influence on the result could also be reduced by the requirement that each party obtain a certain percentage of the primary vote, for example 4%, before the party could be involved in the distribution of preferences. Senator Joe Ludwig, a former Special Minister of State, has noted that Germany and New Zealand use a threshold of 5% while other countries such as the Netherlands, Israel, Italy, Argentina and Sweden use lower thresholds.

The party donkey vote in the Senate could be negated by rotating the position of parties on the ballot paper.

Current situation

Prime Minister, Tony Abbott, has said that the issue should be considered after the Joint Standing Committee on Electoral Matters has conducted its inquiry into the 2013 election.

Senator Nick Xenophon (IND, SA) has announced that he will introduce legislation to allow Optional Preferential Voting below-the-line.

Further reading

S Bennett and R Lundie, Australian electoral systems, Research paper, 2007-08, Parliamentary Library, Canberra, 2007.

Australian Government, Strengthening Australia's democracy, Green paper, September 2009.

Constitutional Reform — Indigenous peoples and local government

Diane Spooner and Kirsty Magarey, Law and Bills Digest

KEY ISSUE

Constitutional recognition of Indigenous peoples and of local government, were both considered by the 43rd Parliament, but neither measure was put to a referendum in the September 2013 election. Consideration of the constitutional recognition of Indigenous peoples now has a legislative framework, and its precise form and timing is set to be debated in the new Parliament and more widely. The status of local government in the Constitution will continue to be of concern and interest, and may be affected by future High Court decisions.

History

Constitutional change by way of referenda held under section 128 of the Australian Constitution is difficult, due to the requirement for a 'double majority' (a majority of people in a majority of states). As a result, referenda that do not have widespread and bipartisan support are unlikely to succeed. Only eight out of 44 referenda have been successful.

The question of recognition of local government has been put to referendum unsuccessfully twice before, in 1974 and 1988. The recognition of Indigenous people in the Constitutional preamble was put as part of the referendum on an Australian Republic in 1999. It was unsuccessful, as were two attempts to remove section 25 of the Constitution (which countenances racially discriminatory voting arrangements) in 1974 and 1988.

Local Government

The Constitution Alteration (Local Government) 2013 was passed and came into effect in 2013. The purpose of this Act was to amend section 96 of the Constitution to make specific

provision for the granting of financial assistance to local government bodies. There was subsequent argument about the Government providing uneven funding for the respective yes and no case for the referendum.

The proposed amendment to section 96, with the added words in bold, was:

Financial assistance to States and local government bodies

During a period of ten years after the establishment of the Commonwealth and thereafter until the Parliament otherwise provides, the Parliament may grant financial assistance to any State, or to any local government body formed by a law of a State, on such terms and conditions as the Parliament thinks fit.

Ultimately, the Government decided not to put the local government question to the Australian people in the September 2013 election – on the grounds that it was unlikely to succeed. This was due in part to the negativity surrounding the funding of the arguments for and against the proposal and the short time frame to conduct an education program.

By not proceeding with the referendum there will be continuing legal and constitutional uncertainty about Australian Government funding programs, such as the school chaplaincy scheme, which was rejected by the High Court.

If the Government again wishes to propose a referendum for recognition of local government, the Parliament will be required to pass another Bill to meet the requirements of section 128 of the Constitution. The current Act in effect lapses, due to the election being called. Section 128 requires a law proposing a constitutional amendment to be passed by an absolute majority of each House of the Parliament; this means the current Parliament, not the previous Parliament.

Indigenous peoples

After various considerations of the possibility of putting a constitutional referendum recognising Indigenous people, the Aboriginal and Torres Strait Islander Peoples Recognition Act 2013 commenced on 27 March 2013.

As well as providing a parliamentary endorsement of certain principles, this Act provides for an administrative review which will consider the readiness of the Australian public to support a referendum to amend the Constitution so that it recognises Aboriginal and Torres Strait Islander peoples. The review will consider proposals for constitutional changes taking into account the work of the Expert Panel on Constitutional Recognition and Reconciliation Australia.

The Expert Panel's January 2012 recommendations included:

- putting a single question to seek approval to amend the Constitution by removing race based sections (section 25, on responses to the exclusion of people from voting on the basis of race and section 51(xxvi), which gives the Commonwealth its race power) and
- creating provisions for the elimination of race discrimination, the 'advancement' of Aborigines and Torres Strait Islanders and the protection of their language and culture.

During consideration of the Act, there were concerns expressed that further reviews were unnecessary and that leaving open the final form of words to be put in a referendum was unwise. However, for the sake of bipartisan support, the decision was taken to pass the Act, with the precise form of the recommendations for change, and the final wording for any referendum proposal still to be decided. The Act simply acknowledges the work of the Expert Panel and gives some of its recommended wording parliamentary endorsement.

The more controversial aspects of upcoming discussions are likely to include whether an anti-discrimination clause should be inserted in the Constitution, and whether to provide for the advancement of Indigenous peoples.

The need to come to an agreed approach and, in particular, to agree on the precise wording of any proposed constitutional amendment, will be vital to the success of any future referendum.

The legislation ceases two years after it commenced (which will be March 2015). The review, which must be established before 27 March 2014, is required to report six months before that sunset clause – by 27 September 2014.

Further reading

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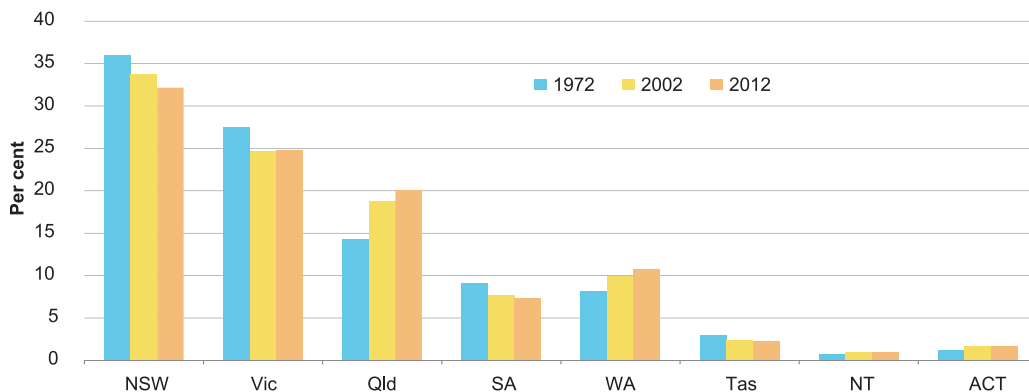
A CHANGING AUSTRALIA

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Australia in pictures

Statistics and Mapping

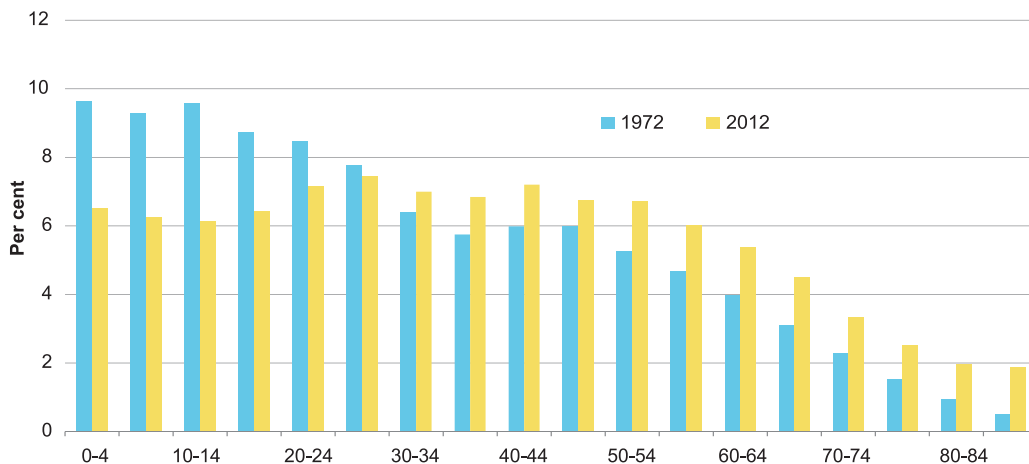
Estimated resident population by state and territory (%): 1972, 2002 and 2012



Source: Australian Bureau of Statistics (ABS), Australian Demographic Statistics, December 2012, cat. no. 3101.0 and ABS, Australian Historical Population Statistics, 2008, cat. no. 3105.0.65.001.

Overall, the proportion of Australia's population in New South Wales (NSW), Victoria (Vic.), South Australia (SA) and Tasmania (Tas.) declined from 1972 to 2012. The proportion of population in Queensland (Qld), Western Australia (WA), Northern Territory (NT) and the Australian Capital Territory (ACT) increased over the period.

Estimated resident population by age (%): 1972 and 2012



Source: ABS, Australian Demographic Statistics, December 2012, cat no. 3101.0.

In 1972, 46% of the population was aged 0–24 years, while in 2012, only 33% of the population was in this age group. Over the same period, those aged 60 years – the baby boomer generation – increased from 12% to 20%.

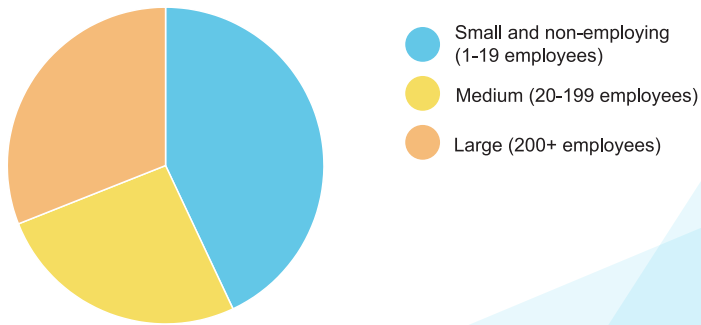
Proportion of persons (aged 15 years and over) with a bachelor degree and above: 2006 and 2011



Source: Australian Bureau of Statistics, Census of Population and Housing 2006 and 2011.

ACT residents are amongst the most educated in Australia, with 34% of the population aged 15 years and over holding a bachelor degree or higher. This compares with 21% in Vic., 20% in NSW and 18% in WA, with the lowest being Tas. at 14%.

Employment by business size: 2011–12



Source: ABS, Australian Industry 2011–12, cat. no. 8155.0.

Of all business entities in 2011–12, small businesses in Australia employed the most people – 43% of all those employed (4,649,000 people). This was followed by large businesses, which employed 31% (3,320,000 people), while medium-sized businesses employed 26% (2,758,000 people).

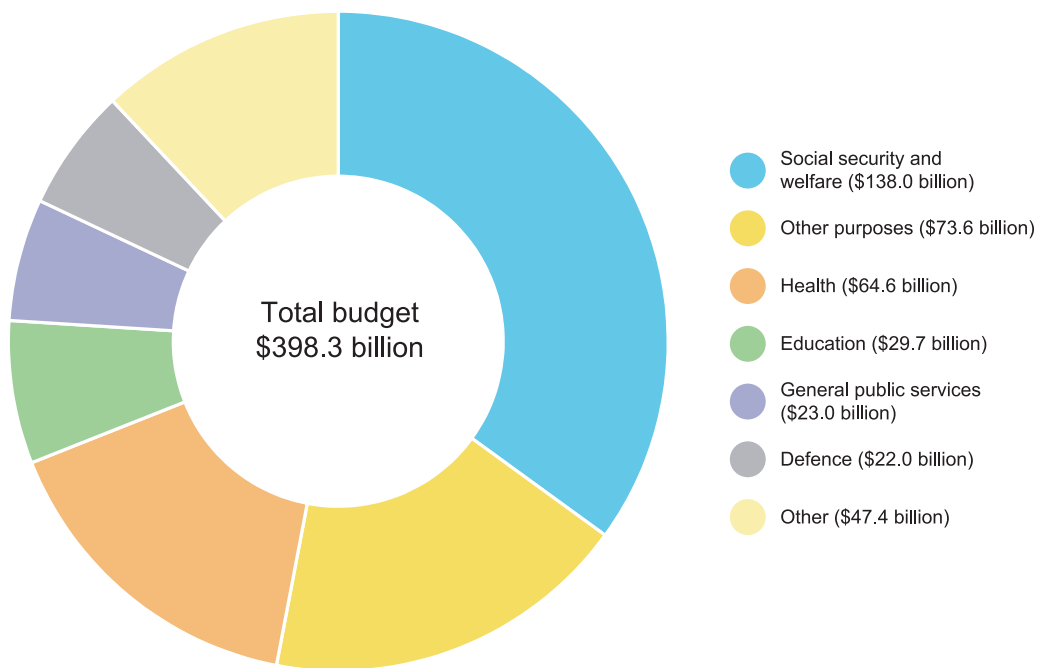
Australian budget outlays by portfolio, 2013–14

Government spending provides a wide range of services to the community. The most significant component relates to social security and welfare, with around one-third of total expenses providing support to the aged, families with children, people with disabilities, veterans, carers and unemployed people.

Another one-sixth of government expenses occur in health, including Medicare Benefits Schedule and Pharmaceutical Benefits Scheme

payments. A similar amount is also transferred to the States and Territories in general revenue assistance under the other purposes function.

There is also significant investment under the education function, supporting government and non-government schools, as well as higher education and vocational education and training. The remainder is spent on defence and a range of other public services.



Source: Budget paper no. 1, Statement 6, 2013-14

Australian government debt and fiscal position

Alan Payne and Alicia Hall, Statistics and Mapping

KEY ISSUE

In recent years, and particularly around elections, there has been significant discussion around Australia's debt levels, as well as Australia's fiscal position (that is, the Government's taxation and spending). However, to understand the real implications of debt, it helps to look carefully at what the numbers mean.

National debt is not necessarily financially dangerous or unsustainable. It depends on the wider circumstances and economists use a number of terms to measure and compare debt (see boxed text). Against these measures, and when compared against both historical and international data, Australia's economy is relatively strong.

Gross debt is the amount of money owed by an organisation. It indicates the magnitude of debt owed, but it does not show whether an organisation can repay that debt and provides limited detail about the overall financial health of an organisation (including governments).

More often reported, net debt is the sum of all liabilities (gross debt) of an organisation, less their respective financial assets (cash and other liquid assets). Net debt is one of numerous economic indicators which provide a quantitative measure of the financial health of an organisation.

For example, if a government has a gross debt that is 50% of GDP but has very little cash and or assets (high net debt) it may struggle with this level of debt. However, if a government has a gross debt of 50% of GDP but has large amounts of cash and/or assets (low net debt) then it is in a much better position to handle this level of debt.

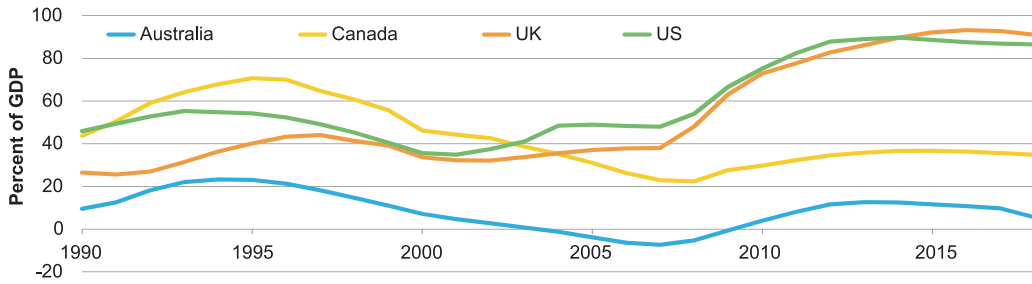
Debt is often reported as a relative indicator to allow comparison across all years, expressed as a proportion of Gross Domestic Product (GDP). In the 2013–14 Budget, the Government indicated that net debt in Australia rose from -3.8% of GDP in 2007–08 to 10.0% of GDP in 2011–12. The August 2013 Pre-Election Economic and Fiscal Outlook (PEFO) estimated that net debt would rise to 11.7% of GDP in 2013–14 and peak in 2014–15 at 13.0% of GDP. These levels of net debt are not unprecedented in Australia. Between 1970–71 and 2011–12, net debt level as a percentage of GDP exceeded 10.0% ten times (mainly in the 1990s). The chart on net debt indicates that, when compared with other advanced economies, Australia's net debt levels are comparatively low, and have been for some time.

Fiscal balance is the difference between revenues and expenditures. A negative fiscal balance implies that expenditures are larger than revenues. In this situation, an organisation is in deficit and will need to borrow money to make up the shortfall in revenues. If the fiscal balance is positive, the organisation is in surplus, which it can then save, give back to its shareholders or use to retire debt.

The chart on Australian Government revenue and expenses shows that at the time of the Global Financial Crisis (GFC), expenses increased significantly whilst revenues declined. Overall, between 1996–97 and 2011–12, Australia's fiscal balance fluctuated between a high of 1.8% (1999–00 and 2007–08) and a low of -4.2% (2009–10). The PEFO projected a return to surplus of 0.1% in 2015–16.

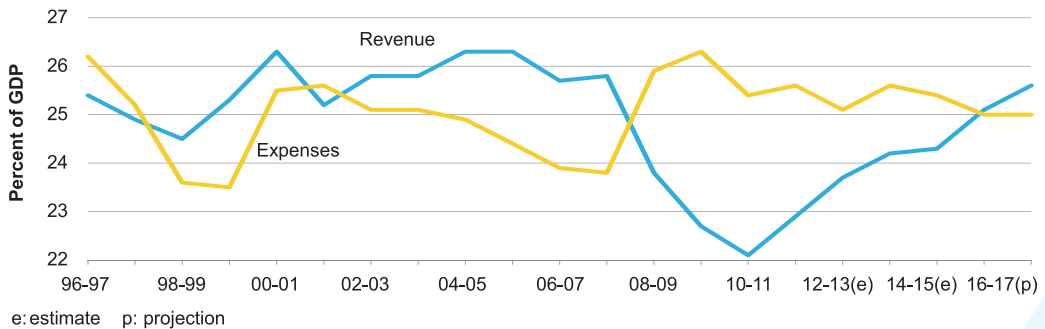
To determine whether Australia's fiscal balance presents a concern, it is useful to compare it with other countries. The International Monetary Fund (IMF) publishes data on various countries' structural budget balances, which adjust budget balances for temporary or one-off factors beyond the economic cycle. As illustrated in the structural budget balances chart, although Australia's fiscal balance fell to a low in the context of the GFC, its structural budget balance is reasonable compared to other advanced economies.

Net debt



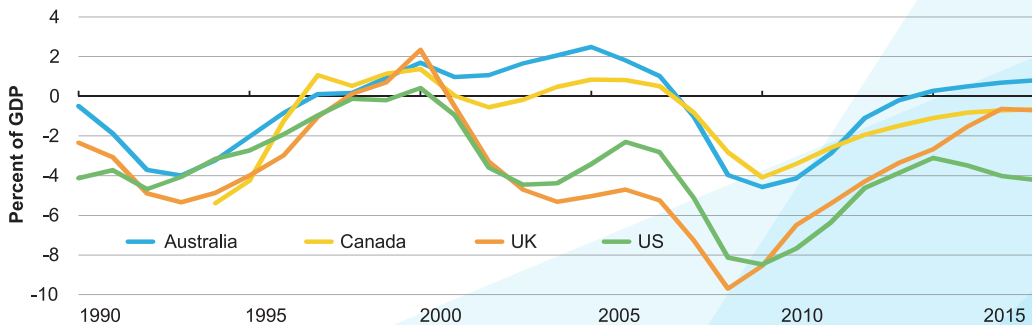
Source: International Monetary Fund, World Economic Outlook Database, April 2013.

Australian Government revenue and expenses



Sources: Australian Government, Budget strategy and outlook: budget paper no 1: 2013–14, p. 10-10 and Secretary to the Treasury and Secretary of the Department of Finance and Deregulation, Pre-election Economic and Fiscal Outlook 2013, p. 23.

Structural budget balances



Source: International Monetary Fund, World Economic Outlook Database, April 2013.

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Australia's changing population

Joanne Simon-Davies, Statistics and Mapping

KEY ISSUE

The Australian population reached 22,906,400 in December 2012, an increase of 394,200 (or 1.8%) on the previous year. Net overseas migration now plays a larger role than natural increase in population growth in Australia. Western Australia saw the biggest increase in population at a state and territory level in the year to December 2012.

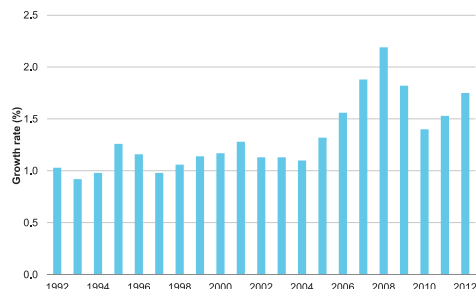
Australia's population

Growth in Australia's population is made up of two components:

- natural increase – births minus deaths and
- net overseas migration (NOM) – the net gain or loss of population through immigration to Australia and emigration from Australia. This can include both permanent and long-term (staying 12 months or more within a 16-month period) arrivals and departures.

The relative contribution of these two components has changed. For example, in 2002 natural increase represented 51% of Australia's population growth and NOM 49%. By 2012, natural increase represented only 40% of Australia's population growth with NOM at 60%. Interestingly, the increase in NOM in recent years has not been caused by an increase in permanent settlers. Rather, it has been driven by people staying in Australia on long-term temporary visas, such as overseas students and temporary skilled migrants. NOM peaked in 2008 at 315,687 people, but by 2010 it had declined to 172,038 people. By 2012, NOM had again risen to 235,914 people. The Department of Immigration and Citizenship projects further increases in NOM over the foreseeable future, largely resulting from growth within temporary programs.

Annual population growth rate: Australia, 1992 to 2012



Components of population change in the states and territories

At the state and territory level, population growth has three components – natural increase, NOM and net interstate migration (NIM).

Net interstate migration is defined by the Australian Bureau of Statistics (ABS) as the difference between the number of persons who have changed their place of usual residence by moving into a given state or territory and the number who have changed their place of usual residence by moving out of that state or territory during a specified time period. This difference can be either positive or negative.

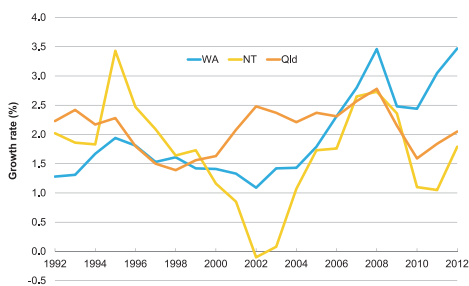
All states and territories experienced positive growth in the year to December 2012, with Western Australia (WA) recording the biggest growth (3.5%) and Tasmania the lowest growth (0.1%). According to the ABS, the make-up of that growth varied between states and territories:

For the year ended 31 December 2012, natural increase was the major component of population change in the Northern Territory and the Australian Capital Territory. Net overseas migration was the major component of population change in New South Wales, Victoria, Queensland, South Australia and Western Australia. A net

interstate migration loss was the highest contributor to population change in Tasmania. Net interstate migration losses were also recorded in New South Wales, South Australia and the Northern Territory.

WA is growing faster than any other state or territory. Between 1992 and 2004, there was steady annual growth of around 1.5%. Between 2004 and 2008, the rate of growth increased from 1.5% to 3.5% due to increased mining activity. However, during the Global Financial Crisis (GFC), the annual population growth slowed to 2.4% in 2010 and then increased to 3.5% in 2012 (see graph). Interestingly, the Northern Territory (with a much smaller population) has shown a similar pattern to WA in recent years, although the growth has been much more substantial, rising from a negative position (-0.1%) in 2002 to 2.7% in 2008. However, during the GFC more than half the growth gained was then lost, falling to 1.1% in 2011. From 1998 to 2002, Queensland had the highest average annual growth rate of all states and territories. This was most likely due to an increase in mining activity.

Annual population growth rate: Western Australia, Northern Territory and Queensland, 1992 to 2012



Interstate migration

People move from one location to another for various reasons, such as employment, retirement, family or study. In 2012, a total of 327,523 people moved from one state or territory to another. This was a decrease of 3.9% from the number who moved in the previous year. In the year ending December 2012, WA, Queensland, Victoria and the Australian Capital Territory all gained from NIM whilst all other states and territories experienced losses.

Over the decade to December 2012, Queensland was the only state to consistently record an annual NIM gain. However, the size of that gain has slowed from 37,437 people in 2002 to only 11,354 people in 2012. This contrasts with New South Wales and South Australia which have had no gains in NIM in the past ten years.

Net internal migration by state and territory, 2002, 2006 and 2012

	2002	2006	2012
NSW	-31,074	-26,105	-17,761
Vic	1,144	-1,012	1,733
Qld	37,437	25,959	11,354
SA	-1,228	-2,734	-3,345
WA	-3,403	4,528	10,417
Tas	-22	-680	-2,650
NT	-2,440	-428	-1,677
ACT	-378	493	1,929

The future

Australia's population can be expected to continue to grow and there is no doubt that migration will play a significant role in that growth. As a consequence of this, population growth will remain a challenge for policy makers at all levels of government, particularly in relation to housing, transport, service delivery, infrastructure and environmental sustainability.

Note: ABS information in this article and statistical information in the charts and the table is from the ABS publication, Australian Demographic Statistics, Dec 2012, cat no. 3101.0.

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Some economic effects of inequality

Dr Anne Holmes, Economics

KEY ISSUE

There are a number of reasons why inequality may harm a country's economic performance. At a microeconomic level, inequality increases ill health and health spending and reduces the educational performance of the poor. These two factors lead to a reduction in the productive potential of the work force. At a macroeconomic level, inequality can be a brake on growth and can lead to instability.

Defining inequality

Economic inequality means unequal access to wealth and income. This brief mostly deals with income. In most developed countries, market income is mainly from wages and salaries, but also from returns on capital such as shares and rents. People's market income is then reduced by taxation and/or increased by government transfers such as pensions and child payments.

Inequality is usually discussed in terms of equivalised household income, which takes account of how many people the income has to support, and (often) whether the household pays rent. Inequality in a society is usually measured as the ratio of high incomes to low; for example, the ratio of the top 20% of equivalised household incomes to the bottom 20%.

It is important to distinguish between inequality and wealth and poverty. A rich country can be relatively unequal, and a poor country can be relatively equal.

Many effects of poverty are well known. For example, children of poor families do not perform as well at school as those of affluent families. Poor people have worse health than rich people.

These are results – or at least correlates – of poverty, and they have been documented in most societies. The relationships are usually fairly easy to demonstrate by correlating two variables; for example, by linking family income of a large number of subjects and the test scores or health status of those subjects.

It is less easy to demonstrate a causal relationship between inequality of itself and other social outcomes, principally because inequality is not a characteristic of an individual. Also, the causal mechanisms may be less obvious.

Is there an economic issue?

Two pressing economic issues today are the need to lift productivity and the need to promote growth while avoiding financial instability of the kind that culminated in the global financial crisis. It is possible that inequality reduces labour productivity. It is also possible that it is a brake on growth and can lead to economic instability.

Health

If people are not healthy they will not work to their full productive capacity.

Ascertaining whether inequality is a direct cause of ill health (as opposed to merely being correlated with it) is difficult. On balance, the research seems to indicate that inequality causes poor health. One possible mechanism for this is through increases in stress, which is a known risk factor for many diseases. Specifically, World Health Organization research shows that in Europe more unequal countries have poorer mental health outcomes.

More simply, in most rich countries there are diminishing marginal returns to an individual's expenditure on health, so a transfer of funds from treating the rich to treating the poor would both reduce inequality and improve the total health of the population.

Education

If children are less successful at school, they are less likely to become highly skilled workers. Their productive capacity, and therefore the productive capacity of the economy, is diminished. OECD research concludes that policies to improve high school and tertiary education completion rates also improve gross domestic product per capita.

Inequality reduces performance because of its segregating effects. There is a good deal of evidence that children's school success depends at least partly on the interests and aspirations of their peers. The influence of peers is greater than any school effects, including teacher quality. If schools are segregated, children from socioeconomically disadvantaged households will mix with other disadvantaged children, and thus with children who do not perform well at school. Segregation is more likely in an unequal society. The negative effects of poor children associating with less gifted children are greater than any positive effects of affluent children associating with more gifted children. So inequality may cause a net reduction in educational attainment.

Unlike in health, a simple transfer of resources to poor schools may not be very effective in reducing inequality. The research cited above suggests that unequal outcomes will persist to some extent as long as there is residential segregation or parental choice of schools.

Economic growth

In his book *Inequality and Instability*, James K Galbraith concludes:

... more egalitarian societies tend to have lower steady-state unemployment. They also tend to have higher rates of technical progress and productivity growth.

A more equal wage distribution encourages specialisation in higher value-adding industries, while low wage, low value-adding industries cannot compete.

Meanwhile, work by International Monetary Fund economists shows that 'longer growth spells are robustly associated with more equality in the income distribution'.

Thus inequality may have a generally slowing effect on economic growth.

Economic stability

A number of economists have argued that inequality leads to economic instability. One mechanism by which this happens is that the rich consume a smaller proportion of their income than the poor. They save money which people on lower incomes would spend. This leads to a reduction in aggregate demand, which in turn leads to unemployment. In response, governments take measures to stimulate demand, such as lowering interest rates. This feeds into asset bubbles – for example, unsustainably high housing prices.

Meanwhile, as inequality grows, individuals facing low or declining relative incomes may maintain their consumption through borrowing (financed by the savings of the rich). A very small rise in unemployment or interest rates can lead to defaults on mortgages or consumer loans and can have catastrophic results.

There is some level of consensus that inequality in advanced countries helped cause the global financial crisis.

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Commonwealth expenditure: legality and scrutiny

Daniel Weight, Economics

KEY ISSUE

The next Parliament will have to grapple with a changing legal landscape surrounding Commonwealth expenditure. Recent High Court decisions have seemingly narrowed the areas in which the Commonwealth may expend monies, and a substantial rewrite of the Commonwealth's financial framework in the last days of the 43rd Parliament has left extensive unfinished work for the 44th. These events may result in questions about the Parliament's capacity to scrutinise the Executive, and debates about the role of the Commonwealth and the states in Australia's federal system.



Commonwealth expenditure

The Commonwealth is budgeted to spend almost \$400 billion in 2013–14. Much of this expenditure is readily identified as programs and activities that are associated directly with the Commonwealth, such as funding for defence or Medicare.

The Commonwealth also has other significant expenditures each year which are less readily identified, such as grants to the states for education and healthcare, or payments to local governments for road upgrades. In 2013–14, grants to the states and local governments will amount to over \$95 billion. Through the ability to attach conditions to grants, the Commonwealth has increasingly been able to

gain greater influence in certain areas of policy that are heavily reliant upon funding.

While the annual Appropriation Bills that authorise the various areas of Commonwealth expenditure are subject to parliamentary debate, there is little scrutiny of many areas of expenditure.

Sources of uncertainty

In its 2012 decision *Williams v Commonwealth* (the School Chaplains Case), the High Court had to consider the limits of the Commonwealth's power to spend money.

Ron Williams, a Toowoomba father of six, objected to the Commonwealth's funding of school chaplains in his local state school. He challenged the school chaplains program in the High Court on the grounds that section 116 of the Constitution, which prohibits religious tests for Commonwealth office holders, meant that the Commonwealth's scheme was unconstitutional. That argument failed; but Williams's other argument — that the Commonwealth did not have the power to spend money on matters outside its constitutionally prescribed responsibilities, like school chaplains and potentially numerous other things — was accepted.

A result of this case, and the earlier 2009 *Pape v Commissioner of Taxation* (Tax Bonus Case), was that the Commonwealth no longer had the power to fund all the things that it had previously funded without a clear legislative underpinning to support the programs, which was based on a clear head of power in the Constitution. Areas of doubtful expenditure included the money that the Commonwealth currently provides directly to local governments, funding for roads and transport, assistance to industry and numerous other discretionary payments.

Legislation is still unsettled

The first response by the Commonwealth to the Williams decision was to make amendments to the existing Financial Management and Accountability Act 1997, aimed at ensuring the validity of numerous Commonwealth

expenditure programs. Those amendments sought to revive the school chaplains program, and legally validate over 400 other Commonwealth programs set out in the regulations.

However, that legislation will be replaced by the Public Governance, Performance and Accountability Act 2013 (PGPA Act), which is to commence by 1 July 2014. This major rewrite of the entire financial framework of the Commonwealth was enacted in the last sitting week of the 43rd Parliament after a truncated parliamentary debate. Much work still needs to be done by 1 July 2014 to 'bed down' the new framework – including clarifying how the Parliament will scrutinise the Executive's use of monies and other resources.

In particular, extensive legislative 'Rules' will need to be developed covering most aspects of the expenditure of, and accounting for, Commonwealth monies. The Rules will be disallowable legislative instruments. Numerous other pieces of legislation will also need to be repealed or amended in order to make the new Act work, which will require at least one more Bill.

In the interim, the continuing uncertainty surrounding aspects of Commonwealth funding potentially exposes many individual programs to ongoing legal challenges. Ron Williams has indicated that he will return to the High Court at a later date to challenge the resurrected school chaplains program, for example.

What's next?

Uncertainty continues to surround many areas of Commonwealth expenditure, and even with new legislation in place, more constitutional challenges are likely.

There remains, however, an alternative mechanism for the Commonwealth to achieve many of the outcomes it wishes. By making grants to state governments – which are explicitly allowed under section 96 of the Constitution – the Commonwealth could continue to fund many existing programs and activities. Aside from whether this would be an efficient arrangement (there may be

extensive duplication of effort between the Commonwealth and the states), it may give state governments more influence in areas of policy that the Commonwealth has increasingly dominated since federation, such as health, education and infrastructure.

Alternatively, some may argue that the realisation that the Commonwealth enjoys a more limited power to hand out money in support or furtherance of things that it considers desirable – and that it must now work more closely with the states – is not a problem. The Coalition has intimated that, in government, it would seek to devolve many functions back to the states anyway. The High Court might have, indirectly, highlighted those areas of governmental activity that would no longer be directly undertaken at the Commonwealth level. Whether the Commonwealth would be willing, however, to continue to fund significant areas of service delivery through grants to the states, albeit with much less capacity to influence the policy design or outcomes, is uncertain.

Aside from the constitutional issues around Commonwealth spending, there will be significant work for the 44th Parliament to do before 1 July 2014 in developing and scrutinising the proposed Rules and other requirements that are required to be implemented under the PGPA Act. And without effective Rules under the PGPA Act, the Parliament may find it difficult to scrutinise the Executive's spending commitments.

Further reading

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THE NATIONAL ECONOMY

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The tools of macroeconomic policy—a short primer

Robert Dolamore, Economics

KEY ISSUE

Macroeconomic policy aims to provide a stable economic environment that is conducive to fostering strong and sustainable economic growth. The key pillars of macroeconomic policy are fiscal policy, monetary policy and exchange rate policy.

Macroeconomic policy is concerned with the operation of the economy as a whole. In broad terms, the goal of macroeconomic policy is to provide a stable economic environment that is conducive to fostering strong and sustainable economic growth, on which the creation of jobs, wealth and improved living standards depend. The key pillars of macroeconomic policy are: fiscal policy, monetary policy and exchange rate policy. This brief outlines the nature of each of these policy instruments and the different ways they can help promote stable and sustainable growth.

Fiscal policy

Fiscal policy operates through changes in the level and composition of government spending, the level and types of taxes levied and the level and form of government borrowing. Governments can directly influence economic activity through recurrent and capital expenditure, and indirectly, through the effects of spending, taxes and transfers on private consumption, investment and net exports.

Under current institutional arrangements, fiscal policy is the only arm of macroeconomic policy directly controlled by government.

As an instrument for stabilising fluctuations in economic activity, fiscal policy can reflect discretionary actions by government or the influence of the ‘automatic stabilisers’. A fiscal stimulus package is an example of discretionary action by government intended to support aggregate demand by increasing public spending and/or cutting taxes.

The ‘automatic stabilisers’ refer to certain types of government spending and revenue that are sensitive to changes in economic activity, and to the size and inertia of government more generally. They have a stabilising effect on fluctuations in aggregate demand and operate without requiring any specific actions by government. For example, if the economy slows, on the revenue side of the budget the amount of tax collected declines because corporate profits and taxpayers’ incomes fall; on the expenditure side, unemployment benefits and other social spending increases. The effects of these changes tend to offset part of the decline in aggregate demand that would otherwise occur. This cyclical sensitivity makes fiscal policy automatically expansionary during downturns and contractionary during upturns in economic activity.

At least conceptually, the operation of the automatic stabilisers over the economic cycle should have no effect on the underlying structural position of the budget. A short-term cyclical deterioration in the budget bottom line should be reversed as economic conditions improve.

As well as having a short-term stabilisation role, fiscal policy can also be framed against longer-term objectives. This can include ensuring the long-term sustainability of the budget and its capacity to meet future challenges, such as population ageing, and seeking to increase the long-term growth potential of the economy, through investments in areas such as infrastructure and education.

In Australia the conduct of fiscal policy is subject to the Charter of Budget Honesty Act 1998 which imposes a formal requirement on the Australian Government to set out and report against a medium-term fiscal strategy. This framework is required to be based on ‘principles of sound fiscal management’ including: having regard for government debt and the management of fiscal risks, the state of the economic cycle, the adequacy of national saving, the stability and integrity of the tax base and equity between generations. The

medium term focus of the Charter does not preclude a role for either discretionary action by government intended to stabilise fluctuations in economic activity, or the automatic stabilisers.

Monetary policy

In Australia, the Reserve Bank of Australia (RBA) Board is responsible for setting monetary policy. Monetary policy decisions are implemented by changing the cash rate (the interest rate on overnight loans in the money market). The cash rate is determined in the money market by the forces of supply and demand for overnight funds. Through open market operations the RBA can target the cash rate by increasing or decreasing the supply of funds that banks use to settle transactions among themselves. For example, if the RBA wants to lower the cash rate it can supply more exchange settlement funds than the commercial banks want to hold. In this case, banks will respond by offloading funds, which pushes the cash rate lower.

By changing the cash rate the RBA is able to influence interest rates across the financial system. Changes in interest rates in turn can influence economic activity by affecting savings and investment behaviour, household expenditure, the supply of credit, asset prices and the exchange rate.

If demand pressures are building up in the economy, reflected in rising prices, the RBA can tighten monetary policy, thereby dampening demand. Conversely, in the face of weak demand, reflected in deflationary pressures, the RBA can loosen monetary policy to support economic activity.

However, it is important to remember that monetary policy can exert an influence on the macro-economy even when interest rates are left unchanged. What matters is the level of interest rates. It is possible the cash rate may not have changed for some time but the level of interest rates is nonetheless exerting a strong expansionary or contractionary effect on the economy.

The RBA Board sets the cash rate with a view to achieving the objectives set out in the Reserve Bank Act 1959, namely: the stability of the currency of Australia, the maintenance of full

employment and the economic prosperity and welfare of the Australian community. In pursuit of these objectives, the RBA aims to maintain inflation between 2% and 3%, on average, over the economic cycle, thereby anchoring inflationary expectations. By targeting low and stable inflation the RBA seeks to encourage strong and stable economic growth.

Exchange rate policy

Exchange rate policy is concerned with how the value of the domestic currency, relative to other currencies, is determined. Australia has had a floating exchange rate since December 1983. The value of the Australian dollar is determined by market forces.

In response to the mining boom, the Australian dollar appreciated, which helped moderate inflationary pressures and ensure the economy received the price signals needed to facilitate the flow of resources to the mining sector. The appreciation of the dollar also helped spread the benefits of the mining boom by increasing the purchasing power of Australian households. However, the high exchange rate had a contractionary effect on a number of sectors of the economy (such as manufacturing).

The Australian dollar has recently depreciated. This should improve the international competitiveness of Australia's export and import-competing industries.

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Fiscal and monetary policy – renewed international debate

Robert Dolamore, Economics

KEY ISSUE

The global financial crisis has sparked renewed international debate about the roles and conduct of fiscal and monetary policy. While the strength of Australia's macroeconomic framework is generally acknowledged, this debate may nonetheless provide important insights.

The global financial crisis (GFC) has prompted renewed international debate about the roles and conduct of fiscal and monetary policy. The International Monetary Fund (IMF) has been at the forefront of this debate as economists try to identify the lessons from the GFC for macroeconomic policy. This note briefly sketches some of the key ideas from this debate.

This note is intended to be read in conjunction with the brief *The Tools of Macroeconomic Policy – a Short Primer*, which explains many of the economic terms used here.

The pre-GFC consensus

In the years prior to the GFC a consensus developed about the roles fiscal and monetary policy should play in economic management. Monetary policy was seen as the appropriate policy instrument to stabilise short-run fluctuations in aggregate demand. Monetary policy can be adjusted relatively quickly and if delegated to an independent central bank is less susceptible to the influence of political considerations.

In contrast, discretionary fiscal policy was seen as having less of a role in short-run demand management. Among other things, discretionary actions are less nimble than monetary policy and therefore less suited to managing 'normal' fluctuations in activity. The effectiveness of discretionary actions tends to be blunted because their formulation and implementation can lag economic developments and are susceptible to political

influence. There were also concerns that such measures are not easily reversed when they are no longer justified by economic conditions.

Generally, fiscal policy was seen as more appropriately focused on the medium to longer term. For example, fiscal policy can help address medium term structural issues and ensure the long term sustainability of public finances.

However, this was not seen as precluding a role for the automatic stabilisers. The automatic stabilisers can cushion short run fluctuations with practically no information and implementation lags, and relatively short impact lags. Importantly, if the automatic stabilisers are left to operate symmetrically over the economic cycle, they should not contribute to any structural deterioration in the budgetary position.

A post GFC re-think

The use of fiscal stimulus measures in response to the GFC has given greater prominence to discretionary fiscal policy as a countercyclical tool. It has been suggested that during the crisis fiscal policy had a 'sleeping beauty' moment – with conventional monetary policy rapidly reaching its limits and with the financial system experiencing acute problems, the 'forgotten' tool of discretionary fiscal policy was 'rediscovered' as a way of supporting aggregate demand.

However, much depends on whether there is sufficient fiscal space to enable governments to run larger budget deficits. The GFC has clearly shown that the scope to use fiscal policy as a countercyclical tool, even if this involves no more than allowing the automatic stabilisers to work, may be significantly curtailed by weak public finances. For example, if a government is running large structural deficits and the level of public debt is already high, a large budget deficit makes it vulnerable to changing market sentiment. This underscores the importance of budget discipline even in the good times.

There is also likely to be pressure for a stronger focus on, and transparency about, the

underlying structural position of government budgets. There is a risk that even favourable cyclical or one off factors can create problems by masking a deteriorating structural budgetary position that ultimately has to be addressed when the 'good times' end.

Among other things, the IMF has floated the idea of designing better automatic stabilisers with a view to strengthening fiscal policy as a countercyclical tool. This might include developing rules that allow some types of government transfers or taxes to vary based on pre-specified triggers tied to the state of the economic cycle.

Internationally, the debate about monetary policy has focused on what it should target and the instruments that should be used. Some argue the GFC has shown monetary policy should target more than low and stable inflation, and officials need to utilise a broader array of instruments than just official interest rates. In relation to the former the concern is that of itself low-inflation is not sufficient either to ensure financial stability or maintain a low output gap and robust growth. Options in this space include requiring central banks to more explicitly target financial stability (with possible proxies for financial stability including measures of leverage, credit aggregates and asset prices) and economic activity.

The GFC has also sparked a re-think about the limits of conducting monetary policy primarily through changes to official interest rates. A concern here is that official interest rates are too broad an instrument to deal with the situation where an asset price bubble is developing in one part of the economy but inflationary pressures in the rest of the economy are relatively subdued. In this scenario raising interest rates may successfully dampen the bubble but risks constraining economic activity more generally.

Reflecting this concern, some argue policymakers should use 'macroprudential' instruments to help contain imbalances. These are tools (such as capital adequacy requirements, loan to valuation ratios and capital controls) that are more typically thought of as being part of the tool kit of financial market regulators. However, as

macroprudential instruments influence aggregate demand through the availability of credit in the economy, there may be potential to actively use them to stabilise fluctuations in economic activity.

As an analogy for the need for more fiscal space, it has been suggested there is a need for more nominal interest rate room. Controversially, the IMF has floated the idea of setting higher inflation targets (perhaps around 4%) with a view to giving central banks more scope to cut interest rates to support aggregate demand in the face of a severe economic shock and lessen the risk of hitting the zero interest rate bound.

It remains to be seen if any of the ideas that have been floated about macroeconomic management following the GFC ultimately stick. Australia came through the GFC better than most countries and the strength of our macroeconomic framework is generally acknowledged. Nevertheless, the current international debate may still provide opportunities to learn from the experience of others, even if this reflection simply reaffirms the importance of those aspects of macroeconomic policy that served Australia well going into the GFC. This seems all the more important given it is unlikely the next economic crisis will coincide with a once in a lifetime terms of trade boom.

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Intergenerational reports – key influences on policy?

Kai Swoboda, Economics

KEY ISSUE

It is likely that the 4th intergenerational report (IGR)—a modelling analysis that examines the fiscal impact on the Australian Government Budget position over the next 40 years assuming no policy change—will be conducted during the 44th Parliament. This brief discusses the lessons from the three previous IGRs (2002, 2007 and 2010).

Under the Charter of Budget Honesty Act 1998, the Treasurer is required to publish an ‘intergenerational report’ (IGR) every five years that assesses the long term sustainability of current Government policies over the next 40 years, taking account of the financial implications of demographic change.

The basis for conducting such an analysis is the principle of intergenerational equity—that actions benefiting current generations should not compromise future generations.

To date, three such IGRs have been published (May 2002, April 2007 and January 2010). The next such report is required to be published by January 2015, which is likely to fall within the term of the 44th Parliament.

Outcomes of previous IGRs

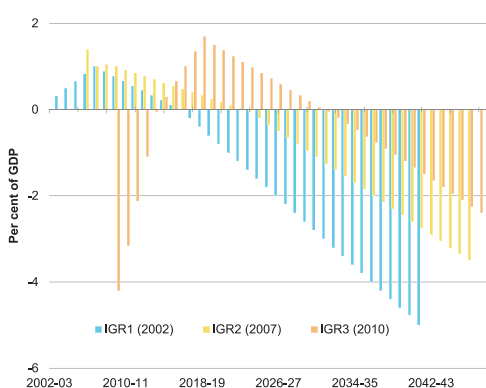
Each IGR requires assumptions to be made for a range of key demographic and economic indicators. These are then used to determine the impact on the revenues and expenditures of the Australian Government budget under the assumption that current policies remain unchanged over the relevant 40-year forward period.

The outcomes of each IGR have generally been similar, with each projecting increasing expenditure as a share of GDP in certain areas, resulting in a significant negative budget position (‘fiscal gap’) at the end of the period covered (Figure 1).

Following the delivery of each IGR, successive governments have implemented policies that have been explicitly linked to the relevant IGR. For example:

- The 2002–03 Budget included measures such as a rise in co-payments for medicines supplied under the Pharmaceutical Benefits Scheme (PBS) and the introduction of the superannuation co-contribution.
- The 2007–08 Budget emphasised measures aimed at enhancing productivity and participation.
- The 2010–11 Budget referred to the IGR as a basis for superannuation changes such as the phased increase in the superannuation guarantee from 9% to 12%.

Figure 1: Projected fiscal gap for each IGR



Source: IGR (2002, 2007, 2010).

The difference between the outcomes of each IGR partly reflects these and other policy changes. The results of each exercise are nevertheless subject to a range of economic and demographic assumptions.

Some of these assumptions are able to be directly influenced by government, such as migration levels. Others, however, such as fertility and productivity growth, can only be influenced indirectly.

Any analysis of the outcomes of such modelling therefore needs to be mindful of the extent that the values assumed for key inputs to the modelling can be achieved. Important too in assessing different policy responses to the 4th

IGR will be views about the role of government, priorities for government expenditure and the extent and mix of taxation.

Key assumptions of previous IGRs

In general, each IGR has assumed higher life expectancies, net migration and labour participation; but key economic assumptions have remained largely unchanged.

Also important in the outcomes of each IGR are assumptions and models used for the key drivers of certain government expenditures that are not directly related to ageing, such as technology change and behavioural changes. The models also incorporate the impact of policy changes, such as the moderating effect on expenditure by raising the age to access the age pension.

Importantly, the 2nd and 3rd IGRs included an analysis of how selected economic indicators are affected by changes to key assumptions. However such a sensitivity analysis did not include the impact of different scenarios on the fiscal balance and was not the subject of much discussion within each IGR.

Criticisms of the IGR exercise and outcomes

Various criticisms of previous IGRs have been made. At a high level, one criticism is that such an exercise is merely an exercise in scaremongering, scape-goating older people for the rising costs of government. Another is that the IGR, by focussing on the impact on the Australian government budget, does not consider the impact of cost shifting or pressures facing state and territory governments.

More fundamentally, the value of such a long-term modelling exercise is questionable, given the negative fiscal outcomes following the 2008 global financial crisis. Significant differences in assumptions across IGRs that should improve IGR outcomes, such as the doubling of annual net migration and a sharp increase in fertility from the 1st IGR to the 3rd IGR, can also lead to the perception that the outcomes can be distorted.

Critics also claim that some assumptions about future terms of trade and productivity have been optimistic and that some assumptions on

the expenditure side (particularly health) do not adequately take into account rising incomes.

The response to each IGR has arguably been piecemeal and ad hoc. While the Government in the 2010 IGR noted the broad range of policies it was undertaking to respond to long-term challenges, there has been no framework to assess the impact of individual policy changes or provide a basis for assessing progress in achieving assumed future levels of economic performance.

Key inputs into the 4th IGR

The 4th IGR will be required to incorporate a range of significant policy changes since the last report in 2010. These include the establishment of a paid parental leave scheme in 2011, the early stages of the phased implementation of a national disability insurance scheme and recent changes to superannuation tax concessions.

Important also in determining the outcomes of the 4th IGR will also be assumptions made on the key variables such as migration, life expectancy, fertility, labour force participation and productivity. While more recent evidence suggests that assumptions about life expectancy will be higher again, the choice for other assumptions is less clear.

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The Australian economy – supporting the transition

Robert Dolamore, Economics

KEY ISSUE

With resources sector investment probably having peaked, other sources of demand will need to strengthen if the economy is going to grow at a rate consistent with full employment. How smoothly this transition unfolds will have important implications for Australian living standards. Economic policy can play an important role in supporting this transition.

As the Australian economy moves into the production phase of the mining boom a significant transition is underway. With resources sector investment probably having peaked, other sources of demand will need to strengthen if the economy is to grow at a rate consistent with full employment. A smooth transition from one set of growth drivers to another is not guaranteed, subject as it is to the influence of changes in global economic conditions and consumer and business confidence. Economic policy can play an important role in supporting this transition in the near future and in facilitating strong and sustainable economic growth in the medium to longer term.

This brief is intended to be read in conjunction with *The Tools of Macroeconomic Policy – a Short Primer*, which explains many of the economic terms used here.

Macroeconomic policy

The macroeconomic environment exerts a strong influence on the economic decisions of households and businesses, and hence, on the level of economic activity. For example, such decisions are influenced by how fast prices are rising, labour market conditions and the availability and cost of credit. Reflecting this, maintaining appropriate macroeconomic policy settings is essential if households and businesses are going to respond positively to changes taking place in the economy.

Monetary policy is playing a key role in supporting economic activity, with interest rates at their lowest level in 50 years. While the economy appears to have taken longer to respond to the current round of monetary policy easing than in the past, demand should nonetheless strengthen in interest rate sensitive parts of the economy, including dwelling investment and non-mining business investment.

The exchange rate, which surprised many commentators by remaining at historically high levels even after Australia's terms of trade peaked in late 2011, has subsequently depreciated. This should provide an important adjustment mechanism for the economy by boosting the international competitiveness of Australia's export and import-competing industries. Key issues in this regard include: how far the Australian dollar needs to fall to be consistent with full employment, how orderly this adjustment is and how long it may take relative to the effects of the decline in resources sector investment being felt.

Fiscal policy is currently on a consolidation path with a view to returning the budget to surplus. This is consistent with seeking to ensure the medium to longer term sustainability of Australia's public finances. One challenge is to ensure that any reprioritisation of expenditure is as 'pro-growth' as possible. Some areas of public expenditure, such as education and infrastructure, are likely to have a greater effect on Australia's long-term growth prospects than others. If the rebalancing of Australia's growth does not go smoothly, so that the level of economic activity significantly falls short of what is required for full employment, then fiscal policy may need to be more supportive of aggregate demand in the short-term.

Microeconomic reform

While supportive macroeconomic policies are important, they will not be sufficient to ensure Australia makes a smooth transition. There is a need for complementary microeconomic reforms that seek to increase the productivity of

Australian businesses, lower their cost structure and encourage innovation. This is fundamental to improving the international competitiveness of Australian firms and securing higher future living standards.

The Productivity Commission has identified three main channels through which government can influence the productivity of business:

- incentives – the external pressures and disciplines on them to perform well
- capabilities – the human resources and knowledge systems, the institutions and infrastructure, needed to devise productivity-enhancing changes and support them effectively and
- flexibility – the scope to make the necessary changes.

The Productivity Commission emphasises the need for a reform agenda that proceeds on all three fronts and for policy consistency to avoid sending mixed signals.

Distributional policies

Structural adjustment in the economy inevitably focuses attention on the distribution of costs and benefits across the community.

During the upswing in resources sector investment, the high Australian dollar increased the purchasing power of Australian households, but also put considerable pressure on trade exposed industries. As the surge in resources sector investment winds down, there will likely be discussion of how the distributional effects of this are playing out.

In thinking about this it can be useful to distinguish between adjustment costs that are borne widely across the community and those that fall disproportionately on particular groups.

For example, the depreciation of the Australian dollar imposes a cost on Australian households by reducing their purchasing power. How far the dollar depreciates will determine how large this cost is and its impact on living standards. It will be important that this cost is absorbed without compensating households through higher wages, while recognising this may be painful in the short-term. Otherwise, the

positive effects of the depreciation in terms of boosting the international competitiveness of Australian businesses will be offset by cost increases.

However, lifting Australia's productivity performance provides a way of moderating the cost of this adjustment. This is because higher productivity would further enhance the international competitiveness of Australian firms and provide some scope for paying higher wages.

Job losses in certain industries may be concentrated in particular geographic locations. When this occurs, there is a case for seeking to reduce some of the costs of adjustment for those individuals adversely affected by structural change. As well as more equitably sharing the costs of adjustment across the community, providing assistance may also improve community acceptance of difficult changes.

Policy action across a broad front

All of the policy areas discussed above have their limits in terms of what they can do to support Australia's transition to a different set of growth drivers. This suggests the need for policy action across a broad front and consistently focused on improving the growth prospects of the Australian economy.

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Industry policy in an open economy

Eugenia Karanikolas, Economics

KEY ISSUE

Australia is one of the world's most open economies. Like other advanced economies, Australia has been moving away from lower skilled and highly labour-intensive industries towards more knowledge-intensive and internationally-focused industries, especially in services and advanced manufacturing. As a result, Australia's industry policy has been gradually shifting its attention towards supporting businesses to become internationally competitive by adopting new technologies and undertaking more knowledge intensive activities.

Background

The structure of the Australian economy has changed significantly in the last 35 years. A strong supporter of the multilateral trade system, Australia has been reducing its trade barriers in goods, services and investment. Economic integration, the widespread adoption of new communication technologies and the rise of cheap labour-intensive manufacturing elsewhere mean that some industries that used to focus predominantly on the domestic market can no longer compete.

On the other side of the equation, industries that have taken advantage of Australia's strengths, such as its educated workforce, competitive environment and sound physical and communications infrastructure, have shifted focus to compete successfully in international markets. This is not only true for two of Australia's largest export industries, mining and education, but also for high value-added industries like wine and manufacturing of medical equipment.

In addition, new types of industries have recently developed that focus increasingly on the online market for consumer, property and business services. These industries

now account for a third of the top 50 growth industries identified by IBIS, the industry research group. For instance, IBIS predicts that revenue in the smartphone app development sector will increase by 37.0% to almost \$300 million in 2013—2014. In addition, industry revenue from online shopping will increase by 11.3% to \$12.3 billion, whilst revenue in the online education sector will increase by 9.6% to around \$5.3 billion.

The service sector now accounts for 80.0% of the economy and 17.0% of exports. Niche exports, including legal, media and business advisory services, are on the rise and are now worth around \$8 billion a year. Growth in exports of sophisticated manufacturing products is also strong, especially exports of mining technology and equipment which are currently worth around \$27 billion a year. Other high-value added exports are also increasing their share of Australia's total exports: the pharmaceuticals and medical technology sector now comprises the largest share of manufacturing exports to China, Australia's largest trading partner.

Consistent with this performance, Australia's trade and industry policy has increasingly been formulated to build on those strengths. Specifically, Australia's efforts are currently concentrated on advancing multilateral and bilateral agreements that facilitate trade in services, including financial, legal and transport services. On the domestic front, current efforts are concentrated on improving business competitiveness in services by investing in the country's communications infrastructure. Efforts are also being made to encourage a stronger culture of innovation and entrepreneurship.

Current industry programs

Many of Australia's industry programs focus on improving the competitiveness of small businesses, providing the incentive for business to invest in innovation and commercialisation of new products and providing export support. Some of the main programs are:

- The R&D tax offset: this is by far the largest program. It provided \$800 million in tax concessions to business in 2012–13.
- Enterprise Connect: this program specifically targets small and medium enterprises (SMEs) and receives funding of approximately \$24 million a year. The program is designed to bridge the information gap faced by SMEs in accessing reliable information and support them to improve their competitiveness. For instance, SMEs receive help to identify opportunities in major projects that may exist in Australia and overseas and receive advice on how to best position their business to take advantage of them. SMEs can also get advice on new technologies and how to go about adopting them in their business.
- Cooperative Research Centres (CRC): this long-standing program aims to establish links between universities and industries. CRCs respond to well-defined challenges faced by industries which have a wider economic, social and environmental impact. The Cochlear hearing implant, one of the great successes of recent years, was produced as part of a CRC. In terms of the funding it receives, this program is one of the largest, with a current budget of around \$145 million.
- Commercialisation Australia: this program focuses on supporting businesses to commercialise their product, process or service by providing funding of up to \$2 million for each participant to help to cover costs. In 2013–2014, this program's budgetary funding amounted to \$75 million.
- Industry Innovation Precincts and Industry Innovation Network: these are new programs which in essence aim to encourage collaboration between businesses and between research organisations and industries that have export potential. Around \$500 million has been committed to build ten industry hubs and to establish a portal that will connect businesses to each other and help them to share information.
- Venture Australia: this program aims to increase the pool of funding for Australia's innovative and knowledge-intensive start-ups including those in the technology, life sciences, bio-medical and medical devices sectors. Funding for this program is currently close to \$380 million.
- Export Market Development Grants (EMDG): this is a long-standing program which aims to support SMEs to break into export markets by reimbursing up to 50% of their expenses relating to export promotion. Recent changes to the program increased the number of grants available to exporters targeting Asian markets whilst the number of grants targeting established markets like the United States and the European Union were reduced. This program has a current funding budget of around \$125 million.

Notwithstanding the move towards programs that aim to create a business culture of innovation and encourage and support entrepreneurship, a significant amount of budgetary funding in Australia is still targeted towards 'old' industries. For instance, funding for vehicle assembly through programs like the Automotive Transformation Scheme and direct assistance to General Motors Holden, which some commentators argue might be better targeted towards niche sectors within the industry that are better able to adapt, innovate and compete internationally.

As Australia's economy moves towards a trade-exposed economy based on knowledge-intensive sectors, industry policy will have to focus more on broad-based programs that encourage innovation, commercialisation and internationalisation in services industries as well as manufacturing.

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The future of the Australian processed food sector

Rob Dossor, Economics

KEY ISSUE

The processed food sector in Australia faces significant pressure, both domestically and internationally. What can be done to increase the sector's survivability?

The future of processed food in Australia

It has been suggested that Australia should take advantage of the 'Asian century' to become the 'food bowl of Asia'.

Australia appears to be moving in this direction, as exports of particular food types are on the rise. Beef, for example, has surpassed its 2004–05 export level. Another major food export, wheat, has almost doubled its 2004–05 level to become Australia's biggest food export.

However, the Australian processed food sector faces a difficult future, as increased imports erode the sector's domestic market share. This leads to the question: how can Australia be the food bowl of Asia, if it cannot compete with imports in the domestic market?

Until recently, the Australian processed food sector was relatively insulated from import competition and was able to survive by supplying the domestic market. However, it has become clear that for the sector to compete, even in the domestic market, it must become internationally competitive.

Those industries that appear to be succeeding have focused on exports and on innovation.

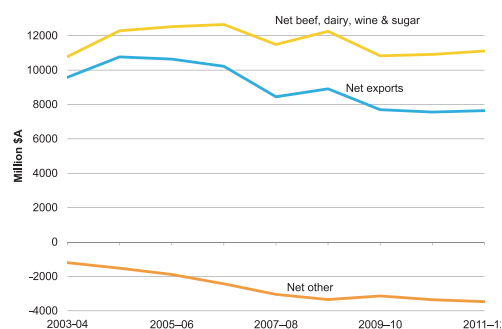
Exports to imports

Australian Bureau of Statistics (ABS) figures suggest that in the period from 2003–04 to 2009–10, the domestic market for food (including fresh food) grew by approximately 46.0%, while the processed food sector grew by only 32.2%. The sector does not appear to be keeping up with demand. Meanwhile, imports of processed foods grew by

approximately 62.0% during the period.

While Australia is a significant net exporter of processed food, the beef, sugar, wine and dairy industries account for over 72.0% of all processed food exports. These industries accounted for around 38.0% of Industry Value Added (IVA) for the sector in 2010–11.

Net processed food exports



Source: DAFF Food Statistics, various years.

The increase in imports of processed foods, typified by the importation of Italian canned tomatoes – the value of which has increased from \$33 million in 2007 to \$51 million in 2012 – has shown that processed food industries face international competition.

The domestic market for processed food is dominated by Coles and Woolworths. For most processors, growth hinges on Coles and/or Woolworths purchasing and retailing their products. Coles and Woolworths are fiercely competitive. They and their customers have demonstrated great price sensitivity, often to the detriment of more expensive domestically grown and made products. Exposure to competitive pressures has revealed the extent to which some parts of the food processing sector are unable to compete with imports.

Economies of scale

In the past many food processors relied solely on the domestic market. While this market has increased, it remains small, so processors rarely achieve economies of scale. Processors

can overcome this constraint by seeking bigger markets overseas to achieve economies of scale in production and reduce average costs.

Regulatory costs

Many food processors have a presence in several states. A number of them have claimed that dealing with multiple regulations in different jurisdictions is costly and time consuming. Several have specifically cited occupational health and safety requirements as extremely costly.

In addition to regulatory duplications, higher standards imposed by regulations may create a competitive disadvantage for Australian food processors competing against imports in the domestic market. Processors claim that higher standards often apply to domestically produced products than imported products. The Productivity Commission recently conceded that this was an issue affecting the sector.

Australian food exports are also required to meet high standards and exporters must obtain export certification from the Department of Agriculture. These standards may be higher than those of the importing country.

Lack of innovation

Ultimately, the sector must ensure it is producing products that consumers want. Effective research and development (R&D) is essential for new products to be introduced and for productivity and profits to be improved. However, in recent years some processors have stated that the limited profit margins and lack of government assistance for R&D in the sector have resulted in low levels of R&D investment. Recent changes to R&D subsidies may have improved this situation, however. ABS figures show that average levels of R&D investment for the sector are increasing – from 1.60 to 2.41% of IVA in the period 2005–06 to 2010–11. These figures remain significantly below the average R&D share of IVA for the whole manufacturing industry; this was around 4% of IVA during the period.

Cost structures

Processors claim that Australia's high domestic and international transport costs reduce their competitiveness. They insist that the current

condition of infrastructure, and transport rules including maximum weights have a negative impact on the competitiveness of their industry. Average labour costs are also higher than in many competing countries.

Labour market

Much of the food processing sector is located in rural and regional areas. This factor, as well as a decline in food and food science tertiary education enrolments, and increased competition with the mining sector, has resulted in many processors having difficulty finding and retaining staff. It is also likely that the relatively low remuneration the sector offers affects processors' ability to attract and retain staff.

The future of the sector

While the majority of the sector appears to be struggling to compete, some industries are succeeding. The beef, sugar, wine and dairy industries have either surpassed previous peak export levels, or have steadily increased their share of processed food exports. These industries have focused on export markets and innovation. They have achieved economies of scale – and improved their bargaining position with Coles and Woolworths.

Industries which are having their market share eroded by imports may be able to learn from industries which are succeeding on the export market. By doing so, they will compete more effectively on the domestic market. If this happens Australia could really become the food bowl of Asia.

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Live animal exports

Moira Coombs, Law and Bills Digest and Hannah Gobbett, Economics

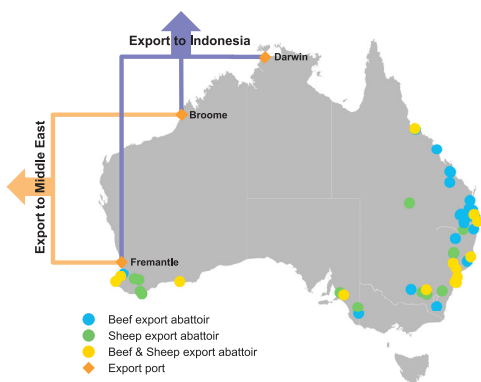
KEY ISSUE

Recent media coverage of animal abuse in the live export trade has led many to question whether the trade should be continued, or replaced with exports of Australian processed lamb and beef.

Live animal exports have been, and remain, a contentious issue. Many petitions have been made to Parliament to end the live export trade, such as that presented in November 2012 by Kelvin Thomson MP with 60,723 petitioners.

In 1985, the Senate Select Committee on Animal Welfare in its report *The Export of Live Sheep from Australia* concluded that if a decision on the future of the trade were made on animal welfare grounds alone, there was enough evidence to stop the trade.

Map of Australian export abattoirs and main live export ports



Source: AusMeat Limited

Please note that due to the close proximity of several livestock processing companies in some areas (Tamworth and Townsville), the location marker may not be exact as locations hold numerous abattoirs with different livestock processing capabilities.

Taking into account economic and other considerations, the Committee recognised that the trade would continue, and therefore called for animal welfare improvements. The Committee also recommended that the Government encourage the expansion of the refrigerated trade, with the aim of eventually replacing the live trade. However, the UN Comtrade database indicates Australia remains the world's largest exporter of live sheep and fourth largest for live cattle, with the industry employing an estimated 10,000 in regional Australia alone.

Animal welfare organisations, including the RSPCA and the World Society for the Protection of Animals (WSPA), advocate that live exports be replaced with meat trade only. Both organisations have commissioned several investigations by consulting firm ACIL Tasman into the live export trade, which indicate that moving away from live exports would offer opportunities for Australian livestock producers. Further, the WSPA report on live cattle export found that domestic processing contributes more to regional economic activity and employment than live exports.

However, there are currently no export abattoirs in the Northern Territory or the northern region of Western Australia, where the majority of live export producers are concentrated. This is largely due to a lack of skilled and semi-skilled labour and low estimated returns. Prohibitively high transport costs (per head of livestock) restrict many north Australian producers from transporting livestock to eastern states' export abattoirs.

Structure of the industry

There is high international demand for Australian livestock, as Australia is one of the few producers of high quality foot-and-mouth disease free animals. A strong preference for live sheep exists in the Middle East due to high fodder, water and meat subsidies provided by a number of Middle Eastern governments, the live sale practices in local souks and the demand for the animals to be slaughtered according to Halal practices.

There is also strong demand for live cattle in South East Asian nations, owing to government support for domestic feedlot industries in Indonesia as well as a lack of cold storage throughout the supply chain. However, a peak Islamic body commented that Australian halal meat could be exported to Indonesia.

The live export trade is dominated by exports of cattle (which comprise 90% of total live exports) and account for 2.7% of Australian agricultural exports from 2006–2009. In this period the total value of live exports was \$5,886.6 million for cattle and \$311.9 million for sheep (in current prices).

Approximately 75% of exported sheep come from Western Australia, 14% from Victoria and 10% from South Australia. Australia's largest market for live sheep is the Middle East, for which farmers are increasingly breeding fat-tailed breeds favoured by Middle Eastern consumers.

In terms of cattle, 40% of total live exports were sourced from the Northern Territory, 39% from Western Australia and 13% from Queensland in 2006–2009. Indonesia remains the largest market for live cattle; however, Israel, Malaysia, Japan and China are developing markets.

Scandal and response

The Keniry Review was commissioned after the Cormo Express disaster in August 2003 when a shipload of 57,937 sheep bound for Saudi Arabia was rejected because importing authorities claimed that 6% were infected with 'scabby mouth'. By the time the ship was finally unloaded in Eritrea, 5,691 sheep had died. The Australian Government suspended live exports to Saudi Arabia but resumed them in 2005. The Keniry Review recommended a greater role for the Australian Quarantine and Inspection Service in setting standards and quality assurance and proposed a compulsory research and development levy on the industry.

An ABC Four Corners program on 30 May 2011 exposed horrific scenes of cruelty to Australian cattle while being slaughtered in Indonesian abattoirs, resulting in a vociferous response from the public. The then Minister for Agriculture, Fisheries and Forestry, Senator

Joe Ludwig, suspended the trade and later announced an independent review of Australia's live export trade conducted by Bill Farmer AO. The Farmer Review recommended a comprehensive review of the Australian Standards for the Export of Livestock and the extension of supply chain reforms, then in place for Indonesia, to all countries.

Regulatory regime

The regulatory scheme governing animal exports is the Exporter Supply Chain Assurance System (ESCAS). The Australian Meat and Live-stock Industry Act 1997 and the Export Control (Animals) Order 2004 set out the export licensing and permit system generally. The ESCAS framework is incorporated into this pre-existing system which means that the framework is mandatory.

The licensed exporter must submit their proposed ESCAS arrangements for assessment together with a notice of intention to export and a consignment risk management plan. The ESCAS must contain evidence of compliance with international animal welfare standards, demonstrate control and traceability through the supply chain, meet reporting and accountability standards, and include independent auditing, before assessment and approval by the Department of Agriculture.

Recent developments

The Indonesian government has signalled that it may seek to buy land in Australia to raise beef. While this may raise concerns about foreign investment, any cattle exported from such enterprises would be subject to the same rules, regardless of ownership.

In September 2013 Deputy Prime Minister and Minister for Infrastructure and Regional Development, Mr Warren Truss, stated that strengthening all of Australia's livestock exports to all trading partners would be a priority for the newly elected government.

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Australia's foreign investment policy

Kali Sanyal, Economics

KEY ISSUE

Foreign investment in traditionally Australian owned and influenced sectors, such as agriculture, banking, air transport, telecommunications and shipping industries has led to foreign investment policy becoming a contentious and increasingly debated issue.

Australia's foreign investment policy consists of five elements:

Legislation

The Foreign Acquisitions and Takeovers Act 1975 (FATA) provides the legislative framework for the foreign investment screening regime.

Australia's foreign investment policy

Australia's foreign investment policy provides guidance to foreign investors on the Government's approach to administering the FATA. The policy also identifies a number of specific types of investment proposals that are required to be notified to the Government even if the FATA does not appear to apply.

Private foreign investors are required to seek prior government approval before acquiring a substantial interest (upwards of 15%) in a corporation or control of an Australian business valued above \$248 million (in 2013 prices, indexed annually). All foreign government owned entities must apply to the Government for approval of any acquisition of Australian assets, irrespective of the asset value.

However, for investors from New Zealand and the United States, the \$248 million threshold only applies for investments in certain sensitive sectors. In other sectors, a \$1,078 million threshold applies.

The Treasurer

The Treasurer is ultimately responsible for all decisions relating to foreign investment, and for the administration of Australian foreign investment policy. The FATA allows the Treasurer or his/her delegate (usually the Assistant Treasurer) to review investment proposals to decide if they are contrary to the Australian national interest. If this occurs, the Treasurer can block proposals, or apply implementation conditions to ensure that the national interest is protected.

Applicants have no right of administrative or judicial review of foreign investment decisions made under the FATA or the policy. The Administrative Decisions (Judicial Review) Act 1977 specifically exempts decisions made under the FATA from judicial review.

The Foreign Investment Review Board

The Treasurer is advised and assisted by the Foreign Investment Review Board (FIRB) which administers the FATA in accordance with the policy. The FIRB is an administrative body with no statutory existence, and FATA makes no reference to it. However, the foreign investment policy confirms the FIRB's role. All decisions by the Treasurer relating to a foreign investment proposal are underpinned by analysis and recommendations made by the FIRB.

Prescribed sensitive sectors

Separate legislation imposes other requirements and/or limits on foreign investment in the following areas:

- the banking sector – foreign ownership in the banking sector must be consistent with the Banking Act 1959, the Financial Sector (Shareholdings) Act 1998 and national banking policy
- airports – the Airports Act 1996 limits foreign ownership of some airports to 49%
- the shipping industry – the Shipping Registration Act 1981 requires that a ship must be majority Australian-owned if it is to be registered in Australia, unless it is designated as chartered by an Australian operator

- the telecommunications sector – aggregate foreign ownership of Telstra is limited to 35% and individual foreign investors are only allowed a maximum of 5%.

Approved foreign investment in Australia

According to FIRB data, between 2007–08 and 2011–12, the total foreign investment approved was \$844.8 billion. Of the total, mining comprised \$348.4 billion (41.2%), services \$155.9 billion (18.5%), manufacturing \$111.3 billion (13.2%) and finance and insurance \$42.6 billion (5%).

During the same period, the total approved investment in agriculture stood at \$12.6 billion, or about 1.5% of the total foreign investment (\$844.8 billion) approved by the Government.

Policy on foreign investment in agriculture

There has been a good deal of debate recently about foreign investment in agricultural land and businesses. As noted above, foreign government entities are subject to scrutiny for any investment proposal. Proposals from private investors in agribusinesses (including those involving agricultural land) are subject to the same thresholds that apply to other foreign acquisitions of Australian companies or business assets.

The Government assesses foreign investment applications by their impact on the following criteria:

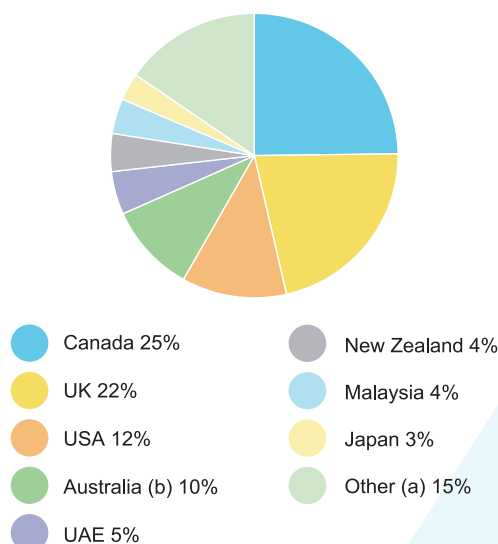
- the quality and availability of Australia's agricultural resources (including water)
- land access and use
- agricultural production and productivity
- Australia's capacity to remain a reliable supplier of agricultural produce, both to the Australian community and its trading partners
- biodiversity and
- employment and prosperity in Australia's local and regional communities.

In 2011–12, the largest source country for investment by value in the agricultural sector was Canada (\$1.4 billion), followed by the United Kingdom (\$0.6 billion) and the United States of America (\$0.5 billion).

The figure below indicates approved foreign investment in the agricultural sector by source country over the period between 2007–08 and 2011–12.

From 2007–08 to 2011–12, Canadian (\$3.1 billion), British (\$2.7 billion) and American (\$1.5 billion) firms were the largest investors in the Australian agricultural sector.

Figure 1: FIRB approval in agriculture 2007–08 to 2011–12



Data source: FIRB

The national land register

In view of the absence of exact information regarding foreign land transactions at the national level, the Government recently initiated the process to form a national land register. The purpose of the register is to improve transparency of foreign ownership in agricultural land without imposing unnecessary burdens on investors or duplicating work already undertaken by State and Territory governments.

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Over-the-counter derivatives – high risk investments in a largely unregulated market

Bernard Pulle, Economics

KEY ISSUE

A main cause of the global financial crisis was the largely unregulated over-the-counter derivatives market internationally. This article sets out briefly the approach of the Australian Government to meeting Group of 20 (G20) commitments entered into at Pittsburgh in 2009 to ensure a transition into a regulated derivatives market.

Introduction

A 'derivative' is a security instrument whose price is dependent upon, or derived from, underlying assets such as stocks, bonds, commodities, currencies, interest rates and market indexes.

Derivative products have traditionally been traded through bilateral arrangements between parties or 'over-the-counter' (OTC) transactions, and not through a central clearing exchange like a stock exchange or trading platform. There was a lack of transparency concerning the risk profile of participants as well as the values of transactions.

In 2009, following the global financial crisis of 2008, the G20, which comprises the 19 largest economies, including Australia, and the European Union, committed at Pittsburgh to a global transition from bilateral trading of OTC derivatives to:

- trading all standardised OTC derivative transactions on exchanges or trading platforms
- centrally clearing all standardised OTC derivative transactions and
- reporting of all OTC derivative transactions to derivative trade repositories (TRs).

In response to a request by the Australian Government to ascertain how its G20 commitments might best be implemented, the Council of Financial Regulators (CFR) (which comprises the Reserve Bank of Australia, the Australian Prudential Regulation Authority, the Australian Securities and Investments Commission and Treasury), after an extensive consultative process, provided a report, OTC Derivatives Market Reform Considerations, on 20 March 2012 (the CFR Report).

The Australian OTC Derivatives Market

The CFR report concluded that the volumes and types of OTC derivatives transactions undertaken in Australia are small by global standards, comprising only 2% of global notional turnover. Further, as is the case in most countries, participants in the Australian-located OTC derivatives market undertake a large amount of cross-border activity.

The CFR report states that financial institutions use a wide variety of derivatives in the Australian market. Some participants use simple single-currency interest rate derivatives to hedge interest rate risks. Others use a range of single and cross-currency derivatives, foreign exchange (FX) derivatives and credit derivatives to manage exposures. Corporates use derivatives covering single and cross-currency interest rates, FX and commodity derivatives.

Proposed financial market infrastructure

The CFR report proposes the establishment of a financial market infrastructure (FMI) comprising three institutions, namely, trade repositories (TRs), central counterparties (CCPs) and exchanges and trading platforms to meet the G20 commitments. It also specifies the roles of each of these institutions.

Briefly, a TR is a centralised registry that will maintain an electronic database of records of derivatives transactions. Trade information will be submitted to a TR by one or both counterparties to a transaction and will include transaction maturity, price, reference entity and counterparty.

A CCP will play a key role in central clearing and settlement of derivatives transactions. Clearing relates to identifying the obligations of both parties to a transaction and settlement occurs when the transfer of the securities and funds takes place. A CCP does this by replacing all bilateral contracts between derivative market participants by a simpler set of exposures between the CCP and each individual participant. Because a CCP deals with several transactions of various participants, it is in a position to take more risks because several bilateral exposures are replaced by multilateral netting of contracts within the control of a CCP.

The CFR Report proposes that increased uptake in CCP centralised arrangements for OTC derivatives transactions should be an industry-led initiative. The incentive for participation in the CCP arrangement would be a lower capital requirement for participants.

The legislative framework in Australia

The Corporations Act 2001 (Corporations Act) was amended in December 2012 to provide a framework for making rules to cover derivative transactions. In July 2013, the Corporations Act and other Commonwealth laws were amended to assist CCPs in managing defaults of clearing participants.

The ASIC Derivative Transaction Rules (Reporting) 2013, which commenced on 11 July 2013, is a legislative instrument which sets out the rules that govern the reporting of derivative transactions to TRs in Australia.

Progress reports by the FSB

The G20 Pittsburgh Statement required the Financial Stability Board (FSB) to assess regularly the implementation of G20 commitments by all members, including Australia. The Fifth Progress Report on Implementation by the FSB was issued on 15 April 2013.

It recorded that legislation was in place in Australia to require reporting OTC derivatives contracts. Reporting requirements were expected to begin for some participants in the third quarter of 2013, and to be fully phased in over 18 months.

It also noted that although necessary laws are in place to implement mandatory trading obligations, authorities have not yet required any products to be traded on organised trading platforms. They are waiting for comprehensive trade repository information before requiring any specific products to be traded on organised trading platforms.

The Sixth Progress Report is expected in October 2013.

Parliamentary committee overview

The Parliamentary Joint Committee on Corporations and Financial Services (the Committee), in a report dated 15 May 2013, recommended that ASIC update the Committee on Australia's implementation of OTC derivatives market reforms.

The Committee approved the strategic approach that the Australian regulators have taken in implementing the law governing derivatives and the central clearing arrangement.

The Committee expects Treasury and ASIC to update it on the progress made by Australia in implementing the reforms, one month after the release of the October 2013 FSB report.

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DIY super: a continuing trend?

Kai Swoboda, Economics

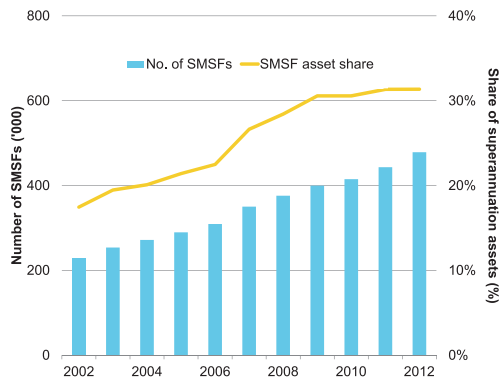
KEY ISSUE

'DIY super', formalised through the self-managed superannuation fund (SMSF) regulatory framework, is an important and growing part of the superannuation system. With the SMSF sector largely seen to operate effectively, any further intervention needs to carefully consider the impact of additional regulation on SMSFs and the superannuation industry as a whole.

Self-managed Superannuation Funds (SMSFs)—funds with one to four members where the members also actively participate in the management of the fund — are an important and growing part of the superannuation sector. The availability of the option to establish an SMSF provides for greater choice and flexibility for superannuation fund members and also creates some competitive pressures within the superannuation industry as a whole.

Over the last decade, the number of SMSFs has increased by an average of 7.7% per year, rising from around 227,000 in June 2002, to around 478,000 by June 2012. Over the same period, the value of superannuation assets held in SMSFs increased from \$90 billion to \$439 billion. By June 2012 the SMSF sector accounted for around 31% of total superannuation assets (Figure 1). Superannuation industry analysts generally agree that the SMSF sector will continue to grow at similar rates.

Figure 1: SMSF growth, 2002 to 2012



Source: Australian Prudential Regulation Authority.

Choosing an SMSF

The main reason people choose to establish an SMSF is to gain control of their retirement savings. Many people believe that they can make sound investment decisions which will outperform those made by an institutional superannuation fund. In addition, establishing an SMSF can save on fees. There are typically three groups of SMSF trustees. Around 30% of SMSF trustees are 'controllers' (those who manage their money themselves), 50% are 'coach seekers' (those who need information to make their decisions) and the remaining 20% are 'outsourcers' (those who hire people to manage their funds).

Compared to those in institutional superannuation funds, members of SMSFs:

- tend to be older (In coming years this difference may decline as younger people are increasingly attracted to establishing an SMSF)
- have significantly higher balances (While this is a reflection of the older population group that is a feature of SMSFs, it is also an indicator that the benefits of establishing an SMSF may not outweigh the costs for those with lower account balances)

- are more conservative in asset allocation, with a higher proportion of cash and term deposits and a lower proportion of international shares — this may also be related to the older population group favouring capital security rather than higher (though potentially risky) returns as they approach retirement.

Regulating SMSFs

SMSFs and institutional funds share the same primary objective — providing benefits on or after the member's retirement, on reaching age 65, or on earlier death. However, a key difference is in the regulatory approach. Institutional funds are subject to a regulatory framework overseen by the Australian Prudential Regulation Authority that emphasises risk management and stability. SMSFs are largely regulated on a compliance basis by the Australian Taxation Office.

In addition to this difference in regulatory approach, some SMSF-specific arrangements are also in place. These additional arrangements support the primary objective of providing for retirement benefits. For example, there are additional rules for SMSFs relating to prohibiting the acquisition of certain assets from related parties.

During the 43rd Parliament, a number of SMSF-specific regulatory arrangements were implemented, including an SMSF auditor registration scheme and limits on investing in collectables and personal use assets. Several others, including a penalty regime for those involved in schemes to access superannuation early and creating an administrative penalty regime for SMSF trustees, were introduced into the Parliament but have lapsed. Some of these may be further considered by the 44th Parliament.

SMSF sector performance and potential regulatory issues

It is difficult to make direct comparisons between the performance of SMSFs and institutional funds. Where data are available, average annual SMSF returns have been similar to institutional funds over recent years. In general, SMSFs with larger balances have performed better than SMSFs with lower balances.

Despite this solid performance relative to institutional funds, there remain a number of concerns about SMSFs, including how funds are established and managed, the appropriateness of certain investments and the capacity of trustees.

The Cooper Review of superannuation (May 2009–June 2010) considered that the SMSF sector was 'largely successful and well-functioning'. Nevertheless, policy interventions that have continued to be discussed or emerged since the Cooper Review include:

- whether a mandatory minimum account balance should be imposed
- the need for an SMSF compensation scheme funded by an SMSF levy to protect against losses
- improving the proficiency of trustees and the capacity of trustees to manage their SMSF as they age or a trustee dies
- the role that service providers such as accountants and financial advisers play in assisting trustees to manage their SMSF.

Balancing the need for further SMSF regulation with the choice to use an SMSF

The decision to establish an SMSF rather than utilise the protections provided in a prudentially-regulated institutional superannuation fund is one that individuals are free to make.

Any further intervention by government needs to balance carefully the relative costs and benefits from additional regulation as well as the superannuation system-wide benefits that are available with an active and successful SMSF sector.

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Current negotiations on free trade agreements

Eugenia Karanikolas, Economics

KEY ISSUE

Australia is currently negotiating nine free trade agreements (FTAs) including bilateral agreements with three of its largest trading partners, China, Japan and South Korea. Australia is also part of the negotiations for two mega-regional agreements, including the Trans-Pacific Partnership Agreement (TPP), which focuses on facilitating trade by tackling issues like intellectual property, environment and labour. Contentious negotiation issues include the lowering of hurdles for investment in sensitive areas, reducing protection in agriculture and dealing with investment disputes. More generally, there is a concern that the proliferation of FTAs may result in overlapping trade rules, which may raise transaction costs for business and result in the fragmentation of trade.

Background

Australia has long been a supporter of trade liberalisation undertaken on a 'non-discriminatory' basis. Australia has committed itself over the years to reducing its trade barriers and has supported multilateral efforts through organisations such as the World Trade Organization.

In the past two decades, however, there has been a significant increase in the signing of preferential trade agreements, commonly referred to as free trade agreements (FTAs) around the world. This is mainly because the governments of advanced economies have failed to reach agreement with those of less developed economies on the extent to which they will liberalise multilateral trade in sensitive areas like agriculture, intellectual property, investment and services.

Australia's trade policy has mirrored these international trends with the country now being a signatory to seven FTAs and undergoing negotiations on nine more.

Australia's FTA debate

Within Australia there is a widely held consensus that international trade is vital for the country's long-term prosperity. Opinions differ, however, on how trade should best be facilitated – that is, should it be multilaterally or through preferential trade agreements.

Proponents of multilateralism believe that FTAs are predominantly trade distortionary and their proliferation may lead to the creation of competing trade blocs with potential risks to economic stability. The preferential and discriminatory nature of FTAs has also been raised as an issue by the Productivity Commission (PC) which expressed scepticism on the extent to which such agreements have significant net economic benefits to Australia.

The high number of trade agreements among countries in the Asia Pacific has also raised concerns about overlapping trade rules and the effect this has on businesses because of the possible increase in transaction costs. A case in point is Australia, which is currently negotiating on a bilateral level with Japan for two different agreements, the Australia-Japan bilateral FTA and the regional Trans-Pacific Partnership (TPP) agreement. Twelve countries are involved in the TPP negotiations but most market access issues are negotiated at a bilateral level – that is, country to country.

On the other side of the debate, proponents argue that FTAs are complementary to, rather than in competition with, the multilateral system and are essential if Australia is to continue to gain favourable market access for its exports. It is also argued that FTAs provide a more pragmatic approach in facilitating trade. This is because the small number of countries involved makes it easier for an agreement to be reached, and the agreement has a better chance of being higher quality with a broader focus. FTAs, it is argued, are more than just economic documents – they are a tool of economic diplomacy.

Current status of negotiations

In negotiating the current FTAs, some common issues are present, albeit to different degrees. Specifically, Australia is resisting pressure by its partners to include investor-state dispute settlements (ISDSs) provisions, which, in essence, grant foreign investors rights above those afforded to domestic investors. This issue is a significant hurdle in negotiating the TPP because countries like the United States, with its large number of multinational companies, is pushing for such inclusions. In Australia, a number of political and economic institutions, including the PC, have highlighted international evidence showing that ISDSs are risky for sovereign countries. They may be used by foreign companies to restrict the Government's future ability to introduce welfare-enhancing reforms.

Foreign investment has been another contentious issue, especially with China. In this case, Australia has been resisting China's demands to grant it the same investment rights as those given to the United States and New Zealand, which allow for investments of up to \$1 billion not to be screened by the Foreign Investment Review Board (FIRB). This issue has been a focus of recent political and public debate in Australia.

Notwithstanding the significant opposition towards granting China such investment rights, positions are beginning to shift. This shift is possibly prompted by evidence showing that Australia's foreign investment policies are restrictive when compared to other Organisation for Economic Co-operation and Development (OECD) countries. There is also the perception that FIRB's screenings are more or less routine – only two major takeovers of Australian assets have been rejected since 2001. (For more information, see 'Australia's foreign investment policy' article in this publication).

Australia has been pushing for market access for its agricultural goods, especially beef and dairy. This is especially so in the negotiations with Japan, Australia's largest export market for agricultural goods, and Korea. In return, Japan and Korea are asking that Australia eliminates its tariffs on cars.

As part of the TPP, Australia is also pushing for negotiations to be re-opened with the United States regarding market access for sugar, which was left out of the Australia-US FTA. The United States is so far refusing to renegotiate.

Criticisms of FTA rationale and negotiating process

Reports by economic institutions like the PC, as well as business surveys, have not found overwhelming evidence to suggest that FTAs have resulted in significant benefits to Australia's businesses. In its Bilateral and Regional Trade Agreements report, the PC pointed out the lack of transparency in the negotiating process and the tendency by governments to oversell the benefits of FTAs. Based on these findings, the PC recommended that a thorough and independent examination of each FTA should be undertaken at different stages of the negotiating process. It recommended that higher levels of transparency and public accountability regarding the process be adopted so that the public is aware of what the issues are and how much is being spent to facilitate the negotiations.

The Government has signalled its intention to place trade and investment at the centre of its economic agenda. Finalising the trade agreements with China, Korea and Japan has been flagged as a priority. Assuming these negotiations are successful, the Parliament will be called upon to consider legislation which will give effect to these agreements.

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Temporary skilled migration

Gareth Larsen, Social Policy

KEY ISSUE

The temporary skilled migration program, or subclass 457, is responsive to economic changes and employment needs. However, the program has been subject to some instances of exploitation, which resulted in reforms and greater oversight. This article focuses on recent integrity concerns. It also considers the program in the context of permanent migration, population and settlement.

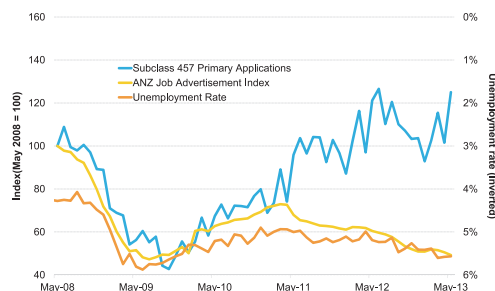
Impact of skilled migration on jobs for Australian workers

The uncapped Temporary Work (Skilled) visa (subclass 457) program has been built on the premise that it does not undermine job opportunities for Australians.

The program, driven by employer demand, allows employers to access the services of overseas workers where a genuine skill shortage exists, or where suitably qualified Australian workers are not available. This is on the condition that the employers commit to the training of Australians to reduce their dependence on overseas labour in the longer term.

Subclass 457 has been highly responsive to the vagaries of the economy and to the needs of employers. When unemployment increases, employers advertise less, and from 2003 until 2011, subclass 457 visa lodgements responded precisely to job vacancies (grants data shows a similar trend, but lodgements provide a more timely connection with job vacancy data). However, as the information in Figure 1 shows, in 2011, as job vacancies declined, there was a sharp rise in the number of subclass 457 visa lodgements.

Figure 1: 457 applications and employment trends, five years to May 2013



Source: Parliamentary Library analysis using ABS Labour Force data, DIAC statistics and the ANZ job advertisement series

The gap between lodgements and job vacancies/unemployment signified strong demand from overseas workers who were experiencing comparatively poor economic conditions. It has been suggested that this trend was also indicative of employers seeking the services of overseas workers in place of Australian workers.

In 2012, the then Department of Immigration and Citizenship (DIAC) identified that the subclass 457 program was growing at a record rate, especially in industries and geographical regions that did not appear to be experiencing skills shortages. A Migration Council Australia survey subsequently revealed that while around 15% of employers had no difficulty finding suitable local labour, they were still sponsoring employees from overseas under the program. Recent media coverage points to underpayments in IT, hospitality, construction and manufacturing industries.

In July 2013, policy changes and legislative amendments sought to improve the integrity of the program without having an adverse impact on its responsiveness to genuine employer needs. Steps were taken to prioritise the employment and training of local workers, to legislate sponsor obligations, to empower Fair Work Australia to investigate breaches and to strengthen the Department's ability to prosecute wrongdoing. It is too early to determine the exact consequences of these steps.

While subclass 457 primary visa holders are approved to meet specific skill needs, spouses and dependents may work across industries in skilled or unskilled occupations during their stay in Australia. So the work rights of secondary visa holders is an additional labour force issue when considering subclass 457 visas.

Temporary to permanent migration

The subclass 457 visa has also become a popular pathway to permanent migration. In 2011–12, subclass 457 visa holders accounted for 81% of the Employer Nominated Scheme and 46% of the Regional Skilled Migration Scheme.

Around 40% of applications for permanent visas are from migrants already in Australia, of these, over half will have held a subclass 457 visa. In 2012 DIAC announced more streamlined, simplified and fast-tracking options for transitioning from the subclass 457 program to permanent migration.

Before becoming permanent residents, subclass 457 visa holders are often counted towards Australia's population gain; people who have stayed in Australia 12 months out of a 16 month period are included in the Australian Bureau of Statistics' calculation of net overseas migration (NOM). NOM accounts for 60% of Australia's population growth and over recent years, the largest contribution to NOM has been from people on temporary visas.

Since 2012, NOM has been above the levels assumed in Treasury's 2010 Intergenerational Report (IGR) which suggested it would fall to, and remain at 180,000 from 2012 onwards. However, for the year ending 31 December 2012, the NOM figure was 235,900. If these levels were to continue, Australia's population would be considerably more than the IGR's projection of 35.9 million by 2050.

Settlement and services

Where temporary residents settle is an important consideration for policy decisions and future planning across all levels of government. Particularly strong growth in demand in Western Australia (WA) for example means that it now ranks second to New South Wales (NSW) for subclass 457 visa holders (almost 33,000 as at 30 June 2012). In WA, construction and mining

are the largest sponsor industries involving many fly-in-fly-out arrangements.

Most subclass 457 visa holders originate from the United Kingdom, India, Ireland, the Philippines and the United States of America. Temporary workers are required to demonstrate a level of English language proficiency unless their income is in excess of \$96,400. There are no English language requirements for dependents. A recent report identified that subclass 457 spouses do not have sufficient support and can struggle in terms of employment, English language acquisition and understanding of Australian culture.

While subclass 457 workers pay taxes, they are not entitled to services such as employment assistance, English language classes, settlement support and Medicare (unless reciprocal health arrangements exist). Comprehensive private health insurance is compulsory. Those who become permanent residents may access settlement services, but only if their arrival in Australia was within the last five years.

Policy directions

The subclass 457 program is designed to respond rapidly to temporary economic and employer needs, but it should not be viewed from this perspective alone. The program has important implications for Australia's population growth and for longer term skilled and unskilled labour market planning.

The program may benefit further from a consistent, planned and measured approach to monitoring and reform. Closer scrutiny of other temporary programs may also be worth consideration by the Parliament.

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PUBLIC FINANCES

The background of the page is composed of several overlapping, semi-transparent geometric shapes in various shades of blue and teal. These shapes create a modern, layered effect, with some areas appearing darker due to the overlap. The overall aesthetic is clean and professional.

Tax avoidance by multinational enterprises – Australian Government initiatives to avoid erosion of corporate tax base

Bernard Pulle, Economics

KEY ISSUE

This article examines the measures the Australian Government has introduced recently and measures under consideration in co-ordinated action with Organisation for Economic Co-operation and Development (OECD)/G20 initiatives to protect the erosion in its corporate tax base by multinational enterprises shifting profits to low tax jurisdictions.

Empirical evidence of profit shifting by multinationals

Over the last two years the fact that certain multinational enterprises shift their profits to low tax jurisdictions, thus avoiding paying tax in the source country where the profits are made, has received much media publicity worldwide.

Attention given to large scale tax avoidance by enterprises such as Amazon, Google and Starbucks led the House of Lords Select Committee on Economic Affairs in the United Kingdom (UK) Parliament to inquire into tax minimisation practices of multinational enterprises. On 31 July 2013, this committee published: *Tackling corporate tax avoidance in a global economy: is a new approach needed?*

In the United States, the President's Framework for Business Tax Reform concluded that income shifting by multinationals is a significant concern and should be addressed through tax reform.

Treasury examination of the issue

In July 2013, the Treasury prepared a scoping paper on Risks to the Sustainability of Australia's Corporate Tax Base.

This paper concluded:

- there was relatively little evidence of widespread base erosion and profit shifting (BEPS) by multinational enterprises (MNEs) operating in Australia.

- The absence of widespread BEPS in Australia is due, among other things, to the actions by successive governments to ensure the integrity of Australia's tax laws, the relative effectiveness of the Australian Tax Office in enforcing corporate tax law and the generally good compliance behaviour of companies.
- The failure of international tax rules to keep pace with changes in the global business environment poses a significant risk to Australia's corporate tax base.
- The rise of the digital economy and the increased importance of intangibles present challenges to the corporate tax bases of all jurisdictions, including Australia.

The scoping paper noted that the proposed joint OECD and G20 work is an opportunity to make significant progress in modernising global multilateral tax arrangements, and that as G20 Chair in 2014, Australia can play a prominent role in determining and driving this reform agenda.

Significant actions taken by the Australian Government

The Australian Parliament has passed legislation over the last three years to tighten the rules in relation to cross-border transfer pricing in income tax law.

Transfer pricing refers to the prices charged when one entity of a multinational group buys or sells products or services from another entity of the same group in a different country. The prices charged will have an impact on the level of profits of each entity of the multinational group, and therefore the amount of tax they have to pay, in the respective countries.

The rules are intended to require multinational firms to price intra-group goods and services between related parties to reflect the economic contribution of their Australian operations properly by applying the arm's length principle.

The concept of an arm's length transaction is to ensure that both parties in the deal are acting in their own self-interest and that they are not subject to any pressure or duress from the other party or a related party that controls both parties, as in a multinational group.

Consultations were undertaken by the Treasury in June/July 2013 on:

- closing loopholes in the Offshore Banking Unit Regime
- targeting the deduction for mining/resource exploration to genuine exploration activity and
- preventing 'dividend washing', which is a device to enable shareholders to claim two sets of franking credits on what is effectively the same parcel of shares.

These and other proposals announced by the former Labor Government await decision by the new Government.

Australia's commitment to the G20 declaration

The leaders of the G20 meeting in St. Petersburg on 5–6 September 2013 made a declaration that BEPS by multinational enterprises should be dealt with by taxing profits in the jurisdictions where economic activities deriving those profits are performed, and where value is created.

They also endorsed an OECD Action Plan to address BEPS which was included as an annex to the declaration. The Action Plan outlines 15 issues that are to be dealt with by individual jurisdictions as well as by collective action and regular reporting of progress made.

The declaration endorsed the OECD proposal for a global model for multilateral and bilateral automatic exchange of information between jurisdictions to take effect by the end of 2015. It called upon all other jurisdictions to participate with the G20 in the automatic exchange of information as the global standard.

The declaration also made a pledge to assist developing countries to benefit from a more transparent international tax system, and thereby enhance their revenue capacity.

Concluding comments

The introduction to the Treasury scoping paper states that it is in Australia's interest to monitor and act on developments that pose a risk to its corporate tax base. This is because it collects more corporate tax as a share of GDP than most other OECD countries, despite having a lower statutory tax rate than the OECD weighted average.

This will require the continuing of, and building upon, initiatives undertaken in recent years in the reform of domestic tax law in areas such as transfer pricing and general tax avoidance. It will also require renegotiating Australia's tax treaties where necessary to ensure that multinationals pay their tax on profits on economic activities performed in Australia, where value is created, in accordance with the recent G20 declaration.

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Tax expenditures: costs to government that are not in the Budget

Dr Anne Holmes and Hannah Gobbett, Economics

KEY ISSUE

A tax expenditure is the provision of a benefit by way of preferential treatment in the tax system. It has a similar effect on the budget to direct expenditure, but is subject to far less scrutiny. Transparency would be increased in many cases if tax expenditures were replaced with direct expenditure.

The nature and scope of tax expenditures

When the Government exempts an activity from tax, it has the same effect on the budget as if the Government had given a direct subsidy to that activity. A benefit that is provided in this way is called a tax expenditure. Treasury defines a tax expenditure as:

... a provision of the tax law that provides a benefit to a specified activity or class of taxpayer that is concessional when compared to the 'standard' tax treatment that would apply.

Tax exemptions, tax deductions, tax offsets, concessional tax rates and deferrals of tax liability are examples of tax expenditures.

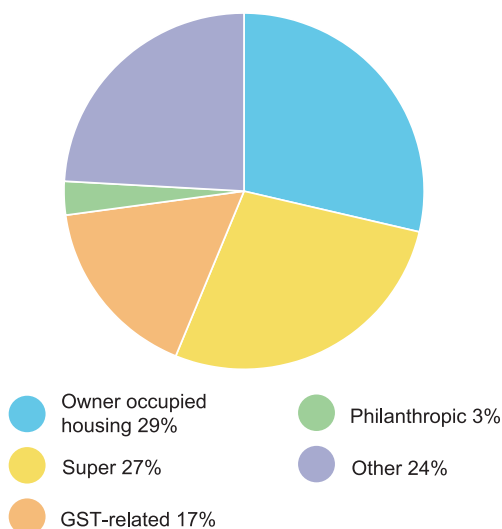
Tax expenditures are reported in an annual statement by Treasury. In 2012–13, there were 363 tax expenditures provided under the Australian tax system, the total value of which was estimated at approximately \$115 billion, or 7.5% of Gross Domestic Product (GDP). For comparison, total government direct spending in 2012–13 was about 23.5% of GDP.

Structural features of the tax system, such as being able to deduct the costs incurred in earning income, can result in large benefits to taxpayers but not be counted as tax expenditures. Negative gearing is an example. Further, Family Tax Benefit and the private health insurance rebate are regarded as direct spending.

The large tax expenditures are shown in Figure 1. There are also several items which Treasury estimates as 'large' but cannot quantify; for example, the income tax exemption for charitable, religious, scientific and community organisations.

Tax expenditures are intended to achieve policy objectives of the Government. They are essentially the same as government spending programs. For example, the Government's support of around \$75 billion in 2013–14 for the retirement income system consisted of direct payments through the

Figure 1: Major measured tax expenditures, 2012–13



Source: Treasury.

age pension (52%), payments to superannuation funds under the superannuation co-contribution scheme and low income superannuation scheme (2%), and various superannuation tax concessions (46%). Because they are administered through the taxation system, tax expenditures do not require annual appropriation bills. The Henry Review of Australia's tax system observed

that tax expenditures are less transparent and accountable than program measures, they are not subject to routine evaluation and usually there is no 'sunset' provision.

It might be expected that tax expenditures should be looked at in the same way as direct spending, in terms of equity, efficiency and effectiveness, simplicity and sustainability.

Equity

Because Australia has a progressive tax system – the marginal rate of tax gets higher as income goes up – most tax expenditures deliver a higher rate of subsidy to the more affluent. Many also require that funds be spent before the claim can be made, which may be difficult for people on low incomes.

The goods and services tax (GST) is levied at a single rate, so on the face of it an exemption should affect everyone equally. However, education, health and financial services are 'superior' goods: people spend a greater proportion of their income on them as their income rises. More affluent people, therefore, gain more from the exemption of these services from the GST.

Kerrie Sadiq, in an Australian Tax Forum article, argues that because tax expenditures are often granted as a result of lobbying, and because they are not transparent, they are often seen as unfair.

Efficiency and effectiveness

The outcomes of tax expenditures are difficult to predict, or to measure after the event. Often the data do not exist to make an evaluation. It is hard to know if a tax expenditure has reached a target group. It also cannot be known whether it has changed behaviour – for example, increasing saving for retirement – or has simply been a windfall to people who were going to save anyway.

There is rarely any evaluation of whether a tax expenditure is the best way to achieve an outcome. If the Government's policy is to increase the amount of educational services people consume, measures targeted to individuals and groups who are seen as under-consuming education might be preferable to a universal GST exemption.

There is simply less scrutiny of tax expenditures.

Simplicity

It is sometimes said that provision of benefits by way of tax expenditures is more efficient because the taxpayer keeps the funds rather than paying them through the tax system and then getting them back as program funds. But in fact tax deductions, rebates and so on make the tax system more complicated.

Richard Krever, in a Sydney Law Review article, argues that tax expenditures invite abuse and restructuring of income to take advantage of them. This in turn stimulates anti-avoidance measures and further gaming of the new rules.

Sustainability

Another issue is that most direct expenditures have a defined budget whereas tax expenditures are open-ended. Superannuation concessions are a particular concern in this regard.

How might things be changed?

In 1996, the Government's Commission of Audit recommended a comprehensive review of such expenditures, with consideration given to converting those that were found to be useful to outlay programs. No review was undertaken then, but it could be now.

If a full review is not possible, a sunset date could be decided for each category of expenditure, with a review to be undertaken at a specified time.

Alternatively, existing deductions could be converted to rebates, perhaps with maximum allowable claims, so that those on low incomes benefit equally and expenditure is better controlled. For transparency, the Australian Tax Office or Treasury could publish more analysis of statistics that are collected on who benefits and by how much from the major categories of tax expenditure.

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Sustainable funding of health care: challenges ahead

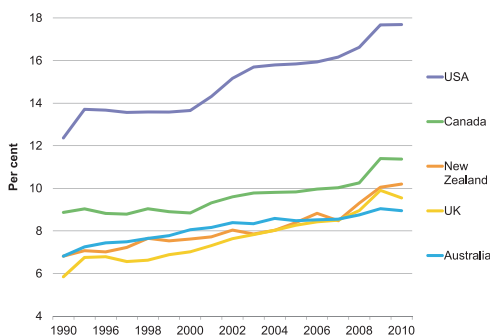
Amanda Biggs, Social Policy

KEY ISSUE

A number of reports highlight the growing burden on governments to fund health care services. This is being driven by population ageing, expensive medical interventions, community expectations and the rise in the incidence of chronic diseases. While Australia has a good health system by international standards, rising health costs represent an obstacle to future reform.

It is widely recognised that despite some failings, Australia has a good health system. Life expectancy of 81.5 years is among the highest in the world, while expenditure on health services (totalling \$130 billion in 2010–11) as a percentage of GDP (around 9%), is below the average for comparable countries (see Figure 1).

Figure 1: Health expenditure, 1990 to 2010



Source: OECD

In its favour, Australia is a relatively wealthy country, with well-developed public health programs (such as immunisation) and good infrastructure (water supply, food quality). There are numerous other positive components of the Australian system – world class medical researchers, low smoking rates, a population

that is generally accepting of health promoting regulations, such as seat belts and random breath testing, and the existence of political leadership and bipartisanship on big health issues, such as HIV-AIDS.

Still, it is recognised that the Australian health system has room to improve, particularly with regards to Indigenous health, quality of care and affordable and timely access to services.

Some challenges in health care

In addition, new health challenges are emerging: the baby boomers are ageing – the number of people over 85 years old will increase from 0.4 million now to 1.8 million in 2050. Risk factors for chronic diseases like diabetes are increasing – many people are overweight or obese and do not get enough exercise. Meeting community expectations of ever higher health standards is also a challenge. While medical research is providing better drugs, devices and interventions to keep people healthier and living longer, subsidising these is increasingly expensive.

There are concerns therefore that the level of funding for health care will soon become a significant burden for governments.

Treasury's Intergenerational Report 2010 (IGR) estimated that spending on health care by government as a percentage of GDP will nearly double by 2050. A recent report from the Committee for Economic Development of Australia (CEDA) warned that current health funding arrangements are not sustainable; new models will need to be considered. Independent think tank the Grattan Institute has also expressed concern over the future sustainability of health funding.

The universal Medicare rebate, high levels of bulk billing (where consumers pay nothing) and free public hospital care means that there are limited price signals which can act directly to moderate demand for subsidised health services. Similarly, fee-for-service payments to doctors encourage them to provide more services, which in turn increases the use of services.

Out-of-pocket spending on health care by consumers is also growing, but much of this is for non-subsidised health care, such as over the counter medicines, or areas with limited subsidies, such as dental services and those provided to private patients. Hence, it has limited impact on government spending (for further information see the brief 'Out-of-pocket payments for health care – finding a way forward').

How much a country spends on health reflects its social priorities, as well as its capacity to pay. While richer countries tend to spend more on health services, there is variability in the amounts each spends. For example, Japan is one of the few countries where people live longer and have healthier life expectancy than Australia, but Japan spends less per capita on health than Australia.

The IGR predicts that Australian GDP per person will grow by 1.5% per year. Whether this will be enough to sustain an expanded health system and meet the health costs of the future remains an issue for debate.

Some argue that a dramatic shift in thinking about how health care is funded is required if government finances are not to be overwhelmed by increased demand for health services.

Prospects for further reform

In recent years, a number of reform options have been discussed, examined and implemented. The National Health and Hospitals Reform Commission (NHHRC) established by the Rudd Government recommended a number of reforms, around hospitals, prevention and primary care. Some of these, such as the establishment of Medicare Locals have been implemented, and it appears they have widespread support.

But health reform is not always easy. Both the Pharmaceutical Benefits Scheme and Medicare, which now have bipartisan support, faced considerable opposition when they were first introduced, and this persisted for some time.

A major dilemma for government is developing effective approaches while maintaining widespread support for reforms. There are a number of obstacles to achieving these

aims: political lobbying from vested interest groups for example is a problem, as a recent proposal to introduce a star food labelling system illustrates. While the labelling system has the potential to help address obesity, it is facing industry opposition, despite widespread support among health groups.

Former chair of the Council of Australian Governments (COAG), Paul McClintock, warned that a lack of clarity between levels of government over responsibilities also hampers reform. Writing in the Australian Financial Review McClintock expressed frustration with the political processes surrounding COAG meetings and the ways in which these derail proposed health reforms.

Recent controversy over hospital funding arrangements in Victoria illustrates how the issue of health care funding remains subject to bitter disputes between governments. Although a new hospital funding formula has been agreed in that state, it remains to be seen if the new plan can operate without recourse to the frequent disputes which characterised previous arrangements.

These examples suggest that future reform efforts may face considerable obstacles. Yet unless political machinations are set aside, and vested interests overcome, genuine long-term reform of health funding may remain an elusive goal.

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The sustainability of retirement incomes policies

Carol Ey, Social Policy

KEY ISSUE

Retirement incomes policy has been a major focus of governments over the last 30 years. There have been significant changes to the system, but it is unclear whether these have reduced the long-term costs of an ageing population.

Concern about the ageing of the Australian population and the potential impact this may have on federal budgets was first raised in the late 1970s. This concern in part led to the introduction of compulsory superannuation contributions for employees.

The first Intergenerational Report (IGR) in 2002 attempted to quantify the likely impact of demographic change and estimated that expenditure on age and service pensions would increase from 2.9% of GDP in 2001–02 to 4.6% in 2041–42 (for further information see Intergenerational reports – key influences on policy? elsewhere in this publication).

In response, governments have introduced a range of measures to encourage personal investment in superannuation and increased the ages at which superannuation and the Age Pension can be accessed.

Age Pension

In 1909 Australia was one of the first countries to introduce an age pension. The Pension was designed as a 'safety net', which entailed means testing to ensure it was targeted at those most in need. It has remained largely a payment targeted at those with few other resources. Today, a full Age Pension is available to a couple with an annual income of less than about \$7,000 and assets outside the family home of less than \$279,000.

However, because the means test is tapered – that is, income or assets above these limits reduce the amount of pension payable, rather than excluding payment entirely – those on relatively high incomes and with considerable

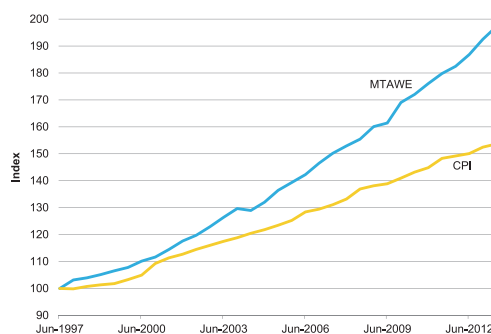
assets may still receive a part Pension. For example, the cut-off rate beyond which a couple would receive no Pension is an income over \$70,500 and assets of over \$1 million in addition to the family home.

Around 50% of Australians over Age Pension age receive a full Age Pension, and a further 30% receive a part Pension, at a total cost to the budget of over \$39 billion in 2013–14.

Indexation

Prior to 1997, the Age Pension rate (and rates for other income support payments) was indexed by the Consumer Price Index (CPI) to ensure pensioners were protected against the impact of rising costs. Since 1997 the Pension has also been benchmarked against Male Total Average Weekly Earnings (MTAWE). This means that where wages rise more quickly than prices, the Pension is increased in line with wage increases, rather than at the CPI rate. Figure 1 shows the difference in these rates over the period since 1997.

Figure 1: MTAWE and CPI, June 1997 to June 2013



Source: Australian Bureau of Statistics

As can be seen from Figure 1, over the period since 2000, wages have risen much faster than prices. This has meant that pensions have increased almost 30% more than they would have otherwise. This increase not only affects the amount of income pensioners receive, through the operation of the taper, it also increases the cut-off levels for receipt of a part Pension.

Superannuation

Government policies encouraging private investment in superannuation appear to have been successful, with around \$1 trillion having been invested in superannuation in the last decade. However, these policies have not been cheap. Tax expenditures associated with the concessional taxation of superannuation cost an estimated \$30 billion in 2011-12, and are projected to rise to \$45 billion in 2015-16 (for further information see Tax expenditures: costs to government that are not in the Budget elsewhere in this publication). The policies have also been criticised for providing significantly greater benefits to high income earners.

This investment does not appear to be achieving the aim of providing sufficient retirement savings to reduce the load on the Age Pension. Superannuation is generally able to be accessed from age 55, and about half of the withdrawals from superannuation are lump sum payments. Some reports, such as a recent study commissioned by CPA Australia, suggest people are accumulating higher amounts of debt in the lead up to retirement in the knowledge that they can use their superannuation savings to repay it.

The result is that some retirees will have used all their superannuation savings by the time they reach Age Pension age. While Treasury modelling suggests the proportion of people receiving the full Pension will decline slightly over future years, this is expected to be almost matched by an increase in part Pension receipt.

Attempts to control costs

There have been some attempts to contain the costs associated with superannuation concessions, such as limiting the annual amount of concessional contributions and moving to increase the taxation of fund earnings for those in pension mode.

In addition, the eligibility age for access to superannuation is being progressively increased from 55 to 60 years. Similarly, eligibility for the Age Pension is being increased from 65 to 67 years. However, these changes will still leave a period of seven years between the age at which superannuation savings can be accessed and Age Pension eligibility.

On the other hand, proposed changes to indexation arrangements for a range of Defence service pensions from their current CPI indexation to the same basis as the Age Pension is indexed, will increase outlays in the future, as indicated in Figure 1.

Options for change

The Henry tax review recommended a number of changes to retirement incomes policy. This included raising the Age Pension eligibility age, which has since been legislated, and aligning the Age Pension and superannuation preservation ages.

As part of addressing current superannuation tax concession inequity, the Henry review recommended changing the tax arrangements for employer contributions so they are taxed at the employee's marginal tax rate, with a flat-rate refundable tax offset. Specifically excluded from the review's terms of reference was the tax exemption of superannuation pension payments for those over 60 years. This had also been criticised on equity grounds.

Others have suggested limiting the withdrawal of lump sums from superannuation accounts to prevent superannuation savings being used to offset high pre-retirement debt levels.

Conclusion

Retirement incomes represent a major expense to government through the payment of pensions and the subsidisation of superannuation, which will increase as the population ages. The current system is not tightly targeted and includes inequities, with the major benefits flowing to high income earners. Changes in retirement income policies typically have long lead times, but potentially large impacts on Australia's long-term fiscal position.

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Australian Public Service—employment and the efficiency dividend

Dr Nicholas Horne, Politics and Public Administration

KEY ISSUE

Australian Public Service (APS) employment and staffing levels are a perennial public administration issue. The efficiency dividend has also been a high-profile issue in recent years.

Staffing reductions

As part of a package of public sector savings measures, the 2013–14 Budget specified a \$148.4 million reduction in APS employment expenditure at the executive levels (EL 1–2 and SES) over 2013–17; media reporting estimated staffing reductions of up to 400 positions. The Budget also estimated total APS-wide staffing reductions in 2013–14 of 1,262 full-time equivalent positions (excluding increases in military and reserve personnel).

Subsequently, in July 2013 the Government announced reductions at the APS executive levels of around 800 staff over 2014–18 as a savings measure further to the introduction of the emissions trading scheme. It is unclear whether these reductions are additional to the reductions specified in the Budget.

For 2013–14, the August 2013 Pre-Election Economic and Fiscal Outlook estimates \$235 million less in General Government Sector (GGS) wages and salaries expenditure than the Budget, and \$771 million less over 2014–16 before a projected increase in 2016–17. However, it is worth noting that for at least the last five years, actual GGS wages and salaries expenditure has increased annually, possibly due to APS staffing growth and annual salary increases.

Employee numbers

According to Australian Public Service Commission (APSC) data, between June 2007 and June 2012 the APS (staff employed under the Public Service Act 1999) experienced

modest growth, rising from 155,424 employees in June 2007 to 168,206 employees in June 2012 – an increase of 12,782 with an average annual growth rate of 1.64%. Over 2007–12, the number of employed persons grew by an annual average of 1.40%.

APSC data also indicates that between 2007 and 2012 ongoing total SES staff numbers increased by 20.71%, whereas ongoing EL 1 and EL 2 staff numbers increased over the same period by 34.28% and 23.56% respectively.

Further according to APSC data, at 31 December 2012 the APS had 165,598 employees. This constituted a small decrease of 2,608 (minus 1.55%) from the 30 June 2012 total.

Enterprise agreements

In 2011 the Government introduced a new employment bargaining framework for APS employees which recommended a nominal expiry date of 30 June 2014 for agency enterprise agreements. The framework also featured recommended common terms and conditions for inclusion in agreements.

The negotiation of new enterprise agreements will be a significant activity within the APS in 2013–14.

The efficiency dividend and outsourcing review

In 2012–13, the efficiency dividend, an annual funding reduction for agencies, was applied at an increased rate of 4.0% (up from a rate of 1.5% in 2011–12). The 2013–14 Budget eased the impost for agencies by reducing the dividend rate to 1.25%.

In its August 2013 Economic Statement the Government announced a 1.0% increase in the efficiency dividend rate to 2.25% per annum over 2014–17; the increase is estimated to result in savings of \$1.8 billion.

There has been some reporting of projected staffing reductions due to the increase, for example, at the Department of Health and Ageing.

The Government also indicated that, if returned, it would task the APSC with reviewing Commonwealth outsourcing arrangements.

Amendments to the Public Service Act 1999

In July 2013, substantial amendments to the Public Service Act 1999 came into effect (passed by the Parliament in February 2013). Changes include new arrangements for the appointment of secretaries, revised APS Values and new APS Employment Principles and extended application of the Code of Conduct in relation to breaches of the Code.

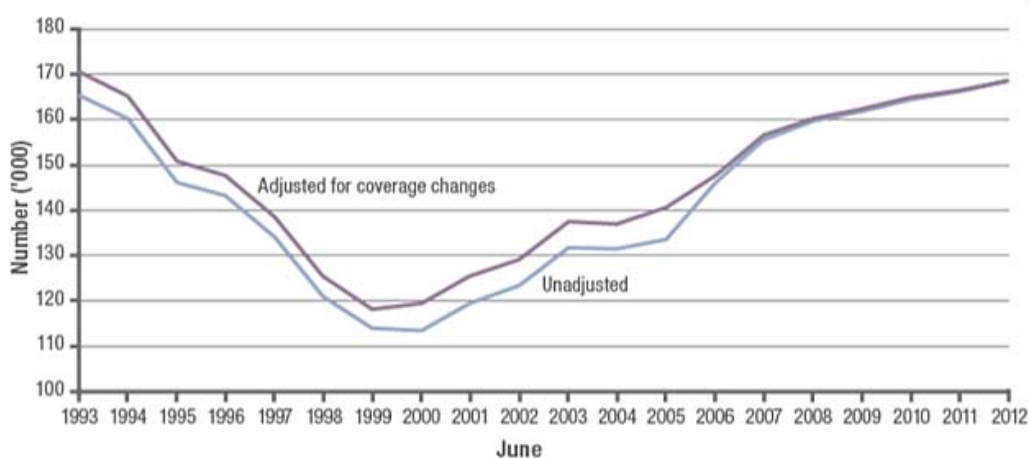
Coalition policies

Since 2010, the Coalition has maintained a policy of reducing APS employee numbers by some 12,000 over two years through natural attrition in order to realise savings.

The Coalition has promised that if it were elected, it will establish a Commission of Audit to review government operations. In addition, under its productivity and regulation policy, a Coalition Government would: require agencies to reduce regulation, with performance targets for departmental secretaries and the remuneration of SES employees would also be linked to regulation reductions. It would also reportedly reintroduce performance bonuses for SES employees.

Following the 2013 election, Prime Minister Tony Abbott has announced additional savings measures and significant Machinery of Government (MoG) changes. The additional savings include the abolition of environmental bodies and the integration of the AusAID into the department of Foreign Affairs and Trade. In reference to the MoG changes, Mr Abbott said that the changes to departmental structure 'will simplify the management of government business, create clear lines of accountability and ensure that departments deliver on the Government's key priorities'.

APS employee numbers 1993–2012



Source: Australian Public Service Commission (APSC), State of the Service Report 2011–12, APSC, Canberra, 2012.

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HEALTH, EDUCATION AND SOCIAL WELFARE

The background features a series of overlapping, semi-transparent geometric shapes in various shades of light blue and teal. These shapes create a dynamic, layered effect, with some areas appearing darker due to the overlap. The overall aesthetic is clean and modern, typical of a corporate or institutional report cover.

Closing the Gap

Dr John Gardiner-Garden, Social Policy

KEY ISSUE

This article looks at the origins, objectives and effectiveness of the Closing the Gap initiative.

What is 'Closing the Gap'?

In his Social Justice Report 2005, Aboriginal and Torres Strait Islander Social Justice Commissioner Tom Calma urged Australian governments to commit to achieving equality for Indigenous people in health and life expectancy within 25 years. Non-government agencies responded to Calma's appeal, developing a National Indigenous Health Equality Campaign in 2006, and launching a Close the Gap campaign in 2007. This rights-based awareness campaign later gave rise to a National Close the Gap Day, which helped inspire cross-government action.

The Council of Australian Governments (COAG) pledged to close key gaps in December 2007, and in March 2008 government and non-government delegates to a National Indigenous Health Equality Summit signed a statement of intent.

In July 2008, the Rudd Government established the National Indigenous Health Equality Council, and in November of that year COAG approved the National Indigenous Reform Agreement which set out six Closing the Gap targets:

- to close the life expectancy gap within a generation
- to halve the gap in mortality rates for Indigenous children under five within a decade
- to ensure access to early childhood education for all Indigenous four year olds in remote communities within five years

- to halve the gap in reading, writing and numeracy achievements for children within a decade
- to halve the gap for Indigenous students in year 12 attainment rates by 2020 and
- to halve the gap in employment outcomes between Indigenous and non-Indigenous Australians within a decade.

To help achieve these goals COAG identified a number of building blocks (early childhood, schooling, health, economic participation, healthy homes, safe communities and governance and leadership). It also facilitated a number of Indigenous-specific National Partnerships, namely:

- National Partnership on Closing the Gap in Indigenous Health Outcomes
- National Partnership on Remote Indigenous Housing
- Closing the Gap: National Partnership Agreement on Indigenous Early Childhood Development
- National Partnership on Indigenous Economic Participation
- National Partnership Agreement on Remote Service Delivery
- Closing the Gap: National Partnership Agreement on Remote Indigenous Public Internet Access
- Closing the Gap in the Northern Territory National Partnership Agreement

What progress has been made?

Three publications track developments in Closing the Gap targets—the Prime Minister's annual report (Closing the Gap: Prime Minister's Report, 2013), the Productivity Commission's biennial report (Overcoming Indigenous Disadvantage: Key Indicators 2011) and the COAG Reform Council's report on progress (Indigenous Reform 2011-12: Comparing Performance Across Australia).

The COAG Reform Council's report indicates that there has been good progress on three targets (child mortality rates, early childhood education, and year 12 or equivalent attainment), but results for the remaining three targets (overall life expectancy, academic achievement and employment outcomes) are less positive.



The Indigenous child death rate is going down and the gap is getting smaller



Australia is close to achieving the early childhood education target



The gap is narrowing in Year 12 or equivalent attainment



There were no significant improvements in Indigenous numeracy



Only the NT is on track to close the gap in death rates by 2031



The employment gap is widening

Source: COAG Reform Council, Indigenous reform 2011–12: comparing performance across Australia

How much is spent on Closing the Gap?

According to the Productivity Commission's 2012 Indigenous expenditure report, total direct Indigenous expenditure was estimated to be \$25.4 billion. This represents 5.6% of total direct government expenditure. Australian Government spending accounted for \$11.5 billion of this expenditure (45% of the total). The estimated expenditure per head of population was \$44,128 for Indigenous Australians, compared with \$19,589 for other Australians.

How effective is this expenditure?

In assessing the progress of COAG's Closing the Gap initiatives, commentators have noted that there are a number of problems. These include: data limitations, agreeing target progress points, measuring achieved trajectories across jurisdictions and the absence of targets in some areas (such as justice). For example, the target of closing the gap in life expectancy cannot be measured in some jurisdictions, it is subject to considerable debate on the methodology that should be used for determining Indigenous life expectancy

and it is not responsive in the short term to interventions. Focussing on death rates is an interim alternative measure, but one still subject to considerable data limitations.

Commentators have also noted the difficulty of following funding lines to assess the efficacy of expenditure. As Jon Altman, professor at the Centre for Aboriginal Economic Policy Research, has observed in 'Black government expenditure—it's a white thing', the Productivity Commission's Indigenous Expenditure Report cannot reveal how much was spent on Closing the Gap – what was spent on service provision and what on administration, how effectively a service was delivered, or how much benefit Indigenous Australians garnered from the estimated expenditure.

Concerns over the efficacy of programs that are meant to be closing the gap featured prominently in the Finance Department's Strategic review of Indigenous expenditure (2010). The report noted:

The Commonwealth's total expenditure on its Indigenous-specific programs amounts to some \$3.5 billion annually. This major investment, maintained over many years, has yielded dismally poor returns to date.

Closing the Gap in the Northern Territory

Not to be confused with the COAG Closing the Gap initiative is 'Closing the Gap in the Northern Territory', which was part of the Howard Government's 2007-initiated Northern Territory Emergency Response (NTER). In November 2009, the Rudd Government introduced legislation to reverse the suspension of the operation of the Racial Discrimination Act 1975, redefine 'Income Management' and address other elements of the NTER, later rebadged as 'Closing the Gap in the Northern Territory'. In 2011, this range of measures was renamed 'Stronger Futures in the Northern Territory'.

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Does income management work?

Dr Luke Buckmaster, Social Policy

KEY ISSUE

Evidence for the success of income management of welfare payments is mixed; while some people report that it has improved their lives, there is little evidence that it is leading to widespread changes in behaviour.

What is income management?

Income management (also known as 'welfare quarantining') refers to a policy under which a percentage of the welfare payments of certain people is set aside to be spent only on 'priority items' such as food, housing, clothing, education and health care. There is an explicit ban on the purchase of certain goods and services including alcohol, tobacco, pornography and gambling.

Income management was introduced by the Howard Government in 2007 as part of the legislation for the Northern Territory Emergency Response. It was later expanded by the Rudd and Gillard Governments.

Income management has been a controversial welfare reform. While conditions have always been applied to eligibility for welfare payments, restrictions on how payments may be spent are a new development, criticised by some as paternalist and stigmatising. Income management is also relatively expensive to administer, with an estimated cost up to 2014–15 in the range of \$1 billion.

Who can be income managed?

Welfare recipients who can be subject to compulsory income management include those in:

- the Northern Territory (NT) who are deemed by the government to be 'Disengaged Youth', 'Long-term Welfare Recipients' or 'Vulnerable Welfare Payment Recipients'
- the NT and parts of Western Australia (WA) who have been referred to Centrelink by a child protection officer to have their

income managed ('Child Protection Income Management')

- Cape York who have been ordered by a Queensland Government statutory body, the Family Responsibilities Commission (FRC), to be income managed for engaging in dysfunctional behaviour
- one of five targeted communities (Bankstown, Greater Shepparton, Playford, Logan and Rockhampton) who have been referred for Child Protection Income Management or the Vulnerable Welfare Payment Recipients measure (known as 'Place Based Income Management') and
- the Anangu Pitjantjatjara Yankunytjatjara Lands (APY Lands) South Australia (SA) or Ngaanyatjarra Lands (NG Lands) and Laverton Shire (WA) who have been referred for Child Protection Income Management or the Vulnerable Welfare Payment Recipients measure.

People in the above locations may also participate in income management voluntarily.

Currently, there are 21,261 people subject to income management across Australia, including 18,632 in the Northern Territory.

Objectives of income management

Evaluating the success of income management requires an understanding of what it is trying to achieve. The stated objectives of income management are to:

- reduce immediate hardship and deprivation by directing welfare payments to priority needs
- help affected welfare payment recipients to budget
- reduce the amount of discretionary income available for alcohol, gambling, tobacco and pornography
- reduce the likelihood that welfare payment recipients will be subject to harassment and abuse in relation to their welfare payments and

- encourage socially responsible behaviour, particularly in the care and education of children.

In addition to these specific objectives, both the previous Coalition and Labor Governments have spoken of the role of income management in terms of broader welfare reform objectives, such as fostering individual responsibility and moving people away from welfare dependence.

Is it working?

A June 2012 Parliamentary Library paper summarised the (limited) available evidence in relation to the operation of income management in the NT, Queensland and WA. The paper found that positive changes had been uneven and fragile. On the other hand, there was little evidence that income management was worsening the situation in areas where it operates.

A March 2013 Australian Government evaluation of the Cape York Welfare Reform Trial found mixed results associated with income management. There was some evidence that income management assists in reducing behaviours that lead to people being reported to the FRC. Further, 78% of income managed people surveyed reported that the scheme had made their lives better. The evaluation found some dissent about income management, 'with common complaints being the inability to use it in some stores and the paternalistic nature of the intervention'. It should be noted that income management in Cape York is part of a broader system involving case conferencing and referral to community support services, meaning that changes in behaviour may not be a result of income management alone.

A July 2013 evaluation of income management in the NT commissioned by the Australian Government also reported mixed findings. This evaluation found:

- some evidence that income management may, to a limited degree, in the short-term, assist some people experiencing adverse outcomes from financial harassment and/or having problems managing their finances

- it is applied in blanket fashion to a large number of people who are able to manage their money and who report that they do not have problems related to alcohol, drugs or gambling and
- considerable feelings of disempowerment and unfairness among those who are compulsorily subject to the scheme.

In relation to longer-term objectives, the evaluation found:

... little evidence to date that income management is resulting in widespread behaviour change, either with respect to building an ability to effectively manage money or in building 'socially responsible behaviour' beyond the direct impact of limiting the amount that can be spent on some items.

Rather, the evaluation suggested that, 'the early indications are that income management operates more as a control or protective mechanism than as an intervention which increases capabilities'.

As the evaluation notes, this raises two important questions for the future of income management in the NT. First, do the gains outweigh the costs? Second, would the situation be improved by a more targeted approach that includes better access to quality services (such as the Cape York approach)?

Further reading

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Department of Social Services (DSS), 'Income Management Evaluations', DSS website.

Out-of-pocket payments for health care—finding a way forward

Roy Harvey, Social Policy

KEY ISSUE

Out-of-pocket payments for health care mean that some low income people do not access needed health care and many experience significant financial difficulties in paying for health services. Changes to health funding arrangements may help to reduce the barriers to better health care for this group, but it appears that more needs to be done.

What are the issues?

In 2009, the National Health and Hospitals Reform Commission noted increasing concerns that a two tiered health system was evolving in Australia; a system under which people who did not have private health insurance faced unacceptable delays in accessing certain services.

Reports have warned that high out-of-pocket costs prevent people with long-term or chronic conditions from seeking health care and place financial strain on low income consumers.

An increasing number of people delay visits to medical practitioners or do not fill prescriptions because of cost considerations.

While bulk-billed services under Medicare provide about 80% of general practitioner, pathology and imaging services 'free', people with chronic conditions often need services that are not funded by Medicare, such as aids and appliances, allied health services, pain relief and massage.

The lack of affordable dental care for low income people, and the negative consequences on dental and general health, has been reported for decades.

Waiting times for significant elective surgery are a continuing problem for public patients, partly as a result of specialists moving to private hospitals. While people with private health insurance can go to private hospitals, they may incur significant out-of-pocket expenses to do so.

How much is spent out of pocket?

In 2010–11, the Australian Institute of Health and Welfare (AIHW) estimated that \$24.3 billion of health spending came directly from the pockets of consumers; an average of \$1,082 per person. Out-of-pocket spending in Australia was about twice as high as in the United Kingdom and New Zealand, but only 75% of out-of-pocket spending in the United States and 55% of that spent by the Swiss.

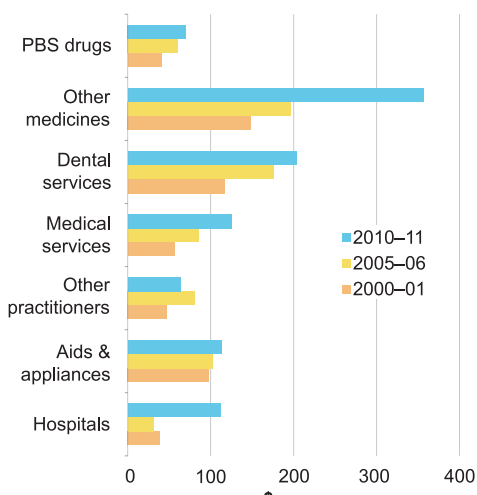
Australian spending in dollar terms is the fifth highest in the Organisation for Economic Co-operation and Development (OECD), but as Australia also has the fifth highest GDP per person in purchasing power parity terms, this level of spending is not unexpected.

The AIHW reported that, in 2010, Australians spent 3.2% of Household Final Consumption Expenditure on out-of-pocket health costs. In ten OECD countries spending was higher, while 12 spent less.

What is the money spent on?

The figure below shows the major components of out-of-pocket expenditure and their growth over the last decade.

Figure 1: Out-of-pocket payments per person, by type of expense, in current prices, selected years



Source: AIHW, Health expenditure: Australia 2010–11

'Other medicines' is the major out-of-pocket expenditure category, with \$8 billion spent in 2010-11; expenditure has increased dramatically over the last decade. Over-the-counter medicines represent more than two thirds of this.

Out-of-pocket spending on dental services in 2010-11 was \$4.6 billion. The National Partnership for adult public dental services reform package has since been introduced and will provide approximately \$750 million a year over six years to improve the dental health of children and low income people. The package will improve access and is likely to reduce costs.

While the level of bulk-billing for medical services has increased, out-of-pocket payments continue to rise, mainly due to increasing specialist fees. In the December quarter 2012, many specialists were charging the privately insured more than twice the Medical Benefits Schedule fee for in-hospital services. Their fees totalled \$254 million: Medicare reimbursed patients \$67 million, private health insurance paid \$47 million and patients paid the gap of \$140 million.

The Extended Medicare Safety Net provides assistance to meet out-of-pocket medical costs, but evidence suggests that most of its benefits go to higher income groups who can afford to pay these costs.

Aids and appliances represent a major cost outlay for people with chronic diseases, but the National Disability Insurance Scheme (NDIS) may improve access and reduce costs over time.

Out-of-pocket payment to access hospital services has seen the largest proportional increase in expenditure. Almost all of the \$2.5 billion spent in 2010-11 was by private patients in private and public hospitals.

Payments for the services of allied health and complementary or alternative health practitioners have fallen in the latter half of the decade. This is possibly as a result of the Chronic Disease Management initiative introduced in 2007. The NDIS may provide greater access to these services for people with chronic conditions.

The Pharmaceutical Benefits Scheme (PBS) Expanded Accelerated Pricing Disclosure (EAPD) policy is expected to result in significant reductions in the price of PBS drugs over the next few years. This will deliver savings to both consumers and the Government.

Conclusion

Improvements are expected from the initiatives described above. Other areas that could be investigated include:

- the use of non-PBS medicines
- using the Extended Medicare Safety Net to better target people in high need
- the private health insurance subsidy for specialist services in hospitals to improve support for privately insured people and to minimise the impact on waiting times for public patients in public hospitals and
- improving access to allied health services through the hospital and primary care networks.

Much of the understanding of the specific needs of disadvantaged groups comes from a relatively small number of surveys and case studies. A systematic study would give a more accurate picture.

Further reading

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Consumer Health Forum, 'Australian healthcare—out of pocket and out of date' Journal of the Consumer Health Forum of Australia, 12, April 2013.

The crisis in the caring workforce

Marilyn Harrington and Dr Rhonda Jolly, Social Policy

KEY ISSUE

Ongoing workforce shortages are inhibiting Australia's ability to meet increasing demands for high quality child care and aged care. They also potentially limit the implementation of the National Disability Insurance Scheme.

According to the Australian Bureau of Statistics, there were some 216,300 workers in residential care services in May 2013, mainly in the aged care sector. There were also 356,500 workers in social assistance, most in child care or disability services. Over 80% of these workers were women, and nearly half were employed part-time. These sectors have struggled to attract and retain workers, due to the relatively low pay rates and lack of secure employment opportunities.

In addition, health professionals continue to be in short supply with a range of occupations appearing on the immigration skilled occupations list. Nurses are in particular demand, with Health Workforce Australia (HWA) estimating that there will be a shortage of over 100,000 nurses by 2025.

These shortages of appropriately skilled workers have an impact on several areas of policy priority.

Early childhood education and care

The early childhood education and care (ECEC) sector is critically short of appropriately qualified staff. United Voice, the union which represents ECEC workers, claims that about 180 educators leave the sector each week because of low wages and poor conditions.

The sector also has many not-for-profit providers operating on small profit margins. Implementation of the National Quality Framework for Early Childhood Education and Care (NQF), with its requirements for a higher qualified workforce from 2014 and lower child-to-carer ratios, will exacerbate this situation.

A number of Australian Government initiatives sought to assist ECEC providers. The most recent, the Early Years Quality Fund (EYQF), will provide \$300 million over two years to long day care centre (LDCC) providers to offset the costs of employing higher qualified staff. EYQF will supplement wage increases by between \$3.00 per hour (for Certificate III qualified staff) to \$5.23 per hour, depending on qualifications. The EYQF initiative includes funding to establish a Pay Equity Unit in the Fair Work Commission (FWC).

An application for an Equal Remuneration Order for LDCC employees (educators) has been lodged with the FWC. According to United Voice, the proposed increase will equate to about \$10.00 an hour for ECEC educators with a Certificate III qualification.

The FWC application signals that the ECEC workforce is not satisfied with the scope and pace of government assistance. Early Childhood Australia (ECA) notes that the EYQF will apply to less than 40% of ECEC educators (preschools and family day care services are excluded). In ECA's view, therefore, the EYQF is an inadequate substitute for a broader wage increase for a low paid workforce.

The Coalition's preference is for the FWC to determine wage increases for the ECEC sector. The EYQF, therefore, will not be extended and the Government has announced a review of its administration. The Productivity Commission, which has already conducted an inquiry into the ECEC workforce, will also be commissioned to conduct an inquiry into the child care system more broadly.

Aged care

In 2010, the then Department of Health and Ageing estimated that the aged care workforce would need to increase between two and three times before 2050 in order to provide care to the growing number of aged care residents. Other challenges include that the aged care workforce itself is ageing, the overall labour market will be more competitive as a result of the ageing of the population and the sector already faces difficulties in attracting and retaining workers.

A Workforce Compact, introduced as part of the 2012–13 Budget, was to provide an employer who met certain conditions, including raising wages to the rate specified, to qualify for access to government-provided workforce supplement payments. The Government has subsequently dismantled this policy. The former Government considered that the Compact would help retain current workers, who are amongst the lowest paid in Australia, and encourage new growth in the industry, but the Government believed that providers would not sign the Compact, as the funding provided fell short of paying for the wage increase.

While union groups, such as United Voice, welcomed the Compact, providers, such as Aged and Community Services Australia and Catholic Health, agree with the Government's position.

Disability care

The introduction of the National Disability Insurance Scheme (NDIS) will involve a substantial expansion of the disability services sector, leading to increased demand for disability support workers. In proposing the introduction of the NDIS, the Productivity Commission suggested:

The capacity to provide expanded services will depend on attracting new employees and enabling workers in the system to work longer or more flexible hours if they want to.

The shortage of allied health professionals, particularly in regional areas, also has the capacity to have an impact on the ability to deliver the NDIS.

Health workforce

Advocates of new thinking about the Australian health system have argued that traditional models of patient care cannot cope with the demands of the future. Serious changes have been recommended to tackle problems associated with access and equity, to embed ideas such as prevention and early intervention and to strengthen patient engagement. A number of reports have pointed out that new models of care are unlikely to work if they are underpinned by old models of health professional training. In addition, new models cannot work if existing health workforces are unwilling to adapt, and while various

components do not cooperate and collaborate to work more effectively within teams. Finally, health workforce analysis has concluded that realigning workforce structures must be an essential element of a new health workforce model that needs to include new types of workers and revised roles for existing workers.

Health Workforce Australia (HWA) was created by the Council of Australian Governments in 2009 to attempt to deal with these issues. HWA's research has confirmed that there are many barriers to health workforce change, despite evidence that innovation has the potential to improve health outcomes.

So far, however, HWA has found the task of promoting innovative structural change difficult, and sometimes daunting. Nevertheless, it has the potential to play a significant role in encouraging and coordinating the revision of old – and the emergence of new – workforce roles. This could improve productivity and support more effective, efficient and accessible health service delivery.

Conclusion

Strategies to address the growing shortage of workers in the child care, aged care and disability support sectors are likely to involve either reducing quality standards or increasing costs, if not both.

Addressing the shortages in the professional health occupations is potentially more challenging, as it appears to require a rethinking of the current training and workforce structures and overcoming the entrenched positions of key interest groups.

Further reading

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M Harrington, 'National quality framework for early childhood education and care', FlagPost weblog, 19 December 2011.

Improving school performance

Marilyn Harrington, Social Policy

KEY ISSUE

More funding, improving teacher quality, greater school autonomy and national testing and reporting are strategies that governments are using to improve school performance.

The achievement of Australian school students

Evidence of declining literacy and numeracy achievements of Australian school students is a major driver of the policy imperative to improve the performance of schools.

An Australian Council for Educational Research report shows an overall decline in the reading and mathematics levels of 15-year-olds since 2000. The growth in the impact of socioeconomic background on student performance is also a major concern, with disadvantaged students more likely to underperform. Further, the period since 2000 has seen Australia surpassed by other countries in international surveys of student attainment.

These developments have occurred at the same time as expenditure on school education has grown significantly and a raft of education reforms and initiatives has been introduced by Australian governments.

More funding, improving teacher quality, greater school autonomy and national testing and reporting are among the suite of reforms that governments have introduced to improve school and student performance. While there is evidence to support these strategies, there is also research that questions their efficacy.

School funding

According to a 2013 Grattan Institute analysis, school education expenditure by all governments grew by 37% (\$11.3 billion) in real terms from 2002–03 to 2012–13. Commonwealth budget data show a similar trend — total Australian

Government expenditure on Australian schools grew by an estimated 58% in real terms over the same period.

Nevertheless, the Review of Funding for Schooling (the Gonski Review) considered that a significant increase in funding by all governments was required to lift the performance of school students, particularly those from disadvantaged backgrounds.

The additional funding for schooling subsequently negotiated through the National Education Reform Agreement (the NERA) will take effect from 2014. Had the NERA been implemented in full (Queensland, Western Australia and the Northern Territory have not signed), there would have been about \$15 billion in additional funding (two-thirds provided by the Australian Government) phased in over a six-year period. The Coalition Government has committed to the same level of funding that is currently in the Commonwealth Budget's four-year forward estimates period. Whether it will commit to the full quantum of the NERA funding is uncertain.

Improving the quality of teaching

Strategies to improve the quality of teaching are paramount in the school reform agenda. This is not surprising given the widespread consensus, supported by extensive research, that quality of teaching has the most impact on student attainment.

Governments in Australia and overseas are pursuing similar strategies to improve the quality of teaching. These strategies include: raising the standard of entrants to the teaching profession, improving and raising the level of teacher education courses, mentoring beginning teachers, national professional standards for teachers and professional development and performance rewards. There are also programs to attract high-performing graduates and other skilled and experienced professionals to the profession and to attract teachers to work in particular schools.

This focus on improving the quality of teaching,

however, is causing some concern about adverse effects on the teaching profession and pedagogy. Australian teaching professor, Stephen Dinham, has warned that solutions promulgated by those 'who are out of touch with teaching' are creating 'panic' and reinforcing 'misconceptions', while providing 'little guidance or positive substance for the profession'.

School autonomy

School autonomy gives school principals greater control over budgets, staffing and school curricula, but it is contentious.

Victoria has long had a devolved school administration model. Western Australia (WA) and Queensland are also now moving towards greater school autonomy with their independent public schools. The Coalition Government is committed to extending this model nationally.

However, evidence about the benefits of school autonomy is mixed. In his 1997 examination of Victorian schools, Stephen Lamb found that devolution entrenched disadvantage for schools in low socioeconomic areas. The Melbourne Graduate School of Education also discounts increased school autonomy as an effective strategy for improving student outcomes. These findings are supported by a substantial body of international research.

In *The Myth of Markets in School Education*, Ben Jensen warns that autonomy requires quality leadership. He considers that school leaders are 'too often' given autonomy but 'lack the direction, support and development to lead ... key reforms'.

The initial evaluation of the WA independent schools model is positive. It reports that principals consider the initiative is enhancing school functioning and 'resource efficiency'. Nevertheless, there are concerns about increased workloads and administrative burdens under the model. It is premature, however, to consider whether student outcomes are improving as a result of increased school autonomy in WA.

National testing and reporting

The National Assessment Program – Literacy and Numeracy (NAPLAN) annual assessments are presented as an important

means of ascertaining student progress and the effectiveness of teaching strategies, identifying student needs and reporting student progress. The My School website, which includes NAPLAN results, was developed as a means of providing greater transparency and accountability for school performance.

However, NAPLAN testing and My School have generated much concern about the uses to which NAPLAN data is put, and the negative effects on students and schools. There is Australian and international evidence that shows standardised testing and 'league' tables can present a narrow view of school performance. They are also open to misinterpretation, can distort pedagogical practice and can adversely affect student wellbeing.

Evidence presented to two Senate committee inquiries into NAPLAN in 2010 and 2013 bears out these findings, as does research by Greg Thompson from Murdoch University. There are also concerns about NAPLAN data being used to determine the Schooling Resource Standard, which is the basis of the new funding system for schools.

The future

It appears that if school performance is to be improved, then the right mix of reform strategies must be found.

Clues to what this mix might look like are provided by Finnish educator, Pasi Stahlberg, who warns against over-emphasising competition, standardisation, school choice and test-based accountability. Rather, he stresses the importance of 'collaboration, individualised teaching, equity and... a trust-based, well-educated [teaching] profession'.

Stahlberg also highlights, as did the Gonski Review, that it is the equity of education systems that is of critical importance to school improvement.

Further reading

M Harrington, *Funding the National Plan for School Improvement: an explanation*, Background note, Parliamentary Library, Canberra, 26 June 2013.

Higher education: sustainability of a demand-driven system

Dr Coral Dow, Social Policy

KEY ISSUE

The Labor Government implemented major reforms to higher education through a student demand-driven system and associated funding reforms. The reforms resulted in increased uptake of Commonwealth-supported places and increased Commonwealth expenditure. The 44th Parliament will be faced with decisions regarding the sustainability of the system.

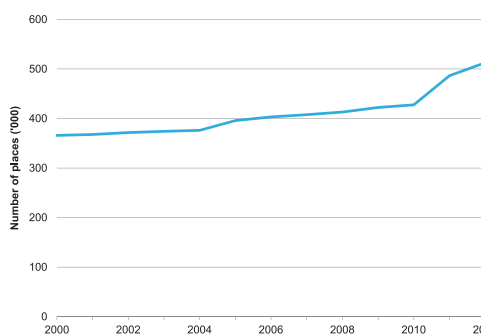
The student demand driven system: enrolment growth

In response to the 2008 Review of Australia's higher education system, chaired by Denise Bradley, the Labor Government implemented major reforms to higher education.

The major reform was to 'uncap' the allocation of university places through a demand-driven system for domestic students. Other reforms included a revised indexation rate of university funding, increased funding aimed at improving the participation rate of low Socio Economic Status (SES) students and increasing the eligibility to student income support.

The partial uncapping of places in 2010, and the full deregulation in 2012, resulted in a strong take up of university places (see Figure 1) and revised budget forward estimates of the numbers of places. In 2009, estimates of 458,000 undergraduate places for 2012 were increased to 512,600; this is estimated to grow to 589,000 places in 2016.

Figure 1: Undergraduate university places, 2000 to 2012



Source: Portfolio Budget Statements.

Analysis by the Grattan Institute shows most additional demand has been in the disciplines of health, science and engineering.

This appears to indicate that the Labor Government's target for 40% of 25 to 34 year olds to hold a degree by the year 2025 will be met. In 2012 the proportion of this age group with a degree was 37%, partly due to the intake of skilled migrants.

The Labor Government's other target, which was that by 2020, people from low SES backgrounds represent 20% of higher education enrolments, might also be met. In 2012, low SES commencing students increased by 9.1% compared to 2011. However, as a share of students the increase is slower: from 16.6% in 2011 to 16.9% in 2012.

The student demand driven system: expenditure growth

Increased uptake has been accompanied by an increase in expenditure from the Commonwealth Grants Scheme (CGS), the primary source of funding for places. In 2009-10 CGS spending was \$4.56 billion and is estimated to increase to \$7.19 billion in 2016-17. Such growth has raised concerns about the sustainability of the uncapped system in a period of budget restraints.

Demand may level off as the initial uptake from years of unmet demand falls, and demographic factors may also contribute. However, economic factors, such as the decline in the mining boom, are likely to increase demand. This is because potential students who have declined university places in preference to high-paid employment may return to higher education.

There is widespread support from stakeholders for the uncapped system, but a number of options have been proposed to contain the costs or to slow demand. The Labor Government announced cuts to higher education in April 2013. The proposed cuts were not legislated before the 43rd Parliament was dissolved, but remain in the budget forecast.

Some of the proposed savings were not direct cuts to the sector but a shifting of the burden to students through the removal of a 10% up-front payment Higher Education Loan Program (HELP) discount and the conversion of youth allowance start-up scholarships to HELP loans.

Student contributions

A more direct cost shift would be an increase to the student contribution.

Student places are funded by a combined Commonwealth government contribution and a student contribution. The student contribution varies across a range of broad disciplines and can be deferred as a HELP loan. Increasing the student contribution while maintaining the Government contribution will not reduce Government expenditure, but it would increase the overall amount for each place and avoid a direct cut to the sector.

Government savings could be made by increasing student contributions and also decreasing government contributions: the funding per place to providers stays the same, but the cost is met by students.

Student contribution amounts are set by the Government, but some universities have argued for partial deregulation of student fees. In a submission to the Base Funding Review, the University of Melbourne recommended, for example, that 'higher education providers be permitted to set maximum student fees of up to 30% more than the base funding rates'.

Full deregulation of fees would see the return of the Howard Government's policy allowing universities to enrol full fee-paying domestic students and generate income for high demand universities and courses. Such a policy would require modification of the demand-driven system – capping certain places or courses and allowing the unmet demand to be filled by full-fee places.

Students are able to defer payments of their student contributions (including full-fee places) through HELP. Any decision to increase student contributions will need to consider the increased HELP debt and an increase in debt considered unlikely to be repaid, which at present is 17% of HELP debt.

In the 2013-14 Budget, the Government estimated the total HELP debt at \$26.2 billion in 2013-14 and that it would grow to \$42.1 billion by 2016-17.

Any increase in student contributions may have the effect of slowing demand. Since loans were introduced in 1989 analysis has shown that in general, they do not deter students. However, some studies have concluded that increases deter some groups of students, such as low SES and regional students, those that the uncapped system is in fact trying to attract.

The 44th Parliament will need to weigh up the advantages, both to the individual and to society, when judging the appropriate levels of growth and investment in the higher education sector.

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A Norton, Keep the caps off! Student access and choice in higher education, Grattan Institute, Melbourne, 2013.

Adequacy of income support payments

Michael Klapdor, Social Policy

KEY ISSUE

Debate over welfare policy in the 43rd Parliament was dominated by concern as to whether allowance payments were adequate to support recipients with basic living expenses and with their search for paid work. Little has been done to address this concern and the issue will remain contentious.

There is now widespread agreement that allowance payments are too low. Allowance payments are the main form of income support for the unemployed, students and those with temporary illnesses or disability that prevent them from working. A 2012 Senate committee inquiry into the adequacy of allowances heard from a broad range of interest groups, the overwhelming majority of which expressed the view that the current rate of payment was inadequate and impeded income support recipients' ability to meet their basic costs of living. While the committee examined all allowances, its main focus was on Newstart Allowance (NSA), which has the most recipients.

A matter of particular concern to the committee is the large number of long-term NSA recipients and the possibility that the low payment is actually hindering their efforts at finding paid work.

Australia's income support system

Providing for a minimum acceptable standard of living is the main purpose of Australia's income support system. The system is made up of two main payment types: allowances and pensions. These are paid at different rates: a higher rate for pensions and a lower rate for allowances. Pensions are primarily paid to the aged, people with disability and carers. Pensions for single parents with young children are paid at a lower rate than other pensions. Allowances are primarily paid to those of working age who are expected to be looking for paid work or undertaking training and education to improve their employment prospects.

All payments are targeted at those who do not have the means to support themselves, and are subject to income and assets tests. Additional assistance is available to families (through family assistance and child care payments) and to those renting privately (through rent assistance). Various supplements, lump-sum payments and concessions are also available.

What is the problem with current rates?

The current basic rate of NSA (the main unemployment payment) for a single person with no children is \$501 per fortnight; around \$36 per day. This amount has been criticised on the basis that, as it does not allow recipients to meet their basic needs, it undermines the main purpose of the income support system.

The Henry Review of Australia's Future Tax System examined levels of assistance offered by the income support system and found that a number of factors need to be considered in setting payment rates. These include: community standards, expected duration of payment, incentives to work and the overall coherence of the system. When the current allowance rates are assessed on the basis of these factors, they are found wanting:

- The Senate committee's findings, a range of poverty and deprivation studies, and concerns expressed by charities, welfare organisations and business groups indicate that it no longer meets community standards.
- Allowances are intended to be short-term assistance while a recipient finds work, but most recipients are long-term: of the 704,005 people receiving NSA in July 2013, 65% (454,506) had been on the payment for 12 months or more.
- The rate is low enough to offer an incentive to find paid work but, as the Business Council of Australia has stated, it is so low that it is likely to prove a barrier to gaining employment. Too little assistance can make it difficult for job-seekers to maintain their readiness to work, to present themselves

well, to be able to access transport and to afford to live in areas where there are employment opportunities.

- The low rate creates a perverse incentive for those who are out of work to try to access higher rate pension payments. This reduces work incentives and the overall coherence of the income support system as well as driving up expenditure.

Why are pensions higher than allowances?

The maximum basic rate for a single person receiving the Disability Support Pension is currently \$751.70 per fortnight; \$250 more than the single NSA rate. The main rationale for this difference is the work incentive factor: allowance recipients are expected to look for and take up any available job so payments should be low enough to ensure taking up paid work will leave them better off. As pensioners are not expected to work for a significant amount of time, if at all, this type of incentive is irrelevant. While this rationale justifies a difference in payment rates, it does not necessarily justify the extent of the difference or the growing gap between the payments.

Changes to indexation arrangements introduced in 1997 have resulted in pensions increasing in line with movements in either prices or wages while allowances have increased in line with prices (as measured by the Consumer Price Index—the CPI). Since these changes, growth in wages has significantly outstripped price increases leading to the large and growing gap between the rates of pensions and allowances. In 1997, NSA recipients received 92% of what was paid to pensioners. Now they receive 67%. If this trend continues, by 2040, allowance recipients will be receiving around 40% of a pension payment.

Options for reform

The obvious solution would be to increase allowance rates. The Henry Review recommended increasing the single allowance rate by around \$50 a week. This recommendation was primarily intended to improve the relativity between the single and couple rate. The single allowance rate is worth

around 55% of the combined couple rate, while for pensions this ratio is closer to 66%. The Senate committee heard evidence that increasing the single allowance rate by \$50 per week and changing the indexation method so that it is the same as pensions, would cost \$2 billion a year.

Measures introduced in 2013 included a lump sum ‘income support bonus’ payment for allowance and Parenting Payment recipients (equivalent to around \$4 a week for singles) and making the income test for NSA more generous. The measures are improvements but they do little to address the underlying issue of adequacy.

Measures to improve employment outcomes and to assist long-term and disadvantaged allowance recipients to move into the workforce could reduce the overall numbers receiving these payments. However, such measures could take time to produce results and effective policies would require significant investment.

A ripe area for reform is Rent Assistance (RA). Housing costs dominate the budgets of those reliant on welfare, but current rates of RA are not matched to these costs and are poorly targeted. Proposals for reform include the Henry Review recommendations to increase RA and index it to rents, rather than to the CPI. Improving the effectiveness of RA would be a significant step towards improving the adequacy of the income support system as a whole.

There are grounds for more widespread reform of the welfare system, in terms of reducing payment complexity, ensuring settings such as means tests and indexation are consistently applied, and addressing the way income support and other payments interact. A system-wide approach to reform may better allow issues such as the adequacy of payments to be addressed while maintaining work incentives and the system’s responsiveness to the diverse needs of those reliant on income support.

Further reading

M Klapdor, *Social Security and Other Legislation Amendment (Income Support Bonus) Bill 2012*, Bills digest, 58, 2012–13, Parliamentary Library, Canberra, 2013.

Reforming Australia's aged care system: are we there yet?

Leah Ferris, Social Policy

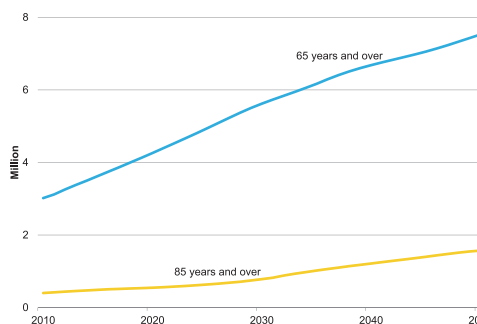
KEY ISSUE

The Parliament recently passed legislation that gives effect to the Gillard Government's Living Longer Living Better reforms. While these reforms will result in significant changes to the current aged care system, discussion has already commenced about the possibility of more reform.

A sector in need of reform

Australians are living longer – due largely to improvements in health care – and as the large cohort of baby boomers ages, the number of older Australians will grow. As Figure 1 illustrates, it is predicted that the number of Australians aged over 85 years will increase from 0.4 million today to 1.8 million in 2050. Significantly, by 2050 an estimated 3.5 million Australians are expected to access aged care services, such as residential aged care, each year. Older Australians are also seeking greater diversity in terms of the range and quality of services available to them.

Figure 1: Population projections (series B), 2010 to 2050



Source: ABS, Population projections, Australia, 2006 to 2101, Cat. No. 3222.0.

Since 1983, the aged care sector has undergone two significant periods of reform. While reforms have resulted in more varied and better quality services, they have delivered little structural change. A third era of reform commenced with

the passage of the Living Longer Living Better legislation package.

Productivity Commission inquiry

In its final report, the National Health and Hospitals Reform Commission (NHHRC) recommended that current arrangements for the provision and financing of aged care services were reviewed. In 2010, the Rudd Government announced that the Productivity Commission (PC) would conduct an inquiry into the options for structural reform of aged care. Following a lengthy public consultation process, including the release of a draft report, the PC reported to the Government in June 2011.

The PC concluded that as the current system suffered from a number of key weaknesses, it needed to undergo comprehensive reform. The PC highlighted a number of issues: challenges faced by consumers in navigating the current system, the lack of integration between the aged care and health system and the need to reform financing arrangements.

The PC made a number of recommendations, including that costs associated with accommodation and care should be separated, and that consumers should have to contribute in part to the cost of their care (safety nets should be in place to protect those of limited means). In addition, consumers should be able to choose to pay either a periodic charge or a bond for residential care, there should no longer be a distinction between high and low care and the restrictions on the number of residential aged care places and care packages should be removed.

Living Longer Living Better reforms

In response to the PC report, the Gillard Government announced the Living Longer Living Better reforms (the LLLB package).

The LLLB package, while adopting a number of the recommendations made by the PC, does not structurally reform the financing of aged care, nor does it lift current restrictions on the supply and allocation of aged care

places. In particular, the reforms do not provide for the level of co-contribution from recipients as envisaged by the PC. The PC's recommendation to establish an entitlement-based system, where consumers choose which care they need, has also yet to be implemented.

Under the LLLB package:

- the costs of accommodation and care will be separated
- older Australians who can afford to do so will pay towards the cost of care with lifetime caps on out-of-pocket expenditure
- accommodation payments for all people in residential aged care facilities will be introduced
- there will be a greater focus on consumer directed care and
- a 'Gateway' will be introduced to help older Australians navigate the aged care system (this will entail a single entry point comprising a new website and a national call centre).

The LLLB package has been structured as a ten year reform program.

The initial response to the package from stakeholders was largely positive. But as aged care providers and others have had longer to reflect, claims have emerged that, as a result of the package, the cost of care provided in the home will increase for elderly Australians.

Despite the package, debate about whether the family home should be included in the arrangements for paying for aged care also persists. While the PC recommended using the value of the family home to finance the cost of aged care, other proposals have suggested including the family home in means-testing calculations of eligibility for public funding.

Where to next?

As part of implementing the LLLB package, the Gillard Government legislated to undertake an independent review of the reforms. Under the legislation, the report of the review, to be provided by 1 July 2017, must consider: whether 'the number and mix of places for residential and home care should continue to

be controlled' and whether 'further steps could be taken to change key aged care services from a supply driven model to a consumer driven model'.

In the lead up to the 2013 election, the Coalition indicated that while it generally supported the LLLB package, more needed to be done to cut aged care red tape. It also committed to work with stakeholders to develop a 'Healthy Life, Better Ageing Agreement', which would 'define reform implementation priorities over a five year period'. As part of this process, it would establish a Steering Committee comprising relevant stakeholders.

It would appear that given the legislative commitment to a review of the LLLB package and proposals for future stakeholder consultation in one form or another, further reforms to the aged care system may be likely to occur. Areas of particular interest for stakeholders may be the current restrictions on residential and home care places and existing financial arrangements. Other issues for consideration may include the level of accommodation payments, the adequacy of safety net arrangements and the ongoing debate over the status of the family home.

Further reading

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R de Boer, 'Paying for aged care—should the family home be counted?', *FlagPost* weblog, 2 May 2012.

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Building the National Disability Insurance Scheme

Dr Luke Buckmaster, Social Policy

KEY ISSUE

The National Disability Insurance Scheme (NDIS) has raised expectations of a transformation in the provision of support to people with disability, but there are substantial challenges associated with implementing the scheme.

Origins of the NDIS

The NDIS (also known as DisabilityCare Australia), a new scheme for providing support for people with disability, has commenced in locations across Australia. The launch of the scheme is the culmination of years of advocacy from the disability and carers sectors. It builds on work undertaken through the National Disability Strategy, the Productivity Commission (PC), Council of Australian Governments and agreements reached between the Commonwealth and state and territory governments.

The NDIS is intended to replace the current system of shared provision and funding of disability services by the Commonwealth and state and territory governments under the National Disability Agreement (NDA). Under the NDA, broadly speaking, the Commonwealth has responsibility for administering disability employment services, while the states and territories administer services such as accommodation support, community support and community access services for people with disability.

In 2011, a PC report on long-term care and support for people with disability found that the current disability support system is 'underfunded, unfair, fragmented and inefficient. It gives people with a disability little choice, no certainty of access to appropriate supports and little scope to participate in the community'.

The PC recommended that the current system should be replaced by a new disability care and support scheme, the NDIS. The Gillard Government announced that it would 'start

work immediately with states and territories on measures that [would] build the foundations for a National Disability Insurance Scheme'.

What is the NDIS?

The NDIS is a major and highly complex reform to the way in which disability support is funded, accessed and provided. It is jointly governed and funded by the Commonwealth and participating state and territory governments.

The main component of the NDIS is individualised, long-term funding to provide support for people aged under 65 years (and then until they enter aged care) with permanent and significant disability or eligible for early intervention support. Participants will meet with the NDIS Agency to identify a set of supports agreed as 'reasonable and necessary' to meet their goals. Participants will be provided with funding for these supports and will have choice over how their needs are met (including choice of provider). When the NDIS is fully implemented it is expected that around 460,000 Australians will receive support under this component of the scheme.

The NDIS also has a broader role in providing information, coordination, referral and funding to assist people with disability (including those not eligible to participate in the main component of the scheme).

What is the NDIS launch?

The scheme is being introduced in stages from 1 July 2013, commencing with a pilot phase known as the NDIS launch. This encompasses:

- South Australia (SA), where support will be provided to children aged up to 14 years
- Tasmania, where support will be provided to young people aged 15–24 years
- the Hunter region of New South Wales (NSW), where support will be provided to people aged up to 65 years and
- the Barwon region of Victoria, where support will be provided to people aged up to 65 years.

From 1 July 2014, the launch will commence in:

- the Australian Capital Territory (ACT) (participants aged up to 65 years)
- the Barkly region of the Northern Territory (NT) (participants aged up to 65 years) and
- the Perth Hills area of Western Australia (WA) (participants aged up to 65 years).

Concurrent with the NDIS launch, the Commonwealth and Western Australian Governments will jointly fund two sites that will operate under the WA My Way model, in the Lower South West and in Cockburn-Kwinana (participants aged up to 65 years).

There is no launch site in Queensland (though the full scheme will be introduced there from 2016).

Full introduction of the NDIS

Agreements have been reached for full coverage of the NDIS to commence in all states and territories except WA. The timetable according to which all eligible residents will be covered is as follows:

- the ACT by July 2016
- NSW and SA by July 2018 and
- Tasmania, Victoria, Queensland and the NT by July 2019.

The NDIS will be available in these jurisdictions to all Australian residents who meet disability/early intervention criteria and are under the age of 65 years on the day they apply to participate in the scheme.

What are the challenges?

An important challenge to be faced in building the NDIS is whether disability service providers will have the capacity to meet the increased demand for support. Will small providers be able to adapt, or will the scheme be dominated by large providers? Will there be enough disability care workers to provide support?

Another challenge will be containing the cost of the scheme. Potential cost pressures over time may include higher than expected demand for support, expectations of NDIS participants

about the level of funding that will be made available to them and the costs of providing services.

Pressure to include people who acquired their disability over the age of 65 may increase, particularly if services available through the aged care system are not equivalent (or thought to be equivalent) to those available through the NDIS.

Joint governance of the NDIS by Commonwealth, state and territory governments could also present challenges, particularly if disputes arise over matters relating to the design of the scheme (for example, significant policy changes in response to cost pressures).

Shared funding of the NDIS may present future problems for the scheme. The PC recommended that the Commonwealth become the single funder of the NDIS in order to 'avoid the inefficiencies of the Commonwealth-State "blame game" that afflicts some shared funding arrangements'. Shared funding was contemplated by the PC, but not preferred. It presents the possibility of some blurring of the lines of responsibility for funding the NDIS, and hence some risk to the funding certainty the NDIS was intended to provide.

Expectations about the extent, standard and distribution of support to people with disability under the NDIS are high, and it is likely some will be disappointed. The scheme will undoubtedly transform many lives for the better, but it will need to overcome many complex challenges to achieve its promise.

Further reading

L Buckmaster and J Tomaras, National Disability Insurance Scheme Bill 2012, Bills digest, 72, 2012–13, Parliamentary Library, Canberra, 2013.

Comparing the Paid Parental Leave schemes

Dr Luke Buckmaster, Social Policy

KEY ISSUE

The Coalition and the Greens have each proposed replacing the current national Paid Parental Leave (PPL) scheme with one that represents a substantial break with Australia's existing framework for income support.

- countering some of the workforce participation disincentives for new parents posed by the tax and welfare system and
- increasing retention rates for business, with reduced training and recruitment costs.

Origins of PPL in Australia

Prior to 2011, while Australia provided some financial assistance for costs associated with newborn or adopted children, it was one of only two Organisation for Economic Co-operation and Development (OECD) countries without a national PPL scheme.

There had been calls for many years for the introduction of such a scheme, particularly as women increasingly began to combine roles in the paid workforce with caring for children. While there had been an assumption that PPL should be the responsibility of employers, by the late 2000s, it was still the case that only around half of working women were covered by this type of arrangement. Further, casual, less skilled and lower paid employees were less likely than other workers to have access to private, employer-funded arrangements.

In 2008, the Rudd Government referred an inquiry into means of parental assistance to the Productivity Commission (PC). The PC subsequently recommended that the Government introduce a publicly-funded paid parental leave scheme. It was suggested that the scheme would meet a range of commonly agreed objectives, including:

- generating child and maternal health and welfare benefits by increasing the time parents take away from work
- promoting social goals, such as that having a child and taking time out for family reasons should be viewed by the community as part of the usual course of work and life for parents in the paid workforce

Current PPL scheme

The current national PPL scheme, introduced by the Rudd Government in 2010, is paid to working parents of children born or adopted from 1 January 2011. To be eligible, persons must be primary carers and have incomes of \$150,000 or less. They must also have worked at least one day a week for at least ten of the 13 months before the birth or adoption of the child.

Those eligible are paid for 18 weeks at the National Minimum Wage (currently \$622.10 a week before tax). While PPL is paid from general taxation revenue, it is generally paid through the recipient's employer. PPL is taxable income and does not include superannuation contributions.

From January 2013, Dad and Partner Pay (DPP), a separate two-week payment, paid at the National Minimum Wage, was made available to working fathers or partners.

In 2012-13, there were around 100,000 recipients of PPL and 17,000 recipients of DPP. In 2013-14, PPL was expected to cost \$1.6 billion and DPP \$72 million.

Proposals for change

The Coalition and the Greens have each proposed replacing the current scheme with ones which, generally speaking, are much more generous. Indeed, according to Peter Whiteford of the Crawford School of Public Policy, 'the maximum level of assistance under the Coalition proposal will be one of the highest in the OECD'.

Support under both proposals would be extended to 26 weeks at replacement wage or National Minimum Wage (whichever is greater) up to a cap. The Coalition's cap would be set at a salary of \$150,000 per annum, the Greens at \$100,000. Both schemes would:

- pay superannuation
- be administered by the Department of Human Services (rather than employers) and
- be financed from a combination of a levy on companies with a taxable income above \$5 million and general revenue.

Both schemes include a two-week component for fathers and partners paid at replacement wage/minimum wage, and this is capped in the same way as the main scheme. The Coalition's option would be included in the 26 weeks in the main scheme, while the Greens' version would be added to the 26 weeks. The Coalition scheme would require Commonwealth and State public sector employees to choose between their existing schemes or the proposed new government scheme.

The Greens' scheme would commence on 1 July 2014 and cost around \$3.8 billion per year. The Coalition's scheme would commence on 1 July 2015 and cost around \$5.7 billion per year.

PPL as a workplace entitlement

An argument often used in support of the more generous Coalition/Greens schemes is that PPL should be seen as a workplace entitlement. As such, PPL should be paid at a rate which reflects the income foregone by a mother who leaves the workplace to care for her baby. According to this position, the current scheme, by paying only the minimum wage treats PPL like a welfare payment.

On the other hand, the current scheme could be seen as a more targeted workplace entitlement that also seeks to retain space for private provision. The PC argued for payment at a flat rate on the grounds that it 'would mean that the labour supply effects would be greatest for lower income, less skilled women—precisely those who are most responsive to wage subsidies and who are least likely to have privately negotiated paid parental leave'. Further, the PC found that generally, highly educated, well paid women already have a high level of attachment to the labour force and a high level of private provision. As such, full income replacement 'would have few incremental labour supply benefits'.

PPL as a welfare payment

The designs of both the current and Coalition/Greens schemes contain elements that make them as much like an Australian Government welfare payment as they are workplace entitlements. For example, rather than being funded and run privately by employers or funded (as occurs in most OECD countries) through a social insurance scheme, they are:

- fully or substantially funded from taxation revenue and
- fully or substantially administered by the Department of Human Services.

Critics of both the Coalition and Greens schemes have tended to argue that PPL should better reflect the existing framework of Australia's welfare payment system, based around targeting flat rates of payment at those most in need. As the Henry Tax Review noted, 'the primary purpose of government assistance payments to individuals is to provide them with a minimum adequate standard of living'. A further value underlying the Australian system is that there should be incentives for private provision, with the benefit system seen more as a safety net.

In this sense, the current scheme is an attempt to use the existing principles of the income support system to promote parental leave pay as a workplace entitlement, but at the same time building on the existing framework of private provision. In contrast, the Coalition/Greens proposals take a more transformative, encompassing approach aimed at decisively achieving gender equity and workforce participation goals.

Further reading

Productivity Commission (PC), Paid parental leave: support for parents with newborn children, Inquiry report, 47, PC, Melbourne, 28 February 2009.

S O'Neill, D Spooner, L Buckmaster and D Daniels, Paid Parental Leave Bill 2010, Bills digest, 175, 2009–10, Parliamentary Library, Canberra, 2010.

AUSTRALIA'S ENVIRONMENT

The background features a series of overlapping, semi-transparent geometric shapes in various shades of light blue and teal. These shapes create a dynamic, layered effect, with some areas appearing darker due to the overlap. The overall aesthetic is clean and modern, typical of a corporate or institutional report cover.

Australia's part in global climate action

Anita Talberg, Science, Technology, Environment and Resources

KEY ISSUE

Climate change is a global issue. As Australia is responsible for less than 2% of annual global greenhouse gas emissions, it is important to look at what actions China, the United States and Europe are undertaking.

The status of international negotiations

The first phase of the Kyoto Protocol, which set legally binding greenhouse gas emissions reduction targets on participating countries, ended in 2012. A second phase started in 2013 with a targeted reduction in emissions of 18% below 1990 levels by 2020. Only 36 countries – 28 of which are European Union (EU) member states – signed on to this second phase. Australia is one of those 36 countries; its target is consistent with a pre-existing and bipartisan commitment to reduce emissions so that by 2020 it produces 5% less than it did in 2000.

Negotiations on a new deal to take effect post-2020 have been underway since 2011. This new deal, which is expected to be finalised in 2015, is to be legally binding and fully inclusive of all nations, both developed and developing. It seems likely that the design of the agreement will allow pledges of various sizes and types so as to accommodate the needs of poorer nations. Australia has indicated its readiness to be part of such an agreement and has been actively participating in the process.

Australia's international commitment

Australia's pledge to reduce emissions by 5% on 2000 levels by 2020 is flexible. Should there be a global agreement under which major developing economies commit to substantially restraining their emissions and advanced economies take on comparable commitments, then Australia will increase its pledge to:

- 25%, if a global pact can stabilise emissions levels at 450 parts per million (ppm) or less; or

- 15% if the agreement cannot meet that condition.

These commitments have had bipartisan support, but whether they represent a fair and adequate contribution is an issue of contention. For comparison, the European Union (EU) targets a 20% reduction on 1990 levels by 2020; the United States (US) targets 'in the range' of 17% on 2005 levels; and China aims to cut the emissions intensity of its economy by 40% to 45% on 2005 levels. Because it is still a developing country, China prefers to measure emissions per unit of gross domestic product, referred to as emissions intensity, rather than absolute volumes of gas.

The EU, US and China together account for more than 50% of world emissions. The actions being taken to meet emissions reduction targets in these countries is of global import. The EU, a pioneer in terms of climate policy, has had an emissions trading scheme (ETS) in operation since 2005. However, climate policies in the US and China are still evolving.

Climate policy in the United States

All attempts to establish climate policies and pass legislation have been met with resistance from Congress. In June 2013, President Obama announced a new Climate Action Plan. The plan has three parts: cutting greenhouse gas emissions, adapting to the unavoidable impacts of climate change and participating in global discussions. The emissions reduction efforts have five elements: deploying clean energy; building a 21st century transportation sector; cutting energy waste in homes, businesses and factories; reducing other greenhouse gas emissions; and leading at the federal level.

Each element is achieved through policy instruments, primarily investment into research and development, grants, loans, targeted government funding and more stringent standards.

Climate policy in China

China's social and economic development

initiatives are outlined in five-year blocks in the Five Year Plans (FYPs). The 11th FYP defined reforms to be instigated from 2006 to 2010. The 12th started in 2011 and shows a strong move towards market-based mechanisms. It establishes carbon trading pilot schemes across seven provinces and cities. These pilot schemes are expected to provide invaluable information and testing grounds for a national ETS to be ready by 2016. And, according to Chinese reports, the ETS does not rule out the potential for a carbon tax. In July 2013, China's Ministry of Finance drafted regulations to put a RMB20 to RMB25 (A\$3.50 to A\$4.40) tax on fossil fuels used by Chinese firms.

Which countries have an ETS?

A total of 39 countries have some form of mandatory legislated ETS either at the national or subnational level: the 28 EU member state, and Norway, Iceland, Liechtenstein, Australia, New Zealand, Switzerland, South Korea, Kazakhstan, Canada (but only in Alberta and Quebec), US (in ten states only), and Japan (only in Tokyo and Saitama).

China is rolling out pilot ETSs in seven regions. Each is at a different stage of legislation or implementation.

What does all this mean for Australia?

In the context of Australia's international pledge, there does not appear to be a global agreement that meets the requirements for a target increase to 15%. However, Australia agreed at international climate negotiations in Copenhagen: 'that deep cuts in global emissions are required ... so as to hold the increase in global temperature below 2 degrees Celsius'. Research suggests that the world is actually heading for an increase of at least four degrees by the end of the century.

Reviewing Australia's commitment

In April 2013, Australia's Climate Change Authority began a review of the national 2020 target and progress towards it. A final report is scheduled for February 2014. The ABC news reported that a leaked draft report advocates a 15% cut in emissions on 2000 levels by 2020, moving to 40% by 2030 and 90% by 2050.

Scientists suggest that to have more than a 60% chance of limiting the temperature increase to within two degrees, global greenhouse gas emissions must be stabilised at 450 ppm. According to the 2007 report of the Intergovernmental Panel on Climate Change (IPCC), meeting this 450 ppm target would require developed countries to reduce emissions by up to 40% below 1990 levels by 2020 and then by 80% to 95% below 1990 levels by 2050. Developing countries would also need to make 'substantial reductions'.

On 27 September 2013, the IPCC released the first part of its latest report. This provides the scientific evidence upon which the next round of international negotiations can draw, but it does not delve into the mitigation of climate change (expected in a report due in 2014). Poland will host the next set of climate change negotiations in November 2013. However, no major announcements are expected before scheduled negotiations in December 2015 in Paris, when a new post-2020 agreement is due to be finalised.

Further reading

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Climate Change Authority, Caps and targets issues paper, April 2013.

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Water

Bill McCormick, Science, Technology, Environment and Resources

KEY ISSUE

Australia's climate and landscape, coupled with the demands of agriculture and a growing urban population, can make water supply a difficult matter. Northern Australia has significant water resources but these are not easy to capture and store.

In terms of rainfall, Australia is the driest inhabited continent, and the amount of rainwater that enters rivers is also very low. On average, only 12% of rainfall flows into rivers in Australia, compared to 39% for Europe and 52% for North America. In addition, our rainfall is often highly variable: 'droughts and flooding rains' is an apt description of the natural condition in much of the continent.

Water is a limited resource in most of the country, and a vital economic asset. In 2010-11, total water consumption was 13,337 Gigalitres (GL) of which agriculture used 54%, households 13%, manufacturing 5%, and mining 4%: 3% of total water used was recycled.

Under section 100 of the Constitution the Commonwealth cannot interfere with the right of states to make 'reasonable use' of river waters for irrigation purposes. The Commonwealth's attempts to solve the problems associated with water use in the Murray-Darling Basin (MDB) have been affected by this fact (see Murray-Darling brief). Much of the Commonwealth's involvement in water matters has occurred through financial assistance to the states.

Water supply and demand

The growth of urban centres puts pressure on existing water supplies both directly (more homes) and indirectly (more food consumption and industrial use). The major source for cities is surface water (that is, rivers, lakes or accumulated rainwater).

In order to combat the problem of our naturally

variable rainfall, water storage dams in Australia are designed to store far more water than is the case for similar population demands in Europe. Many of the best dam sites are already utilised and future storage options are therefore limited.

Climate change is increasing the existing variability of rainfall and reducing the average rainfall in some areas. For example, there has been a long-term decline in rainfall in south-west Western Australia since the 1970s. Water utilities across the nation are looking at ways to save water and to increase supply.

Desalination plants

An option for increasing regular water supply even during droughts is seawater desalination, although this applies mainly to coastal settlements. Desalination plants remove salts and other dissolved substances from seawater, brackish water or waste water. The usual technology used in the desalination process is reverse osmosis (RO), which allows water to pass through a membrane, leaving behind salts and other impurities. Seawater desalination plants reduce reliance on rainfall but can be expensive compared to water conservation or recycling. Significant electrical power is required to drive the RO process.

During the recent drought, severe water restrictions were put into effect and several water authorities started construction of desalination plants. However, once the drought ended, water storages were replenished, thereby reducing the need for supplies from the RO plants. Some plants have subsequently been closed.

Dams and northern development

Over the past hundred years there have been many calls to develop the substantial water resources in northern Australia. Several schemes were proposed to channel water from tropical Australia to supply farms and cities in drier areas, but the benefits were considered inadequate for the great economic and environmental cost.

The Bradfield Scheme, first discussed in

1936, proposed to divert rivers from coastal north Queensland westwards for use in the dry interior. Schemes to pipe water from the Kimberley to Perth were also proposed in the 1980s and 2000s.

In 2009, the Northern Australia Land and Water Taskforce reported on the potential for further water development in the north of the country. It found that the development of groundwater resources provides the best prospect. Unlike the MDB, most rain in the tropics falls near the coast (not in the river's headwaters) and this therefore limits the potential for new dams. The few streams in northern Australia that maintain flow through the dry season do so through groundwater discharge to the stream.

The rainfall in northern Australia is equivalent to eight and a half times the annual runoff in the MDB, but only 20% enters the rivers and streams, and 15% recharges groundwater resources. The rest ultimately evaporates. The report concluded that, despite the huge volumes of water in the wet season, 'the north can be described as being water limited'. This is because there may be little or no rain during the dry season; rainfall is highly variable between years; it mostly occurs near the coasts and on floodplains making it hard to capture; and the very high rates of evaporation require very large and deep storages.

The Coalition's Dams and Water Management Taskforce identified some opportunities for new or enhanced surface water storages in northern Australia. Its 2013 election policy for developing northern Australia proposes a White Paper that will consider establishing a Water Project Development Fund to support the advancement of water infrastructure proposals across northern Australia, including dams and groundwater projects.

Depletion and pollution of aquifers

Groundwater is important for many remote settlements and properties in Australia, but is not a major source of water supply for the bulk of the population. However, it can be a significant source in some areas, for example in Perth. It may also be used to replace surface water during drought or when restrictions are placed on use of surface water.

There was a significant shift to groundwater extraction in the MDB when the cap on surface water use came into effect in the late 1990s. As a result, the Basin Plan will implement further caps, referred to as sustainable diversion limits (SDLs) on groundwater as well as surface water extraction. However, unlike the situation with surface water, only three out of the Basin's 81 groundwater resource units are over-allocated; 34 of the resources units are under-allocated. A potential concern with groundwater use is that we have less immediate knowledge of how quickly the water is replenished and how sustainable its use is compared with that of surface water.

Sections of the community have concerns about the impacts of coal mining and coal seam gas (CSG) production on the quantity and quality of water in aquifers that are used for domestic and agricultural purposes. This is part of the reason that New South Wales has placed restrictions on CSG exploration in agricultural areas and is carrying out a review of CSG-related activities. The Commonwealth now requires assessment of the impact of coal mining and CSG proposals on aquifers.

Further reading

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Murray-Darling Basin management

Bill McCormick, Science, Technology, Environment and Resources

KEY ISSUE

The Basin Plan's implementation is essential for the sustainable management of the Murray-Darling Basin.

Agricultural water use

The Murray-Darling Basin (MDB) covers 14% of Australia and is home to over two million people. The Basin's agriculture (both dryland and irrigated) accounts for almost 40% by value of Australia's agricultural production.

The great bulk of the Basin's water use is for agriculture. Most of the irrigated area is given to pasture and crops. Some crops (vegetables, fruit and nuts) yield relatively high prices for low levels of water use, but others (such as rice) produce lower value for high levels of water use.

The Basin's highest water consumers in 2005-06 were for dairy farming, cotton-growing (20% of agricultural water), pasture and rice.

Water is also needed for domestic and industrial uses and to maintain life in the rivers and floodplains. As a result, the MDB is the most highly regulated river system in Australia, which is complicated by the fact the Basin straddles four states and the ACT.

Environmental issues

Many issues affect the water resources and ecosystems of the MDB including salinity, erosion, blue-green algal blooms, water quality, and invasive species. Climate change and resultant possible increases in drought pose a significant risk to the availability of surface water in the MDB.

The almost decade-long millennium drought, starting around 2000, caused significant damage to ecosystems as well as to the economy. It ended with widespread flooding in 2010, resulting in inundation of many floodplains and raising the Basin's water storages from 32% to 81% during 2010-11.

The flooding enabled many species to recover from the effects of a long drought but also caused widespread damage to property.

The lower Murray as a threatened ecological community

In August 2013, the River Murray and its associated wetlands, floodplains and groundwater system, was listed as a 'critically endangered' ecological community under the Environment Protection and Biodiversity Conservation Act 1999 (EPBC Act). Listed threatened ecological communities are matters of national environmental significance (MNES) under the EPBC Act and any new proposal may require approval under the Act. Only those proposals that have or are likely to have a significant impact on a MNES must be referred to the Commonwealth.

Early management

The Commonwealth's numerous attempts to facilitate the improved management of the MDB by the states were restricted by its limited constitutional powers over water and land use.

The 1915 River Murray Agreement, signed by the Commonwealth and New South Wales, South Australia and Victoria, was restricted to the main stem of the Murray. The 1987 Murray-Darling Basin Agreement addressed the broader problems of the MDB, including water quality, and established the Murray-Darling Basin Commission (MDBC).

To combat the over-allocation of water in the MDB, a cap on water diversions came into effect on 1 July 1997 for NSW, South Australia and Victoria. Programs such as the Living Murray were made to recover water entitlements so more water could stay in the rivers.

Present management and Basin Plan

In response to the millennium drought and the continuing over-allocation of MDB water resources by the states, in 2007 Prime Minister John Howard proposed a \$10 billion 10-year National Plan for Water Security. He called for the MDB states to transfer their powers to enable the Commonwealth to oversee the

management of the MDB. The MDBC would be reconstituted as an Authority (MDBA), responsible for setting a cap on the sustainable use of Basin water resources.

Agreement was not reached with all the states, so the Commonwealth legislated to achieve its aims using only Commonwealth powers. The Water Act 2007 established the MDBA which is responsible for preparing the Basin Plan for the Minister. The Plan must contain:

- long-term average Sustainable Diversion Limits (SDLs) for the amount of surface water and groundwater that can be taken from Basin water resources
- an environmental watering plan
- a water quality and salinity management plan and
- rules about trading of water.

The social, economic and environmental outcomes of the water resources must not be compromised. The Plan outlines risks to Basin water resources, such as climate change, and strategies to manage them.

The SDLs are implemented through state water resource plans, accredited by the Commonwealth. There will be a five-year phase-in period for the SDLs for each Water Resource Plan before they start in 2019.

Programs of the incoming Labor Government in 2007 implemented much of the Howard Government Plan. The Sustainable Rural Water Use and Infrastructure program provides \$5.8 billion to modernise irrigation infrastructure, thereby saving water. The Restoring the Balance in the Murray-Darling Basin program is investing up to \$3.1 billion to address over-allocation in the MDB, including through buying back water entitlements.

In 2008, all the Basin states agreed to refer their powers to the Commonwealth, and the Water Act was amended accordingly.

Basin Plan implementation

After the 2010 release for comment of the Guide to the Basin Plan there were significant public demonstrations against the proposal to reduce surface water SDLs. The MDBA raised

the SDLs in its November 2011 draft Basin Plan. The final Basin Plan was tabled on 26 November 2012.

Implementation steps of the Basin Plan include the 2013 release of the constraints management strategy; the 2014 release of the Basin-wide environmental watering strategy and new water trading rules; the 2016 determination of the adjustment to the surface water SDLs; and the 2019 start of the surface and groundwater SDLs.

Changes to SDLs

The proposed reduction in surface water SDLs from a 2009 baseline is 2,750 Gegalitres (GL) per year, but 1,658 GL of this has already been recovered through projects and water buybacks.

The level of reduction of SDLs was a major issue during the development of the Basin Plan, with the South Australian Government wanting to increase the reduction in surface water SDLs. Two Acts have been subsequently passed to amend the Water Act.

The Water Amendment (Long-term Average Sustainable Diversion Limit Adjustment) Act 2012 permits the MDBA to adjust the SDLs by up to 5% (540 GL per year) in response to environmental works and measures proposed by the Basin states. The Water Amendment (Water for the Environment Special Account) Act 2013 provides for \$1.77 billion to be deposited over the ten years starting 2014-15 to fund water recovery projects; \$200 million of this will be used to remove key constraints which limit the amount of environmental water that can be delivered through the river system. These projects aim to return an additional 450 GL of environmental water so the SDLs can be reduced by 3,200 GL per year as requested by South Australia.

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Oceans

Bill McCormick, Science, Technology, Environment and Resources

KEY ISSUE

Over the coming years Australian governments are likely to face increasing challenges in balancing conflicting interests when managing marine resources.

Australia has a vast marine jurisdiction – the third largest in the world – with an exclusive economic zone (EEZ) covering 8.2 million square kilometres. The economic and conservation value of this zone is considerable, as it contains oil and gas fields, fisheries and shipping lanes.

Managing this area is challenging with the need to achieve sustainable resource use and conservation of natural systems.

There is increasing potential for uses by one group to create adverse impacts for others.

Enforcement: There is a challenge to effectively enforcing our jurisdiction across these large ocean territories through operations covering national security, customs, quarantine, border control and search and rescue.

Jurisdictional complexity: Maritime boundaries are complex. Australian territorial sea runs from low water mark out to 12 nautical miles (NM) — a nautical mile is 1.85 kilometres.

The Offshore Constitutional Settlement (OCS) set out arrangements between the different Australian jurisdictions regarding responsibilities for fisheries, mining, shipping and marine reserves. The first three NM from the shore (coastal waters) are part of the relevant state or territory. Usually, management of the coastal waters and ownership or development of resources therein is a state/territory matter. From three to 12 NM, they belong to the Commonwealth.

The EEZ extends up to 200 NM from the coast of any Australian land (including islands). Australia also has certain rights over an additional 2.5 million square kilometres of seabed beyond the limits of its EEZ under the Continental Shelf regime.

Fisheries

Fishing is an important industry, with the 2010-11 catch of wild-caught fisheries valued at \$1.3 billion.

Under the OCS arrangements for fisheries, the states and the Northern Territory generally manage coastal species. The Australian Fisheries Management Authority (AFMA) manages deepwater or migratory species within the Australian Fishing Zone, which covers the area of the EEZ outside coastal waters. While managing Commonwealth fisheries, AFMA shares its compliance functions with other agencies and state/NT fisheries officers.

Illegal, Unregulated and Unreported (IUU) fishing is an issue in some waters of northern Australia and the Southern Ocean. In the north, illegal fishers come principally from Indonesia and Papua New Guinea, motivated by poverty and the fact that Indonesian fisheries are already under intense pressure. Coastwatch coordinates the surveillance and response to illegal foreign fishing by the Australian Defence Force (Operation RESOLUTE) and Customs.

The fishery in the EEZ off Heard Island and McDonald Islands (HIMI) in the southern ocean targets Patagonian toothfish and mackerel icefish, and is governed under the Convention on the Conservation of Antarctic Marine Living Resources. From the late 1990s, IUU fishing for Patagonian toothfish in the Southern Ocean increased dramatically, driven by industrial scale fishing involving boats flying flags of convenience. Supported by a treaty, increased Australian and French patrols in the relevant parts of their EEZs significantly reduced IUU fishing.

The Southern Ocean Maritime Patrol and Response Program, along with AFMA and the ADF, provides surveillance and apprehension of vessels operating illegally in the Southern Ocean.

Whaling in the Southern Ocean

Australia has opposed commercial whaling consistently since 1980. In 1986, the International Whaling Commission (IWC) declared a moratorium on commercial whaling, but issued permits to Japan for 'scientific

whaling' in the Southern Ocean, under Article VIII of the Whaling Convention.

Anti-whaling countries argue that 'scientific whaling' is in fact commercial whaling in all but name. In 2007, the IWC passed a non-binding resolution asking Japan to halt scientific whaling in the Southern Ocean after the IWC Scientific Committee found that the current research goals were neither critical nor requiring lethal measures.

In 2010, Australia initiated proceedings against Japan in the International Court of Justice, citing breaches of the Whaling Convention, including 'scientific' whaling without reference to conservation and management of whale populations and hunting fin and humpback whales within the Southern Ocean Sanctuary. The case was heard in 2013 and a decision is pending.

Commonwealth Marine Reserve Network

The creation of a National Representative System of Marine Protected Areas, as part of Regional Marine Plans, originated as a component of Australia's 1998 Oceans Policy.

The reserves are located in Commonwealth waters (i.e., more than three NM offshore). The south-east Commonwealth Marine Reserve Network Management Plan came into force on 1 July 2013, and plans for the other regions, plus the Coral Sea, are scheduled to come into effect on 1 July 2014. The network includes examples of all of Australia's different marine ecosystems and habitats. The sustainable use of natural resources is allowed in some parts if consistent with the primary objective of conservation.

Recreational fishing is permitted in four of the six zones, which cover large portions of the marine reserves. However, many fishers are opposed to loss of access to fishing ground.

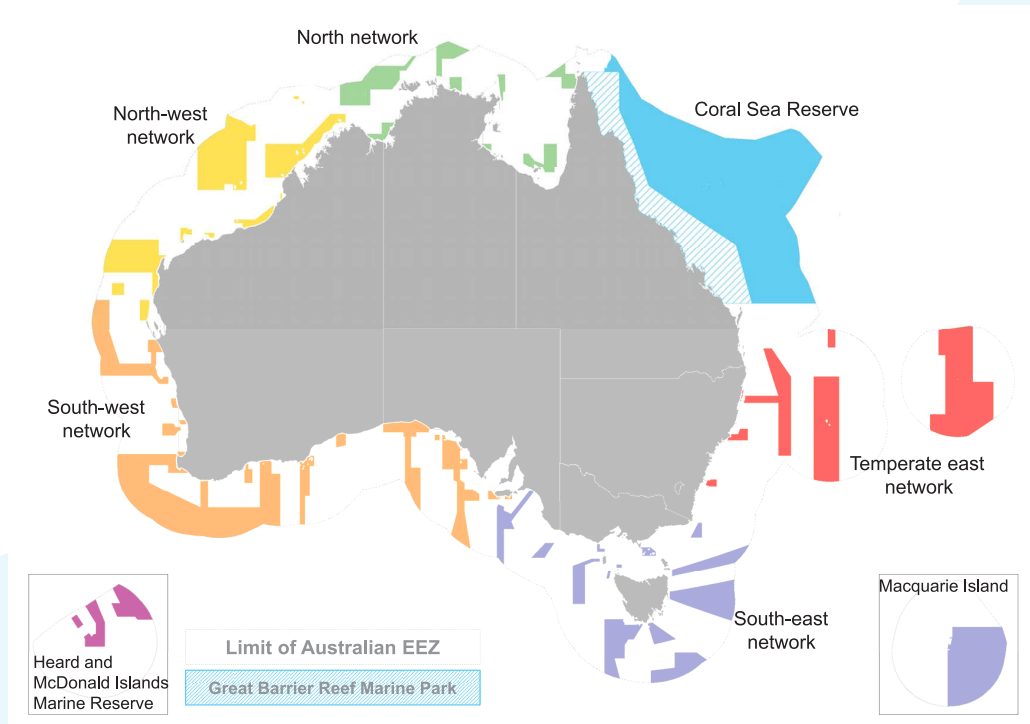
A Fisheries Adjustment Assistance Package worth around \$100 million was announced in 2012 to help communities and industries affected by the proposed network of marine reserves.

The Coalition policy on fisheries is to suspend and review management plans for the reserves.

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Commonwealth Marine Reserve Networks



Great Barrier Reef

Bill McCormick, Science, Technology, Environment and Resources

KEY ISSUE

Threats to the Great Barrier Reef need to be addressed to ensure the long term sustainability of our uses of the park.

Great Barrier Reef

The Great Barrier Reef (GBR) extends 2,300km along the coast of Queensland and is the world's largest system of coral reefs. With great diversity of species and habitats, the GBR is one of the richest and most complex natural ecosystems on earth.

However, managing and conserving this unique piece of Australia's natural heritage is a challenge. Major shipping lanes run through the region, linked to growing ports on the Queensland coast, exporting coal and other products. The health of the reef can also be affected by agricultural activities on the land, the two million tourists that visit each year, and both commercial and recreational fishing.

The Great Barrier Reef Marine Park Act 1975 (GBRMP Act) established the Great Barrier Reef Region. Nearly all the GBR region comes under the Great Barrier Reef Marine Park (GBRMP), an area of 344,000 square kilometres. In 1981, the Great Barrier Reef Region was placed on the World Heritage List. The resulting World Heritage Area (WHA) includes all waters and islands within the GBR Region, seaward from the low water mark on the Queensland coast.

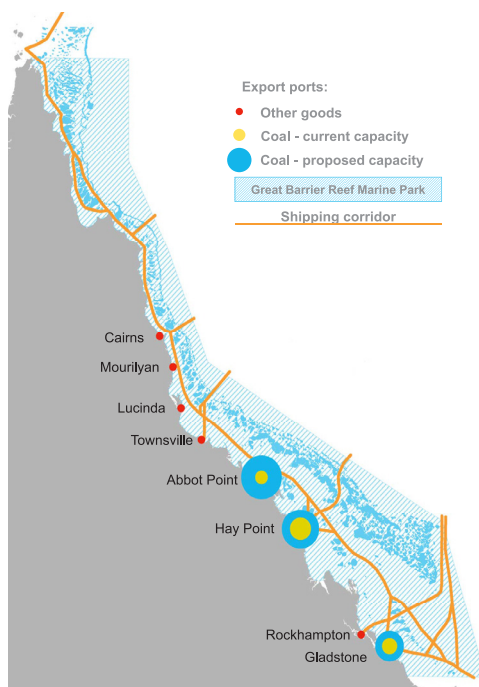
The GBRMP Act prohibits drilling and mining for minerals within all areas of the GBRMP. In 1999 regulations were promulgated to extend this ban to the entire Region.

GBR industries contributed \$5.4 billion to the economy in 2006-07. The three major industries were tourism (\$5.1 billion), commercial fishing (\$139 million) and recreational fishing (\$150 million). The GBRMP is a multiple use park, managed by the Great Barrier Reef Marine Park Authority (GBRMPA). Activities are regulated according to different zones. These range from general use zones

(where normal marine activities are permitted) to preservation zones (where people cannot enter without a permit and extractive activities are prohibited).

Under the original zoning plans, about 4.5% of the total area of the Marine Park was declared as 'no-take' areas or 'green zones', where all fishing (both recreational and commercial) was prohibited. GBRMPA found that this area was inadequate to protect the biodiversity of the GBR, so a new Zoning Plan was developed based on representative examples of each habitat type within a network of 'no-take' areas. This revised Zoning Plan, which included the 33% of the GBRMP covered by Marine National (Green) Zones, came into operation on 1 July 2004. The Great Barrier Reef Marine Park Structural Adjustment Package provided \$213.7 million in financial support to 1,782 fishers and fishery-related businesses affected by this rezoning.

Shipping lanes and ports in the GBRMP



Threats to the GBR

According to the 2013 Scientific Consensus Statement, coral cover on the whole GBR has declined by about 50% since 1985. This is a worrying finding, but coral cover in the northern GBR has remained stable—probably as a result of less coastal and port development there.

The four main direct causes of damage to reefs are coral bleaching due to prolonged elevated sea temperatures, increasing acidity of seawater, outbreaks of Crown of Thorns starfish (COTS), and cyclones. Warmer water temperatures and acidification are related to climate change and greenhouse gases. It is likely that climate change will also intensify cyclones. The GBRMP developed its Climate Change Adaptation Strategy and Action Plan 2012–2017 to address key climate change impacts on the GBR.

Occasional small COTS outbreaks are considered natural, but research suggests that their frequency has increased as a result of human influence (principally increased sediment and nutrients entering the water in run-off from the land). There are, however, specific short and long term strategies that may reduce the frequency of COTS outbreaks. GBRMPA and tourism operators are working to directly remove COTS from coral reefs of high tourism value.

Indirect Threats: GBRMPA has also identified threats from pesticides and herbicides in run-off water, and from coastal development (e.g. clearing or modifying wetlands and mangroves). The Reef Rescue program (along with the associated Reef Water Quality Protection Plan) aims to minimise runoff of nutrients, pesticides and sediments, and improve water quality entering the Park. This should also reduce the long-term risk to the reef ecosystem from COTS outbreaks.

Ports and Shipping: Large bulk carriers and tankers travelling in narrow channels through the reef can potentially run aground, as happened in 2010 when the Shen Neng1 hit Douglas Shoal 10 km outside the shipping channel and spilt 4 tonnes of heavy fuel oil.

Expansion of ports for coal and other exports requires substantial dredging of the harbours and will result in increased shipping. With more traffic comes increased risk of grounding and oil spills, and there is concern about the impacts of these activities on the GBR.

Dredge spoil from Gladstone harbour is being dumped within the WHA but five kilometres from the GBRMP. The Commonwealth has delayed its decision whether to permit spoil from the Abbot Point expansion to be dumped at a site within the GBRMP.

World Heritage in danger?

All these threats have raised concerns about the cumulative impacts on the GBR's World Heritage values. In March 2012, a delegation sent by the World Heritage Commission (WHC) visited Australia to ascertain whether the new developments affect the GBR to a level where it would need to be classified as 'World Heritage in Danger'. The Australian government provided a State Party Report on the state of conservation of the GBR WHA to the 2013 meeting of the WHC which requested an updated report to show whether substantial progress is being made to protect the GBR. The 2014 WHC meeting will consider this report in deciding whether the GBR should be listed as 'World Heritage in Danger'.

In early 2012, the Australian and Queensland governments agreed that a comprehensive strategic assessment of the GBR WHA and the adjacent coastal zone would be undertaken in accordance with section 146 of the Environment Protection and Biodiversity Conservation Act 1999 (EPBC Act). The draft reports are due to be released later this year.

Further reading

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Challenges in regulating biotechnology

Genevieve Butler, Law and Bills Digest

KEY ISSUE

Rapid developments in biotechnology pose challenges for legislators and courts internationally, as legal systems struggle to keep pace with scientific advances. Key issues include ownership of genes and genetically modified crops, equity of access to treatments, bioprospecting, biopiracy and biosafety.

Biotechnology—the use of biological knowledge and materials for human benefit – has been used for thousands of years in agriculture and medicine. However, recent decades have witnessed revolutionary scientific advances in fields such as genetic modification, use of human biomaterial, and biopharmaceuticals.

Ownership and equitable access

Fundamental to many of the new technologies is the question of ownership of biomaterial. Multinational companies providing seed, agricultural chemicals, food-processing and pharmaceuticals play a major role in biotechnology research, and are keen to see a return on their investments. However, the patent system, which protects ownership rights to new biotechnologies, can also serve to block access for many who could benefit, especially in developing countries.

Genetically modified (GM) seed commercialisation practices have come into conflict with farmers' customary practices of saving, reusing, sharing and developing plant varieties. The US biotechnology corporation, Monsanto aggressively defends its patents, requiring some users of GM canola seeds to purchase new seed every year, with a licensing fee to use the patent rights.

Gene patents have also been at the forefront of public debate, with contentious litigation both domestically and internationally. The key

difficulty is the distinction between a 'product of nature'; an altered product of nature (modified by human inventiveness) and a method of using a product of nature.

The landmark decision of the US Supreme Court in *Association for Molecular Pathology v Myriad Genetics* on 13 June 2013 overturned three decades of gene patent awards. The Court ruled that a naturally-occurring DNA segment is a product of nature and cannot be patented simply because it has been isolated. Myriad had originally obtained the patents after discovering the location and sequence of the BRCA1 and BRCA2 genes, mutations of which can increase the risk of breast and ovarian cancer. This enabled Myriad to develop and patent tests for cancer risk, which cost up to \$US4000, precluding many from access.

In a similar lawsuit brought by Cancer Voices Australia in February 2013, Australia's Federal Court provided the opposite view: that the two genes extracted from natural cells obtained from the human body could be patented. The decision is currently on appeal before the Full Court of the Federal Court.

Bioprospecting and biopiracy

Bioprospecting is the process of finding and commercialising new products, such as medicines and agrichemicals, based on biological resources.

Bioprospecting is particularly significant in Australia due to the country's diverse biological resources. In 2001, the House of Representatives Standing Committee on Primary Industries and Regional Services inquired into the contribution that bioprospecting may make to the development of new industries, especially in regional Australia.

Part 8A of the Environment Protection and Biodiversity Conservation Regulations 2000 provides a legislative framework for biodiversity, establishing a legal basis for biological discoveries and providing security for investments in research and development.

The regulations apply to biological resources of native species in Commonwealth areas taken for research and development of any genetic resources or biochemical compounds.

Bioprospecting is often based on indigenous knowledge of uses and characteristics of plants and animals. Biopiracy occurs when corporations use traditional knowledge of nature for profit, without acknowledging indigenous intellectual property rights or compensating indigenous peoples.

Many patents operate to deny economic compensation to indigenous groups or prevent them from using specific plant materials.

International laws in place to regulate bioprospecting and prevent biopiracy include the Convention on Biological Diversity (1992), to which Australia is a party, and the Nagoya Protocol (2010).

Indigenous communities in Australia have a unique understanding of native plants and their potential uses for medicine, cosmetics and nutrition. The Jarlmadangah Burru Community in the Kimberley has used the bark from the Marjala plant – said to be more powerful than morphine – as a traditional painkiller for generations. When Community Chairman John Watson lost his finger while crocodile hunting and used the Marjala plant for pain relief, the community was prompted to consider the commercial potential of the treatment. They formed a research partnership with Griffith University, resulting in a successful joint patent application.

Biosafety

Biosafety refers to the prevention of large-scale loss of biological integrity, particularly in health, agriculture and ecology. Biosafety in agriculture involves reducing the risks of disease outbreaks, quarantine breaches, genetic engineering and food contamination, while in medicine biosafety procedures ensure the integrity and suitability of organs or tissues.

In Australia, under the Gene Technology Act 2000, the Office of the Gene Technology Regulator (within the Department of Health) has a mandate to protect people's health and

safety, and the environment, by identifying risks posed by gene technology, and by managing those risks through regulating dealings with genetically modified organisms (GMOs).

GM crops produced in Australia include canola and cotton, but experimental trials of other crops are underway. GM produce can be imported into Australia, provided it meets the usual food safety guidelines. GM crops are banned in Tasmania and South Australia until 2014, when the bans will be reviewed. States that allow GM crops require buffer zones of five to 20 metres, but some critics suggest that buffers need to be at least two to three kilometres.

A case expected to set a national precedent over GM seed contamination in Australia will come before the Western Australian Supreme Court in early 2014. Stephen Marsh, a farmer near Kojonup, south-east of Perth, is suing neighbouring farmer Michael Baxter for loss of income and compensatory damages after harvested seed heads of GM canola allegedly blew onto Marsh's organic farm in 2010. As a result, Marsh lost his organic certification with the National Association for Sustainable Agriculture Australia, along with export contracts for organic oats and local deals for organic wheat, spelt, seeds and lamb. Monsanto says that while it supports its client, Baxter, it will not join as a party to the court case.

Further reading

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The Commonwealth's role in protecting the environment – cutting green tape?

Juli Tomaras, Law and Bills Digest

KEY ISSUE

Will the proposed plan to hand over environmental assessment and approvals to the states simplify the process for business while maintaining robust and transparent environmental standards?

The Environment Protection and Biodiversity Conservation Act 1999 (the Act) is aimed at assisting a co-operative implementation of Australia's international environmental responsibilities. Its basic objective is to provide for ecologically sustainable development through the protection of the environment, focusing on Commonwealth interests in the nine matters of national environmental significance listed in the Act. These include World Heritage sites, wetlands of international importance, migratory species, endangered species and the Great Barrier Reef Marine Park.

The Act provides that certain actions (including projects, developments, undertakings, or activities) which are likely to have a significant impact on a matter of national environmental significance, known as 'controlled actions', are subject to an assessment and approval process by the Environment Minister. The unlawful taking of an action that has a significant impact on a matter of national environmental significance may attract a civil or criminal penalty.

A person proposing to take an action that they think is, or may be, covered by the Act must refer the proposal to the Environment Minister. On the basis of the referral, the Environment Minister decides whether the proposal is a controlled action under the Act. If so, the Minister must choose how the impacts of the proposed action will be assessed. It is through the assessment and approval process that the Commonwealth performs its role in ensuring that Australia's obligations under international environmental treaties are met.

Currently, most proposed major projects must obtain separate approvals from both the Commonwealth Government and the relevant state or territory government. The Coalition and some industry groups, such as the Minerals Council of Australia and the Business Council of Australia, maintain that the duplicative assessment and approvals process is costly, resulting in unnecessary delays or deferral of economic activity, while not yielding any corresponding increase in environmental outcomes.

Bilateral agreements

One of the assessment options available to the Minister under section 87 of the Act is a bilateral agreement entered into with a state or territory. There are two types of bilateral agreements:

- assessment bilateral agreements provide for the accreditation of a state or territory process to assess the environmental impacts of a proposed action. However, after assessment at the state level, the approval decision is still made by the Commonwealth Minister under the Act and
- approval bilateral agreements go further by providing for the accreditation of a state or territory assessment and approval process in accordance with an agreed management plan or authorisation process under a state or territory law. Thus, a proposed action that is covered by an approval bilateral agreement does not require any further approval by the Commonwealth Minister under the Act.

With the exception of an approval bilateral agreement for the Sydney Opera House, thus far the Commonwealth has only negotiated assessment bilateral agreements. Where assessment bilateral agreements are in place, approval requirements are duplicated, but assessment requirements are not.

A push for more bilateral agreements

In 2012, the Labor Government signalled its preparedness to negotiate the transfer of environmental approval powers (that is, the level beyond assessment) to states and territories as part of its response to the Hawke review of the Act.

However, at the Council of Australian Governments meetings in April and December 2012, then Prime Minister Julia Gillard indicated more work was needed to progress such bilateral agreements. One reason cited by the Prime Minister was the need to ensure that high environmental standards would be consistently maintained across all jurisdictions. The Government had commenced negotiations on bilateral approval agreements and became concerned that states and territories may not be sufficiently committed to upholding the environmental standards it expected.

In 2012, the Australian Government also requested that the Productivity Commission (PC) benchmark Australia's major project development assessment processes against international best practice. In February 2013, the PC published an Issues Paper canvassing two potential reforms for consideration: reducing jurisdictional overlap through the use of 'approval bilateral agreements' and increasing the use of 'strategic assessments'. A strategic assessment is a big-picture approach to environment and heritage protection that is able to consider a broader range of impacts on an area than those which look at the impacts of individual action. Thus, for example, they take into account the cumulative effect of proposed or potential area use.

In June 2013, the Coalition announced that, if elected, it would implement a one-stop-shop for environmental assessment and approvals that would set high standards, make swift decisions and deliver certain outcomes.

Several business groups have argued that approval bilateral agreements would result in significant time and cost savings and be a boon to economic activity. However, there is an argument that when measured as a proportion of project value, the majority of costs are

incurred in the assessment stage, rather than in the actual approval process. As a result, the potential gains to business from a truncated approval process may be limited.

Environmental groups have expressed concern that these agreements would place undue power in the hands of state and territory governments, whose economic interest in a project may be greater than the Commonwealth's interest in environmental compliance, as illustrated in the case of *The Wilderness Society of WA (Inc) v Minister for Environment* [2013] WASC 307. This Western Australian Supreme Court decision overturned a number of decisions relating to the environmental assessment for one of WA's most controversial development proposals, the Browse LNG Precinct Proposal at James Price Point. Chief Justice Martin ruled that the decisions were unlawful, and therefore invalid, because a number of those participating in the decision-making did not declare their financial interest in the proposal.

Recently, Minister Hunt has clarified that the Commonwealth will not delegate decisions to states that have a 'conflict of interest'.

Conservation groups and some scientists would prefer that the Commonwealth retain a close and vigilant regulatory role over matters of national environmental significance.


Further reading

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Productivity Commission, Major project development assessment process: issues paper, 2013.

Productivity Commission, Major project development assessment process: draft report, 2013.

ENERGY AND INFRASTRUCTURE

The background features a series of overlapping, semi-transparent geometric shapes in various shades of light blue and cyan. These shapes create a dynamic, layered effect, with some areas appearing darker due to the overlap. The overall aesthetic is clean, modern, and professional.

Australian non-renewable energy resources

Dr Alex St John, Science, Technology, Environment and Resources

KEY ISSUE

Australia has extensive non-renewable (or traditional) energy resources, including oil, coal, gas and uranium. Tensions between domestic and export markets may increase significantly during the next few years, especially for gas.

Coal resources

Australia possesses 10% of global recoverable black coal resources, sufficient for around 125 years' production at current rates. About 87% of coal production is exported; of the remaining coal used domestically, 88% is used for power generation nationally. The heavy use of coal in Australia's energy mix is controversial, but coal still accounts for 35% of primary energy consumption and provides export earnings of more than \$30 billion annually.

Oil resources

The production of crude oil, condensate and liquefied petroleum gas has declined since 2001. Australia possesses less than 0.3% of the world's oil resources, and it exports most crude oil to Asian refineries.

Completed and announced closures of refineries will shortly see Australian refining capacity halve compared to 2000–01 levels, and liquid fuel supply will increasingly rely on imports. In the 2013–14 Budget, funds were appropriated to examine Australia's compliance with its International Energy Agency fuel stockpiling obligations.

Uranium resources

Australia possesses the world's largest low-cost uranium resource, and it is the world's third largest uranium producer. Moves to establish new uranium projects are possible during the 44th Parliament, after Queensland and New South Wales relaxed restrictions on uranium projects. New mines are being planned and constructed in Western Australia

and South Australia. All uranium is produced for export and a domestic nuclear power industry seems unlikely in the near term, despite calls from some industry and scientific groups.

Gas resources

Australia is rich in natural gas on a per capita basis, possessing 2.0% of the world's proven gas reserves, but only 0.3% of the world's population. Economically demonstrated resources amount to 147,000 petajoules (PJ) of natural gas, sufficient for around 60 years of production at current rates. This figure includes both conventional and coal seam gas (CSG). Significant further resources of unconventional gas (including CSG and shale gas) have been inferred by geologists; Geoscience Australia speculates these potential resources could yield an additional 753,000 PJ of gas. Although this represents a large additional gas resource, only a fraction of this will be economically recoverable in the foreseeable future.

Gas production

About 95% of Australia's gas is currently produced from a few main geological basins — the Carnarvon Basin offshore from Western Australia (32%); the Gippsland Basin offshore from Victoria (23%); the Surat and Bowen basins in Queensland (21%); the Otway Basin offshore from Victoria (10%); and the Cooper Basin in South Australia (9%).

Australia shares the gas fields in the Joint Petroleum Development Area that lies between Australia and East Timor; gas from this area is piped to Darwin for liquefaction and export.

Gas markets

Australia is divided into three gas markets; the Western and Northern gas markets that cover Western Australia and the Northern Territory respectively; and the Eastern gas market which covers South Australia, Tasmania, Victoria, Queensland, New South Wales and the Australian Capital Territory. The three gas markets are not connected and market conditions are different in each.

Domestic and export pricing

In contrast to the wholly domestic Eastern gas market, domestic consumers in the Western and Northern gas markets compete with export customers for the supply of gas. Prices in the Western gas market (\$8 to \$10 per gigajoule, GJ) are now significantly higher than the historic norms in the Eastern gas market (\$2 to \$6 per GJ).

The start of LNG exports from Queensland in 2014–15 is expected to place upwards pressure on gas prices in the Eastern gas market. At the same time, a number of long-term domestic gas supply contracts in New South Wales and Victoria will expire and new supply contracts will need to be negotiated. Lobby groups representing gas users claim that some Eastern gas market users are having difficulty sourcing gas supply; prices offered for long-term supply are around \$9 per GJ, which is close to export prices.

Calls for market intervention

The significant rise in Eastern gas prices from historic norms that is expected to occur has prompted calls from some gas consumers for government action to ensure gas supply. In the Eastern gas market, manufacturing, mining and electricity production accounted for 74% of gas consumption in 2009–10. For these industries,

gas is a significant cost and price increases could affect the viability of parts of these industries, particularly manufacturing.

Gas consumers sometimes call for a gas reservation policy. This market intervention would involve setting aside a proportion of gas production for domestic consumption, rather than export. Western Australia applies a domestic reservation policy to the resources it controls and Queensland reserves the right to implement one. However, both major political parties have consistently argued against such a policy and maintain that energy supply is best guaranteed by a well-functioning market. Whether a reservation policy would materially place downward pressure on prices, or contribute to surety of supply, is a matter of dispute.

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The coal seam gas debate

Dr Alex St John, Science, Technology, Environment and Resources

KEY ISSUE

Coal seam gas (CSG) is a polarising issue in some communities. Proponents argue that CSG is a vital energy resource, necessary for continued gas supply. Opponents claim that CSG could have serious environmental and social impacts.

What is CSG?

CSG is natural gas (methane) which is sourced from underground coal formations, sometimes known as coal bed methane (See Figure 1). CSG is increasingly being used to supply gas to eastern Australia.

Figure 1: Different natural gas types.

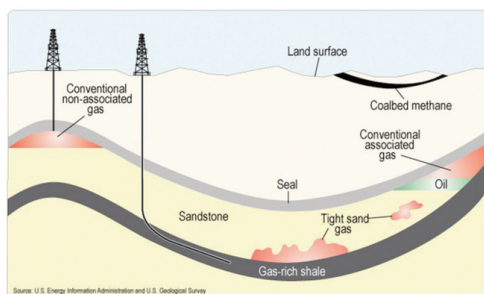


Image source: Energy Information Administration.

How is it different to conventional gas?

In conventional gas fields, the gas exists in permeable sandstone reservoirs. CSG, however, is found in coal seams, where underground water pressure keeps it contained. Pumping water out of the coal seam releases this pressure and allows gas to escape from the coal into a well.

Well spacing: in conventional gas reservoirs, a single well can give a good flow rate, as the gas steadily migrates towards the well and then out. However, it is harder for gas to move through coal seams towards a well. This means that with CSG, there needs to be more wells,

closely spaced, to achieve a satisfactory flow, which in turn means more land is needed for CSG developments.

Water production: as water pressure in the coal seam must be reduced, some CSG wells produce large volumes of water (averaging 10,000 litres of water per day per well in Queensland). This water can contain salt and other contaminants that exist normally in coal seams in varying concentrations.

Need for stimulation and directional drilling: as gas moves through coal less freely than conventional sandstone reservoirs, CSG wells sometimes are stimulated by hydraulic fracturing to make the gas flow at an acceptable rate. Similarly, vertical gas wells can be supplemented by 'lateral' wells, which are drilled horizontally along the coal seam, often over a kilometre or more. This brings the well closer to the gas, reducing the number of vertical wells that need to be drilled.

Cost: CSG fields involve more infrastructure than conventional gas wells, so the cost to produce CSG is generally higher than conventional natural gas.

Why use CSG?

Existing conventional gas resources in the eastern states are limited (see brief on energy resources). Large conventional gas resources exist offshore from Western Australia, but these are not connected to the eastern market. Gas producers have turned to CSG to supply expanding demand and replace declining supplies from conventional gas fields. Proponents also point to a valuable export market from CSG, once liquefaction plants open at Gladstone in Queensland from late 2014.

What is the controversy?

CSG development has sparked concern from environmental, agricultural and community groups. Their concerns can be summarised as follows:

Water resource competition: de-watering coal seams during gas production withdraws water from subterranean aquifers, placing pressure on limited groundwater resources, which is of concern in agricultural areas in the Great Artesian Basin.

Land-use competition: CSG deposits in Australia are often co-located with prime agricultural land, such as the Liverpool Plains in New South Wales and the Darling Downs in Queensland. Academic and media reports suggest that in some cases there is conflict between agricultural activity and CSG development.

Community concerns: some communities feel that CSG development does not fit with the character or objectives of the area, such as wine or tourist regions. Some communities are also concerned that CSG development may have an impact on their health.

Possible environmental effects: environmental groups have raised concerns that CSG development might cause environmental damage through release of untreated production water at the surface; damage to, and contamination of underground aquifers by hydraulic fracturing; damage to wildlife habitat in sensitive areas and contamination of surface water resources in drinking water catchments.

What is the evidence?

Limited evidence is available on environmental and health impacts of CSG. International comparisons are difficult, due to limited overseas use of CSG and different local conditions.

Water usage: modelling undertaken by the former Queensland Water Commission suggested that CSG activities might affect a small proportion of agricultural aquifers in the Surat basin.

Environmental/aquifer damage: although some scientists have drawn correlations between certain environmental phenomena (such as gas bubbling into the Condamine River) and CSG activity, a causal link between the factors is not yet established. It is possible that these phenomena could also be caused by natural processes. A review by the New South Wales Chief Scientist into CSG has highlighted the need for ongoing research.

Health effects: some communities near CSG developments (such as Tara in Qld) have reported a range of non-specific symptoms, which they attribute to exposure to CSG activity. A state government investigation of the reports concluded that CSG could not be established as the cause of the reported symptoms, but some groups have criticised the investigation as superficial.

Current regulatory position

As CSG is an onshore gas resource, the regulation of its development is primarily the responsibility of the states and territories, although the National Partnership Agreement on Coal Seam Gas Development attempted to implement a national approach to assessing CSG developments.

The water trigger and the IESC

In 2013, the Australian Government amended the Environment Protection and Biodiversity Conservation Act 1999 to require CSG and large coal mining developments to obtain federal approval where they would have a 'significant impact' on water resources – the so-called 'water trigger'. This approval is separate to state approvals and must take into account advice from the Independent Expert Scientific Committee on Coal Seam Gas and Large Coal Mining Development.

What about shale gas?

Although comparisons are sometimes drawn between CSG and the shale gas industry in the United States, there are substantial differences between the two and it is difficult to make direct comparisons. There is some speculation that shale gas development will start in Australia in the near future. However, it is likely that this will produce a different set of regulatory issues to CSG.

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Energy prices – the story behind rising costs

Kai Swoboda, Economics

KEY ISSUE

The rate of price increases for electricity and gas is expected to moderate in most states and territories over the next few years after a period of significant rises. The federal Government is able to directly influence only a small part of price outcomes. Intergovernmental agreements and action by state and territory governments are the most important policy levers to curb future price increases.

Electricity and gas prices for manufacturing businesses and households have increased sharply in recent years and indications are that prices will continue to increase. The underlying cause of these increases is different for electricity and gas and the contribution of each factor is also different for each state and territory.

Responsibility for regulating the electricity and gas supply industries is shared across the Commonwealth and state/territory governments. The Commonwealth Government can only directly influence price outcomes in a small way. Its key role is in coordinating and incentivising action by state and territory governments.

Extent of price increases

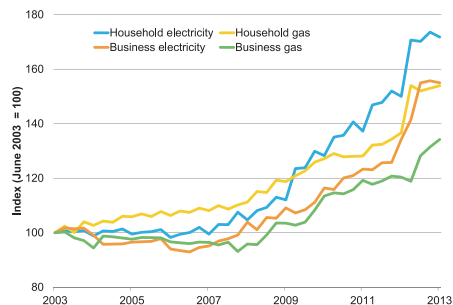
In real terms—that is, taking into account the general increase in prices across all goods and services—prices for households increased on average by 72% for electricity and 54% for gas in the 10 years to June 2013.

Real electricity price increases for manufacturing businesses over the same period have been of a similar magnitude (60%). For gas, prices for manufacturing businesses have risen to a lesser extent (29%) (figure 1).

The increase in real prices after June 2012 of around 14% for household electricity and 13% for household gas is associated with the implementation of a carbon price from July 2013.

The pattern of price increases over the 10 years to June 2013 has differed across states and territories. In real terms, the rate of increase for electricity has been 30% in Perth, 41% in Adelaide, 73% in Brisbane and 107% in Sydney. For those cities connected to natural gas networks, household gas price increases over the 10 years to June 2013 have ranged from 40% in Sydney to 78% in Perth.

Figure 1 Real electricity and gas price increases, 2003 to 2013



Source: Australian Bureau of Statistics.

Factors contributing to price increases and future outlook

There are three major components of a typical energy bill: wholesale costs (covering electricity being generated or gas being extracted); network charges (paying for the reliable delivery of energy via power lines or gas pipelines); and a retail margin (paying for meter reading and other services).

Energy bills can also include components for federal and state/territory government-based environmental programs such as those aimed at increasing renewable electricity generation. The share of each component can vary significantly across jurisdictions and for different types of customers. However the cost of transporting energy and wholesale costs typically accounts for around three-quarters of the final energy bill.

Retailers compete for customers on price and other services, in all jurisdictions except

Tasmania. All states and territories except Victoria and South Australia regulate electricity or gas retail prices in some way. Retail prices incorporate the costs of maintaining and upgrading supply network costs which are largely set by a single Commonwealth regulator under nationally agreed rules. The wholesale cost of electricity and gas prices is largely set in competitive markets. While major electricity and gas wholesale markets are connected across some state and territory boundaries, state and local factors can be an important determinant of wholesale price outcomes.

In recent years, much of the increase in prices has been attributed to the need to invest in the network component because of previous underinvestment in maintaining the network or to increase capacity. Also important has been the impact of policies to address environmental issues.

In the case of electricity, the rate of price increase is expected to moderate in the next few years. Overall, household electricity prices are expected to increase at an average of 3% over the next year, with outcomes varying across jurisdictions from a high of 16% in the Northern Territory to a 1% fall in prices in South Australia.

Smaller electricity price increases are largely the result of recent changes to the regulation of transmission and distribution networks and competition in electricity wholesale markets due to low demand growth. These may be offset in some jurisdictions by removing state and territory government interventions that have kept electricity prices lower.

In the case of gas, prices for households and businesses are expected to increase significantly in eastern Australia, as the development of new gas export terminals leads to a tightening of supply. This effect will depend on how quickly new gas resources are developed.

Proposals to keep further price increases in check have included:

- further privatisation of state government-owned electricity networks
- adjustments to environmental policies that impact on wholesale energy costs
- further retail price deregulation
- setting reliability standards based on the value that customers place on network reliability.

Commonwealth Government influence over retail price outcomes

Commonwealth intervention to directly affect retail price outcomes is largely confined to the impact of the carbon price as well as other renewable energy and energy efficiency measures. Changes to energy prices from amending these measures (which would require legislative action) should flow to through, to some extent, to end users.

Commonwealth action can also be directed at gaining intergovernmental cooperation to change regulatory outcomes and influence government-owned energy suppliers. One current policy debate is about the merits of a gas reservation policy to address price issues that are associated with LNG exports on the east coast.

There are a number of intergovernmental processes, particularly through the Council of Australian Governments and the two key regulators – the Australian Energy Market Commission and Australian Energy Regulator – to address some of these issues. However, it remains to be seen whether they will be effective in containing price increases in the medium term.

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Support for renewable energy

Anita Talberg, Science, Technology, Environment and Resources
and Kai Swoboda, Economics

KEY ISSUE

Choosing a policy to promote renewable energy in Australia has involved some trial and error. Essentially, two approaches can be taken: one that sets a target to be met at any cost or one that sets a price without commitment to the amount of renewable energy. To date both have been deployed in Australia, at the federal and/or state level.

Renewable energy is growing

Renewable sources provided around 10% of Australia's electricity generation in 2011–12. More than half of the renewables total came from hydropower, and wind power accounted for a quarter. Over the 2012 calendar year, 14 new large-scale renewable energy projects were delivered and 322,000 additional rooftop solar systems were installed. Another 15 major renewable energy projects, including 10 wind farms, were underway by January 2013.

A key objective of renewable energy policies in Australia is to reduce greenhouse gas emissions. The two main policy instruments currently driving increases in renewable energy are the Australian Government's Renewable Energy Target (RET) scheme and state-based feed-in tariff (FIT) schemes. Reviews of these schemes show that they have increased investment in renewable energy infrastructure and increased uptake of renewable energy systems. However, there has also been criticism of both types of mechanism, particularly in relation to cost and investment certainty.

The Renewable Energy Target scheme

The RET scheme – which began in 2001 and has bipartisan support – is a market-based mechanism with the aim of adding renewable energy to electricity demand. When the RET began in 2001 it aimed to increase electricity from renewable sources by 9,500 gigawatt-hours (GWh) by 2010.

The RET scheme works by requiring energy retailers to relinquish a certain number of Renewable Energy Certificates (RECs) to the government, where each REC proves that one extra megawatt-hour of electricity has been produced from renewable sources. RECs are bankable and tradeable. In 2009, new legislation increased the target to 45,000 GWh by 2020 (representing 20% of projected demand). The mechanics of the scheme were reviewed and amended in 2010 when the scheme was split into two parts: one for small-scale household systems and another for large-scale projects.

Despite almost doubling the capacity for electricity from renewable sources, and thereby achieving emission reductions of 20 million tonnes since 2001, the RET has been the subject of heavy debate.

Some criticisms of the RET

- **Target and cost:** the RET is an absolute target in GWhs. Because energy demand projections have been revised downwards, the RET may overreach its 20% goal. Industry groups say this will increase costs.
- **Policy uncertainty:** the RET scheme has been the subject of regular reviews and numerous legislative changes. This adds investor risk and increases costs. Because the RET legislation does not guarantee connection to the grid, renewable energy developers must negotiate long-term power purchase agreements (PPAs) with electricity retailers. The availability of these PPAs is hampered by policy uncertainty as energy retailers are wary of committing to long-term contracts.
- **Interaction with state laws:** the RET scheme does not compel state or local governments to facilitate the development of new renewable energy projects. Planning laws are making it increasingly difficult and costly for project developers to find suitable sites.

Despite these criticisms, the Climate Change Authority (CCA) review of the RET in 2012 made few recommendations. Chief among these were that the target remain unchanged and that reviews be undertaken only every four years.

State-level feed-in tariffs

The RET scheme imposes a target that can be met at the lowest cost. An FiT scheme sets a firm price for renewable energy and allows the market to decide how much capacity will be added. Every Australian state or territory has offered some form of FiT for renewable energy. Most of these are aimed at household systems, such as rooftop solar panels. Under such a scheme the household is guaranteed connection and receives a set rate for the electricity fed into the grid.

The popularity of these FiT schemes has exceeded all expectations with more than one million rooftop solar systems have now been installed in Australia. Nonetheless, these schemes are not without problems.

Some criticisms of FiT schemes

- **Increased network costs:** a grid that was designed to export electricity must now be changed, at some cost, to import as well.
- **Cross-subsidising:** to recoup out-of-pocket FiT costs, electricity retailers increase their charges. As a result, the benefits of reduced energy bills enjoyed by those people with rooftop solar panels come at the cost of increased energy charges for everyone else (often the people least able to afford it).

Boom/bust: in response to unanticipated high uptake of rooftop solar panels, governments have reduced tariffs or ended schemes with little or no warning. This has injected uncertainty into the policy landscape and affected small solar panel businesses.

Coal-free and gas-free electricity?

A modelling exercise by the Australian Energy Market Operator concluded that all of Australia's electricity could be generated from renewable sources by 2030. This would cost at least \$219 billion, would require 2,400 to 5,000 square kilometres of land, and would need an installed capacity more than double the expected maximum peak demand (because of the intermittent nature of renewable energy).

Interaction with other policies

In theory, a price on carbon could provide a boost for renewables by reducing the relative competitiveness of carbon-intensive electricity generation. Incentive for reducing emissions is also provided through energy efficiency programs and direct co-investment by governments in renewable energy technologies.

The Australian and state and territory governments are using intergovernmental forums to address the overlap between various policies to reduce carbon emissions.

The CCA's 2012 RET review recognised jurisdictional overlaps. However, the CCA considered that the RET was important because it mitigates the risk that uncertainty in a carbon price – in Australia or elsewhere – might suppress investment in renewables.

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Greenhouse gas reduction options

Anita Talberg and Dr Alex St John, Science, Technology, Environment and Resources

KEY ISSUE

The bulk of Australia's greenhouse gas emissions reduction efforts are likely to come from the energy sector through improved efficiency, renewable energy, and potentially carbon capture and storage. However, the land sector can also make a contribution, mainly through changed farming and forestry practices.

Australia's greenhouse gas inventory

Most of Australia's greenhouse gas emissions result from energy use, as the table below shows. The largest single category of energy use is the generation of electricity, while agriculture is also a significant contributor, accounting for almost as much as transport. This brief considers some technologies and processes that could be used to reduce Australia's emissions.

Australia's net emissions by sector, year to December 2012

Sector	Share of 2012 emissions
Energy – Electricity	34%
Energy – Stationary energy excluding electricity	17%
Energy – Transport	16%
Energy – Fugitive emissions	7%
Industrial processes	6%
Agriculture	15%
Waste	2%
Deforestation	7%
Afforestation and reforestation	-4%

Source: Quarterly Update of Australia's National Greenhouse Gas Inventory, December Quarter, 2012.

Reducing emissions from energy use

There are three ways to reduce greenhouse gas emissions from energy use. The first is to use less energy (see brief on energy efficiency). The second is to use energy sources that do not emit greenhouse gases (see brief on renewable energy). The third is to capture the greenhouse gases generated before they are released into the atmosphere. This last option is known as carbon capture and storage (CCS).

CCS removes carbon dioxide (CO₂) from waste gas streams (like a power station exhaust) and then stores the CO₂ underground in suitable geological formations. CCS is not envisaged for vehicles, but is particularly suitable for emissions that are produced from large power plants burning coal, oil or natural gas (methane). It could also be incorporated in some industrial processes.

Two CCS projects are under development in Australia: the South West CO₂ Geosequestration Hub, near Collie in Western Australia, and the CarbonNet project near the La Trobe Valley in Victoria. If commissioned, both projects will capture emissions from local industry and sequester them underground.

Globally, only eight large-scale CCS projects were in operation in 2012 and none of these is similar to the two proposed Australian projects.

CCS can be costly, especially where it is retrofitted onto existing coal and gas power stations. It is not yet clear whether CCS will be economically viable in the long term. In 2011, the Commonwealth Science and Industrial Research Organisation (CSIRO) estimated that a carbon price of between \$70 to \$90 per tonne of CO₂ would be needed for CCS to break even, which is much higher than the 2013–14 price of \$24.15 per tonne. With no carbon pricing, CCS's cost-benefit balance appears even less appealing.

Reducing emissions from waste

When household waste is deposited and piled up over a period of time, the organic components eventually begin to decompose. Depending on a number of factors, including

the type of waste and the climate of the area, the breakdown of the waste produces a mix of gases. The one of greatest concern in this context is methane, because it is a more powerful greenhouse gas than CO₂. Activities that reduce emissions from landfill include: capturing the methane, which can be burnt to generate electricity or piped to homes; flaring the methane (that is, burning it so that it does not remain in the atmosphere); and recycling or treating some of the waste, so that it does not accumulate to produce methane.

Reducing emissions from the land sector

The gas CO₂ in air is just one form of the element carbon. Carbon also exists in large quantities in the ocean, the soil and all living things (especially trees). Through the process of photosynthesis in plants, CO₂ is pulled out of the air and the carbon slowly circulates through plants, animals, soil and back to the atmosphere. Soil also absorbs and retains carbon. According to the Wentworth Group of Concerned Scientists' paper, *Optimising Carbon in the Australian Landscape*, the total stock of carbon in the Australian landscape is approximately 100 billion tonnes. National carbon emissions are in the realm of 0.5 billion tonnes per annum.

Certain factors can influence how effective the landscape is at storing carbon. For example, a short-to-medium term decrease in rainfall can cause reduced growth in plants. This means less daily photosynthesis and, therefore, reduced carbon absorption. Extreme events, such as bushfires, floods and droughts, can also have significant effects – bushfires, for example, release CO₂.

Carbon absorption by the biosphere is also known as carbon sequestration. Farmers and landholders can take steps to maximise carbon sequestration or to minimise carbon emissions. In the farming sector examples include:

- zero-tillage farming, where organic matter such as crop residues is left undisturbed to add carbon to the soil
- cover-cropping, in which another crop is planted alongside the yield crop to improve soil quality and add carbon-rich organic matter to the soil
- grazing management to reduce emissions from livestock and
- the use of biochar, which is charcoal made from plant material and agricultural waste. It is produced as an additive to soils, mainly to improve nutrient retention and carbon storage.

Generally, improving carbon retention in farming improves productivity, albeit at some economic cost. The problem with managing carbon sequestration in the farming sector is that it is difficult to monitor, assess and verify. Emissions reduction efforts in forestry are less problematic in this sense. Some possible activities include: reducing land clearing, particularly avoiding deforestation of established outback vegetation; allowing vegetation regrowth, especially native vegetation in previously cleared land; and changing fire management practices towards early dry season burning.

The Carbon Farming Initiative

Through the Carbon Farming Initiative (CFI), Australia became the first country to establish a scheme for farmers and landowners to earn carbon credits for activities that absorb or retain carbon. The credits can be sold to individuals or businesses wishing to offset their CO₂ emissions. The CFI can be linked to the Australian emissions trading scheme (ETS), allowing landholders to participate in carbon trading, but an ETS is not essential for the CFI.

The CFI has bipartisan support. The Coalition Government plans to expand the scheme to include activities outside the land sector, such as energy efficiency projects. An emissions reduction fund will pay farmers for approved projects.

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Capitalising on energy efficiency

Anita Talberg, Science, Technology, Environment and Resources, and Kai Swoboda, Economics

KEY ISSUE

There is no silver bullet for reducing Australia’s greenhouse gases. The challenge is determining the right combination of policy responses. Improving energy efficiency can be a useful path – it can reduce both emissions and operating costs at the same time.

The potential of energy efficiency in Australia

According to research group ClimateWorks, improving the energy efficiency of commercial buildings and industrial processes and equipment could save 46.9 million tonnes of greenhouse gas emissions per year. If correct, this would represent nearly one-third of Australia’s current abatement challenge (of cutting 155 million tonnes of greenhouse gases in 2020). It could also save businesses \$1.7 billion and another \$2.3 billion across the economy per year.

Australian emissions reduction cost curve

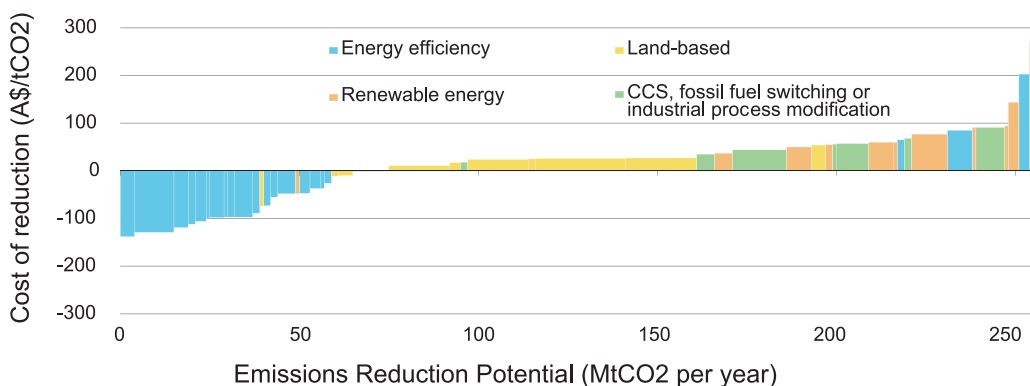
Although sometimes costly in the shorter term, improving the efficiency of energy use can provide economic benefits in the longer term. The marginal cost graph of emissions reductions, shown below, ranks the cost and abatement of policy options, classified into categories. Several energy efficiency developments are ranked highly (to the left). This means that making those changes can lead to considerable abatement for little long-term cost, or even for financial gain.

Energy efficiency policies in Australia: current and proposed

Mechanisms targeting business and industry have proven successful. For example, the Energy Efficiency Opportunities Program, which requires large energy-using companies to submit reports on energy-saving opportunities within the business, has been running since 2006. Successive reviews of the program have concluded that it is effective.

Australia’s states have been frontrunners in

Australian emissions reduction cost curve



Source: Parliamentary Library using ClimateWorks data.

energy efficiency policies. Both Victoria and New South Wales (NSW) operate market-based schemes that require energy retailers to relinquish tradeable energy efficiency certificates demonstrating that energy savings have taken place. Similar schemes (although without the use of certificates) operate in South Australia and the Australian Capital Territory.

Most jurisdictions have also implemented programs that help businesses identify energy efficiency opportunities. Victoria is rolling out digital 'smart meters' that allow power companies to track energy usage in real time. The aim is to help electricity retailers better manage demand by offering customers flexible pricing structures. All states and territories operate schemes to regulate minimum energy performance standards (MEPS) and product labelling. Federal legislation was passed in 2012 to harmonise and expand the MEPS schemes nationally.

To accelerate progress in energy efficiency, in 2009 the Council of Australian Governments agreed on a National Strategy on Energy Efficiency (NSEE) for 'a nationally consistent and coordinated approach to energy efficiency'.

In the lead-up to the 2013 election, the Australian Greens released their own policy for reducing energy intensity and cutting electricity bills. The proposal details the creation of an Energy Savings Agency (ESA) charged with removing barriers and creating incentives for energy efficiency by providing 'information, analysis, advocacy and financial support'. Amongst other responsibilities, the ESA would make recommendations on the implementation and design of a market-based scheme like those operating in Victoria and NSW.

The Coalition has been less explicit in its position on energy efficiency. From a policy perspective, it treats energy conservation as one of many ways to reduce greenhouse gas emissions, all of which will be eligible for funding from the Emissions Reduction Fund that forms part of its Direct Action Plan.

Impediments to energy efficiency

In a perfect world, rising energy prices and the imposition of a carbon price might be enough to stimulate improvements in energy efficiency. In reality there are a number of barriers that systematically stall such progress. Barriers relate to both the identification of, and

investment in, energy efficiency opportunities.

One major hurdle for stakeholders is the lack of relevant information and data. Some, but not all, of the information gap can be remedied through government interventions, such as mandatory minimum standards and labelling.

Another important barrier is known as the split incentive. The most common example is that of the landlord versus the tenant. A landlord has no incentive to spend resources on improving energy efficiency if the tenant pays the energy bills and is therefore the one who will benefit from reduced energy costs. In the owner/tenant situation, government intervention can help address the issue to some extent through more stringent building standards.

Behaviour and cultural norms are also impediments to smarter energy use. Historically, Australian cities, housing and consumption patterns have not prioritised energy efficiency. It is often easier, more convenient and cheaper in the short term to disregard energy efficiency during decision-making. This is true even at the household level. There is, therefore, a large scope for improvement. Lack of change can be due to insufficient up-front funds, lack of motivation or awareness or the particular cultural norms of the people in question. Changing these factors is a challenge.

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Broadband

Matthew James, Science, Technology, Environment and Resources

KEY ISSUE

The election debate focused on differences between the major parties' competing broadband deployment plans. However, it is also important to compare Australia's access rates with the rest of the world.

National broadband plans

National broadband plans are not unique to Australia. The International Telecommunications Union 2013 report, *Planning for Progress: Why National Broadband Plans Matter*, notes that there has been recent strong growth in plans, with some 134 plans in place by mid-2013. There is a preference for national broadband plans in European countries. The plans take different forms, such as legislation, policy frameworks, strategy and/or regulations.

In Australia, a plan for a National Broadband Network (NBN) was announced in April 2009 by the then Labor Government. Besides addressing Australia's performance in broadband availability and performance, the policy foundation for the NBN was the structural separation of Telstra to prevent it from providing retail services on a fixed line network it controls.

An article in the Parliamentary Library's *Budget Review 2013–14* provides background on each of the major party's NBN policy commitments prior to the election. Both plans would deliver access for all premises using a mix of technologies. The Labor NBN plan was to connect optical fibre to 93% of premises and use a mixture of satellite and fixed wireless for the remaining 7% of premises.

The Coalition Government's plan retains the same solution for the 7% but uses a mix of technologies for the other 93% of premises. These premises are to be connected with optic fibre. This mix has three main components:

- fibre to the node (FTTN), which runs fibre to a powered cabinet in the street that then connects to the existing Telstra copper lines running to premises

- fibre to the premises (FTTP) for new estates as in Labor's plan and
- hybrid fibre coaxial cable (HFC) that is used for pay TV, internet access and telephony. HFC cables already pass more than two million premises, mainly in more affluent metropolitan areas.

Structural separation

The NBN is being built and run by a government-owned enterprise, NBN Co. This is a wholesale-only network, which does not provide retail services directly to end-users. Its customers are retail service providers (RSPs). Under the NBN model, Telstra stands on the same footing as the many other RSPs in the market. As the fibre network is rolled out, Telstra will cease to provide retail services over the network it controls – the copper network – consistent with the legislative definition of structural separation.

For many premises, copper lines will continue to be maintained by Telstra under an agreement with the Australian Government in order that standard phone and payphone services can continue to operate pursuant to the universal service obligation.

The Coalition also supports structural separation of Telstra, but, as its technical solution requires the use of Telstra's copper lines to the premises, it proposes to buy the copper lines from Telstra. The Coalition asserts that it will be able to acquire the copper lines from Telstra without further cost beyond those contemplated by agreements already in place with Telstra.

Australia's broadband performance

According to a report from the Australian Bureau of Statistics, there were 12.2 million internet subscribers in Australia in 2012, with over 98% of internet connections being broadband. There were also six million wireless broadband connections. Advertised download rates that recorded the highest number of users – 5.4 million subscribers – were in the 8 megabits per second (Mbps) to 24 Mbps range. In the 24 Mbps or greater range, there were over 1.6 million subscribers.

According to the authoritative Akamai report, *The State of the Internet: 1st Quarter, 2013*, the average global connection speed (or data transfer rate) is 3.1 Mbps. The global average peak speed (maximum measured speed) is 18.4 Mbps. South Korea had the highest average connection speed at 14.2 Mbps, while Hong Kong had the highest peak speeds (63.6 Mbps). Australia ranks in the middle range.

The OECD Communications Outlook 2013 report notes that advertised broadband speeds are based on download data rates. However, an exception to this approach is broadband plans where data capacity is limited by data-capped offers which seem to occur in only a few Organisation for Economic Co-operation and Development (OECD) countries.

Fixed and mobile access

The OECD report also notes that, in some countries, mobile broadband providers are increasingly advertising broadband capacity at levels much closer to those of fixed broadband offers. The OECD median capacity for September 2012 for broadband mobile at 12 Mbps is not far from the fixed broadband median rate in 2010 of 15.4 Mbps. This keeps alive a debate on fixed and mobile access.

Points of difference between plans

The Coalition promises a faster completion date and lower costs compared to the Labor plan. The fact that the Coalition's plan has a target of 20% of premises getting fibre directly seems to suggest some recognition that FTTP is desirable. Speaking for the Coalition, Malcolm Turnbull stated there would be a strategic review of the time and costs to complete the NBN on the current specifications and the implications for consumers.

Funding

The Labor NBN involved peak government equity of \$30.4 billion with NBN Co having peak debt funding of \$13.7 billion. The forecast total was thus \$44.1 billion in peak funding. The Coalition forecast total peak funding of \$29.5 billion for its plan, all of which could be public funding if required.

NBN Co's Corporate Plan 2012–2015 states that the rate of return on invested funds will be 7.1%, which means that the Government's equity injections are not treated as outgoings in the Budget (they are thus 'off-budget'). Similarly, the Coalition will require NBN Co to provide a positive after-inflation return on government equity invested after the election with the aim of allowing those contributions to be off-budget. In both cases, assumptions underpin the calculations.

NBN rollout

NBN Co has revised down its rollout targets from its first corporate plan for 2011–2013 which had forecast that the fibre network would pass 1,268,000 premises by 30 June 2013. The 2012–2015 corporate plan revised that forecast down to 341,000. On 4 July 2013, NBN Co stated that it had actually passed 207,500 fibre premises which fell within the revised target range it had set since the last corporate plan.

Key issues for the Coalition Government's plan

A challenge for the Coalition Government will be the need to renegotiate aspects of the agreements that NBN Co has with Telstra, in order to allow the use of Telstra's copper lines which would otherwise be decommissioned under Labor's FTTP plan. Related to this is the challenge of keeping the NBN investment 'off-budget.' Malcolm Turnbull, now Minister for Communications, has also already acted to change the NBN Board.

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Transport infrastructure

Matthew James, Science, Technology, Environment and Resources

KEY ISSUE

Australia's transport infrastructure continues to attract criticism. Several major projects are proposed, but infrastructure decisions continue to be complicated by complex jurisdictional responsibilities, problematic financing arrangements and an overall lack of national coordination.

Infrastructure deficit

As Australia advances into the Asian century, shortcomings in its national transport infrastructure are becoming more apparent in terms of increasing traffic congestion, antiquated public transport networks, inadequate airport facilities and general shipping delays and restrictions. Each on their own can prove troublesome, but when combined they can reduce productivity and affect Australia's national reputation and living standards.

Reinforcing the idea of an infrastructure deficit, in June 2013, the advisory body Infrastructure Australia (IA) produced the National Infrastructure Plan (NIP) which stated clearly that, despite progress, much remains to be done:

Most notably, transport infrastructure construction has increased two and a half times, with over \$22 billion in engineering and construction activity occurring in 2009-10 ... Nonetheless, we still face a significant infrastructure deficit, estimated at around \$300 billion.

These are not new issues and the infrastructure backlog has been evident for much of the past decade and in global rankings. Engineers Australia's Australian Infrastructure Report Card 2010 found that, notwithstanding significant expenditures over the previous five years, standards had not improved largely due to the enormous backlog of projects.

Candidate projects

However, the wish list of projects that IA has on its books does not necessarily reflect those championed by state governments, political parties and various interest groups. Before the election, both major political parties committed funds to various proposals such as urban motorway schemes and metropolitan rail projects. Local priorities can vary from strategic national choices.

For instance, the ALP favoured the Melbourne Metro urban rail tunnel project over the East-West Link road tunnel championed by the Coalition. However, it was reported that the coalition parties did not support funding for urban rail projects over regional projects, such as the inland rail scheme. The Greens supported greater urban rail spending, high-speed rail and a funding shift that prioritises sustainable transport infrastructure, such as public and active transport and freight rail.

However, a second Sydney airport and an east coast high speed rail network were not listed as candidate projects by IA. Following the August 2013 release of the High Speed Rail Advisory Group's report, the ALP committed to preserving the property right of way for the tracks that would be required in the future. The Coalition stated that it would make a decision on the site for a new Sydney airport in its first term of government.

The federal Labor Government claimed that over the six years to 2013-14, it committed \$36 billion to Australia's transport infrastructure. Given the considerable time often required to prepare for the construction of particularly large projects, much of this funding was provided in the budget forward estimates. The 2013-14 Budget allocated almost \$24 billion to infrastructure spending, including funds for large projects, such as the Sydney F3 to M2 motorway link, the Brisbane Cross River Rail project and the Melbourne Metro rail expansion. All of these projects will take years to complete.

Integrated infrastructure

The choice of infrastructure projects is not a straightforward matter and the IA's NIP notes the effects of multiple competing interests:

Australia has nearly 600 different local, state and territory Governments that, together with the Australian Government, fund and plan infrastructure. Through this multitude of players, our infrastructure development is slow and delivery risks are high, which constrains our productivity and makes our projects less attractive for potential investors.

The NIP urges integrated infrastructure planning across all levels of government.

In May 2013, the Urban Coalition (UC), a coalition of various sustainability and development organisations, separately proposed an Urban Infrastructure Fund. The UC recommended the establishment of a new federal government department for cities and urban development and strengthening IA's role.

Meanwhile, through IA, the National Infrastructure Construction Schedule (NICS) established the first national government infrastructure listing of committed projects as a collaborative effort between the Australian, state and territory governments and local governments. The NICS provides information on major infrastructure projects committed by governments across the country in an online database.

Financial issues

When it comes to project costs and construction times, Australia's best efforts seem high when compared to similar projects overseas. The IA's NIP states:

Another recent comparison shows per kilometre costs for Australian road, heavy and light rail projects toward the upper end of similar projects in developed countries around the world. Poor project governance in Australia is one major reason why projects fail to meet their timeframes, budgets and quality objectives.

Financial solutions to the infrastructure backlog are being studied, both locally and by the Organisation for Economic Co-operation and Development.

An Infrastructure Finance Working Group (IFWG) was tasked with investigating ways to improve the capacity of Australian governments to invest in infrastructure projects. There has also been a reported policy push for a new office of financial management to examine an Infrastructure Partnership Bonds Scheme to encourage private investment in infrastructure projects.

Nonetheless, there are likely to be jurisdictional complexities that hamper infrastructure funding. Under the Australian Constitution, the Commonwealth has some powers in respect of transport, but responsibilities and funding for the various transport modes and key infrastructure facilities are shared between all three levels of government.

The Coalition's infrastructure policy proposes the strengthening of IA to develop a 15-year overview list of major projects. This would be revised every five years, along with audit and evaluation responsibilities. The policy also suggests the creation of a funding and advisory unit to investigate financing options.

Engineers Australia has released a request that Australia's political leaders move away from picking out projects just before an election:

To achieve the best outcomes for all Australians from the limited funding available, our long term infrastructure planning decisions should be made in a transparent manner unaffected by election cycles.

With the election over, the new Parliament will need to grapple with new thinking and a wider vision in this arena for the sake of Australia's future. Challenges will continue when it comes to the difficult task of selecting, prioritising and paying for infrastructure.

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SECURITY AND HUMAN RIGHTS

The background features a series of overlapping, semi-transparent geometric shapes in various shades of light blue and teal. These shapes create a dynamic, layered effect, with some areas appearing darker due to the overlap. The overall aesthetic is clean and modern.

Cyber security

Nicole Brangwin, Foreign Affairs, Defence and Security

KEY ISSUE

Cyber security is a strategic priority for Australia's national security with the threat of cyber-attacks dramatically increasing. Recent strategic policy statements and organisational reforms have highlighted the need to develop robust responses to this rapidly evolving national security issue.

Initiatives and current status

The first significant official recognition of cyber security as a national security issue emerged from the pages of the 2000 Defence White Paper, *Defence 2000: Our Future Defence Force*. This White Paper recognised the 'new security challenge' of cyber-attacks against Australia's critical national information infrastructure (NII) and noted Defence's key role in developing effective responses to such attacks. Cyber-attacks can involve instances such as espionage to obtain classified information or sabotage to disable key NII.

Subsequently, the E-Security Initiative was launched in May 2001 as part of the Howard Government's budget announcement on national security. The initiative focused on safeguarding Australia's NII, requiring a collaborative approach from the Australian Security Intelligence Organisation (ASIO), Defence Signals Directorate (DSD, now known as the Australian Signals Directorate—ASD), the Australian Federal Police (AFP) and the Attorney-General's Department (AGD) to assess and deal with identified threats.

On 2 July 2008, the Rudd Government announced a review into Australia's e-security policies, programs and capabilities (E-Security Review). The initial outcomes from the review were made public on 19 December 2008. They included the introduction of mechanisms to support exchanges of information on threats and responses between government and the private sector, particularly in the areas of banking, finance and utilities. The development

of a code of practice for e-security was flagged, with consultation expected to take place with Internet Service Providers. The remaining outcomes and recommendations were deferred to be included in an overall e-strategy framework.

The 2009 Defence White Paper, *Defending Australia in the Asia Pacific Century: Force 2030*, emphasised the potential impact of the 'emerging threat' of 'cyber warfare' against Australia's national interests. The 2009 White Paper stated that cyber-attacks on Australia's 'defence, security, government and civilian information infrastructure' could seriously threaten Australia's national security. In response, the Government established the Cyber Security Operations Centre (CSOC) to operate within ASD. CSOC was mandated to provide greater situational awareness and respond to cyber threats.

In November 2009, the Cyber Security Strategy (CSS) was released. The CSS set out the Government's strategic priorities for securing Australia's NII and featured two initiatives: the Computer Emergency Response Team (CERT Australia) and the CSOC.

CERT Australia commenced operations on 28 January 2010 and incorporated the previously established GovCERT.au to become the national coordination authority within government. CERT Australia provides information and advice on cyber security to the Australian community and engages in international cooperation.

CSOC was officially launched on 15 January 2010 and established within ASD to identify cyber intrusions against Australian interests of national importance. It also provides an operational response to cyber-attacks.

The Trusted Information Sharing Network (TISN) was established under the Howard Government and remained in place under the Rudd and Gillard Governments. TISN represents major sector groups that have been identified as critical infrastructure for the purposes of national security. These include: banking and finance, communications, energy, the food chain, health, transport and water

services. CERT Australia works closely with the TISN to advise and assist sector group members on strategies for protection against cyber-attacks.

Threat assessment

The ASIO Report to Parliament 2011–12 emphasised the extent of the cyber threat to Australia's national security:

Espionage, including via cyber means, also continues as an enduring and first-order threat to Australia's security – targeting not only government departments and agencies, but key commercial enterprises and industries. The hostile and pervasive nature of this threat required increased cooperation and coordination with domestic and international partners, as well as active engagement with elements of nationally critical industry.

ASIO reported that state and non-state actors are involved in targeting Australian interests through cyber espionage.

In June 2013, ASD official, Major General Steve Day, stated that CSOC had detected or reported 1,790 cyber security incidents in 2012. Of these, 685 required a 'heightened response' from CSOC. What was meant by a 'heightened response' was not disclosed. Major General Day noted that 'state-sponsored actors are the most active' threat and 65% of all cyber intrusions (state and non-state sponsored) involve targeting commercial information. Common commercial targets included: energy, mining and resources; banking and finance; defence capability; telecommunications; and technology.

Future prospects

In April 2013, in response to ongoing cyber intrusions, the Gillard Government mandated that all government agencies must apply the 'Top 4' Strategies to Mitigate Targeted Cyber Intrusions as part of the revised Protective Security Policy Framework. ASD assessed that around 85% of intrusions would be mitigated once the 'Top 4' strategies were implemented.

As part of the National Security Strategy, announced by Prime Minister Gillard in January 2013, the new Australian Cyber Security Centre (ACSC) is in the process of being established.

The ACSC builds on the existing CSOC and ASD is expected to continue playing a primary role in its operation. The new ACSC will comprise cyber security capabilities from ASD, ASIO, AGD, AFP and the Australian Crime Commission.

International cooperation

In 2002, Australia signed a Memorandum of Understanding with Canada, New Zealand, the United Kingdom and the United States, establishing the International Computer Network Defence (CND) Coordination Working Group (ICCWG). The ICCWG, among other things, facilitates information sharing and resolution of CND-related issues.

The 2009 Defence White Paper noted that the Government would fund the Defence Science and Technology Organisation (DSTO) to investigate advanced computer security options, via the Technical Cooperation Program. DSTO also engages with other militaries on issues such as cyber warfare.

Australia participates in a United States-led multilateral cyber security exercise known as Cyber Storm. In March 2013, Australia took part in a United States-sponsored international exercise as part of Cyber Storm IV.

During the September 2011 AUSMIN talks, Australia and the United States agreed that the Australia, New Zealand, United States Security Treaty (ANZUS Treaty) could be invoked in response to a cyber-attack. The 2013 Defence White Paper emphasised this position.

Parliament should be cognisant of any policies and international agreements that involve offensive activities to counter cyber-attacks; specifically, the criteria for which offensive action might be taken under the ANZUS Treaty.

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Surveillance in society—global communications monitoring and data retention

Nigel Brew, Foreign Affairs, Defence and Security

KEY ISSUE

In mid-2012, the Federal Government announced a proposal to routinely retain data associated with every Australian's use of Internet and telephone services. The Government has since become implicated in global monitoring programs and had its data retention proposals stymied.

In May 2012, the federal Labor Government announced a review of national security legislation. This was followed in July 2012 by a Discussion Paper on the issue. Perhaps the most controversial of the proposed reforms was the introduction of mandatory 'data retention', under which carriage service providers (CSPs) would be required to routinely retain for up to two years, communications data associated with the use of the Internet and both fixed and mobile phone services.

Communications data is information about an electronic communication, and does not include its actual content. Described by the Australian Federal Police (AFP) as 'one of the most efficient and cost effective investigative tools available to law enforcement', communications data can provide, for example, 'a snapshot of events immediately before and after a crime' and evidence of 'connections and relationships within larger associations over time'.

After revelations broke in May 2013 of secret monitoring by the US and UK Governments of their citizens' private communications following the public disclosure of classified documents by (US) National Security Agency (NSA) contractor, Edward Snowden, suspicion fell on the Australian Government over its potential involvement and use of the intercepted material.

Media reports outlined how the NSA and the UK's equivalent, the Government Communications Headquarters (GCHQ), routinely harvest, store and analyse communications data and content from

international fibre-optic cables, often by co-opting CSPs. According to one report, by May 2012, '300 GCHQ analysts and 250 NSA analysts had direct access to search this data at will'. Despite public assurances that people's privacy was protected, this was evidently not always the case.

As one report suggests, the NSA clearly suffers from 'gaps in governance and oversight', with leaked documents revealing that some staff had 'looked up the details of people they were obsessed or infatuated with'.

The interception of international communications by US and UK national security agencies quickly became conflated in the public's mind with the Australian Government's data retention proposals, due in part, to some of the commentary on the issues. Reports emerged in the Australian media 'revealing' that the AFP was accessing phone and Internet records without a warrant, as if it was a new power, when in fact warrantless access by police to communications data has been in place for over 15 years and reported in detail annually since 2008. The Australian Greens also linked the NSA revelations with data retention in a number of press releases, giving the impression that data retention is just "the thin end of the wedge".

Although, since 1956, Australia has been a party to the UKUSA Agreement that enables the sharing of 'signals intelligence' between Australia, the UK, the US, Canada and New Zealand, this is distinct from police access to communications data and content for domestic law enforcement purposes. The routine secret monitoring of telecommunications by the US and UK Governments has only served to confuse this distinction in Australia.

The AFP has denied any links between US Government monitoring programs and the data retention proposal in Australia, and has also denied receiving any information from global surveillance programs. The AFP has stated that its requests for interception and access to telecommunications data relate only to the investigation of criminal offences, and that data

retention 'is not about spying or proactively looking at things'.

Agencies are currently able to request historical communications data from a CSP without a warrant by authorisation under the Telecommunications (Interception and Access) Act 1979, in cases where the information is considered reasonably necessary for the enforcement of the criminal law or a law imposing a pecuniary penalty, or the protection of public revenue. Disclosures of prospective data (that which comes into existence after an authorisation is received and during the period it remains in force) can only be made in cases where it is considered reasonably necessary for the investigation of an offence that is punishable by imprisonment for at least three years. Data can also be released under authorisation by CSPs to the Australian Security Intelligence Organisation.

Each individual request to a CSP must be approved by a designated senior official of the relevant agency and the total annual number of requests is reported publicly. In contrast, to access the content of a communication, police must obtain a warrant.

As CSPs are not required to store communications data longer than they need to for their own business purposes, and given the increasing volume of data they handle, the information upon which police have relied in the past is increasingly not being stored for long enough, if at all. Mandatory data retention would require CSPs to store communications data for a defined period of time.

The collection of signals intelligence in Australia is conducted by the Australian Signals Directorate (ASD; a defence agency), and although it is prohibited under legislation from performing the functions of a law enforcement agency, it may assist or cooperate with such agencies in limited circumstances. The ASD is also subject to Rules to Protect the Privacy of Australians.

According to media reports, the Snowden documents have so far revealed that the ASD receives information derived from the NSA's monitoring programs, is intercepting international undersea fibre optic telecommunications cables, and has access to technology developed by US and UK intelligence agencies to crack encryption used

worldwide to protect the security of emails, phone calls and online business and banking systems.

The data retention proposal attracted strong criticism on privacy and civil liberties grounds, and for lacking detail. The Government was accused of deliberately trying to restrict public scrutiny of the proposal while not actually making a sufficient case for its introduction. The then Shadow Minister for Communications and Broadband, Malcolm Turnbull, proclaimed his 'very grave misgivings' about the proposal, calling it 'the latest effort by the Gillard Government to restrain freedom of speech', and adding that 'it seems to be heading in precisely the wrong direction'. The Australian Greens responded to the proposal with a Bill to 'strengthen the regulation of data collection on Australians' by requiring agencies to obtain a warrant.

In June 2013, the Parliamentary Joint Committee on Intelligence and Security (PJCIS) tabled the report of its year-long inquiry into the proposed reforms.

Noting that its task had been made more difficult in the absence of any draft legislation, the Committee reserved its judgement on data retention, concluding that it was for the Government to decide whether or not to introduce it. However, the Committee did recommend that any draft legislation should, amongst other things, expressly exclude content and Internet browsing records; limit the retention period to two years; provide for oversight by the Inspector-General of Intelligence and Security; and ensure that costs incurred by providers are reimbursed by the Government.

In response, the Labor Government shelved its proposals. Just before the federal election, the then Shadow Attorney-General, George Brandis (who, as a member of the PJCIS, raised concerns about the data retention proposal), was reported to have said that the Shadow Cabinet had not yet made a policy decision on data retention.

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Counter-terrorism laws – review and reform

Monica Biddington, Law and Bills Digest

KEY ISSUE

Major reviews have been undertaken and the new Parliament may consider their recommendations with a view to improving counter-terrorism laws. This article provides an overview of recent reviews recommending change, and in some cases repeal, of specific counter-terrorism laws.

The 2010 Counter-Terrorism White Paper and the more recent National Security Strategy state that the threat of terrorism to Australia and our interests is real. Terrorism has become a persistent and permanent feature of Australia's security environment. It threatens Australians and Australian interests both at home and overseas. The Government's intelligence agencies assess that further terrorist attacks could occur at any time.

Since 2001, 38 people have been prosecuted in Australia as a result of counter-terrorism operations and 22 people have been convicted of terrorism offences under the Criminal Code Act 1995 (the Criminal Code).

Anti-terrorism laws since 2001

The most controversial aspects of the counter-terrorism laws introduced since 2001 are found in Part 5.3 of the Criminal Code; namely control orders, preventative detention orders and questioning warrants. Further, academic and independent commentary for almost a decade has widely supported amending the definition of terrorism. As early as 2009, aspects of the legislation have also been of concern to the international community. The United Nations Human Rights Committee commented on the vagueness of the definition of 'terrorist act' within counter-terrorism legislation and requested that Australia reconsider the legality of its power to detain people without access to a lawyer and in conditions of secrecy.

A control order is issued by the Australian Federal Police and places specific restrictions on a person's movement, communication and associations. These are used when the AFP considers that an order would substantially assist in preventing a terrorist attack or when a person has trained with a terrorist organisation. Two have been issued, one against David Hicks and one against Jack Thomas (whose conviction was subsequently overturned).

A preventative detention order (PDO) allows a person to be detained where the AFP believes there is an imminent threat of a terrorist attack. To prevent the attack happening or to prevent the destruction of relevant evidence after an attack, a PDO allows a person to be held for up to 14 days without charge and without judicial authorisation. It has been noted that these particular provisions in the Criminal Code have not been used. While the reviews have focused on Part 5.3 of the Criminal Code, there are other existing legislative means by which a person can be detained. For example, Dr Mohamed Haneef was detained for 12 days in 2007 on suspicion of being involved in terrorist activity under section 23DB of the Crimes Act 1914, which sets out timeframes for the detention of a person arrested for a terrorist offence.

Law enforcement agency powers to prevent or investigate terrorism activity have also been the focus of recent review. In June 2013, the Parliamentary Joint Committee on Intelligence and Security tabled its Report of the Inquiry into Potential Reforms of Australia's National Security Legislation. The focus of this report was telecommunications interception reform, telecommunications sector security reform and Australian intelligence community legislation reform.

Major recent reports

In May 2013, the government released the report by the Council of Australian Governments (COAG) which reviewed an extensive range of counter-terrorism laws in all jurisdictions. The review made almost 50 recommendations, including that preventative detention provisions be repealed and the definition of terrorism be amended to include 'hoax threats', psychological harm and 'hostage taking'.

Another major report on terrorism laws was prepared by the Independent National Security Legislation Monitor (INSLM), Bret Walker SC. Walker was appointed to this position in 2011 with the task of reviewing the operation and effectiveness of national security laws. Some of the recommendations are similar to those made by the COAG Review, but the INSLM report also found that aspects of the laws, such as control orders under Division 104 of the Criminal Code are ineffective, inappropriate and unnecessary. It is worth noting that the INSLM had access to a broader range of information, including classified sources.

A key difference between these two major reports is that the COAG review concludes that legislative provisions allowing for control orders should be amended, rather than repealed, to ensure that a control order is a last resort measure.

In August 2013 the then Attorney-General, Mark Dreyfus, and shadow Attorney-General, George Brandis, were not willing to state whether they would adopt recommendations by the INSLM and COAG.

The Australian Labor Party said that it would carefully consider the reports before reaching a final position on the substance of the recommendations.

The Coalition has stated that subject to 'specific recommendations' of the INSLM, which will be carefully considered, it has no plans to make material alterations to the anti-terrorism legislation introduced under the former Coalition Government following the 11 September 2001 attacks. The specific recommendations are not further specified. More broadly, the Liberal Party policy platform states that a Coalition Government will deliver improved counter-terrorism and domestic security measures in Australia and secure our ports and airports.

Future

If the new Parliament decides to reform aspects of counter-terrorism legislation it should consider the recommendations from these detailed reviews as well as considering the broader national security landscape, which encompasses telecommunications, surveillance and intelligence.

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Transnational organised crime

Cat Barker, Foreign Affairs, Defence and Security

KEY ISSUE

Organised crime represents significant and persistent risks to Australian governments, businesses and individuals. Domestic and international collaboration is improving, but there are legislative and capability gaps.

Transnational organised crime has been estimated to generate US\$870 billion each year globally. Illicit drugs account for around half of the total, with significant funds also derived from trafficking in persons, firearms, natural resources and wildlife, people smuggling, counterfeit goods and cybercrime. Only a small portion of these funds—estimated at around 0.2%—are recovered.

The Australian Crime Commission (ACC), Australia's lead agency for combating nationally significant organised crime, assesses the overall risk to Australia of organised crime as high, and conservatively estimates the annual cost in this country to be \$15 billion. This cost represents a range of harms and losses to governments, businesses and individuals in Australia—some obvious, such as public violence—some less so, such as market distortion. Serious and organised crime was also listed as one of seven key national security risks in the 2013 National Security Strategy.

The increasingly transnational nature of organised criminal activity impacting Australia is evident. Two-thirds of Australia's nationally significant targets are linked to at least one other country. When law enforcement representatives from the United States, United Kingdom, Canada, New Zealand and Australia compared their top 20 targets, there were substantial overlaps.

Many of the same threats and trends noted in the ACC's latest report on organised crime in Australia were also highlighted in Europol's latest threat assessment. These include:

- the increasingly fluid and networked nature of organised criminal groups (a trend that has been evident for some time)
- increasing sophistication, including the exploitation of complex legal business structures and professional expertise and
- the important role of enabler activities such as money laundering, identity crime and corruption.

Two of the three critical risks identified by the ACC in its 2011 assessment—money laundering and identity crime—were enabler activities (the third was amphetamine-type stimulants; the latest assessment does not rate the risks). While enabler activities can present high risks because they facilitate a broad range of crimes, they also present opportunities as the effects of successful interventions against enabler activities are felt across all illicit markets.

Recent responses

The 2009 Organised Crime Strategic Framework (OCSF) was based around three key elements—an Organised Crime Threat Assessment (OCTA) prepared by the ACC, an Organised Crime Response Plan (OCRP) developed on the basis of the OCTA, and multi-agency responses. The Commonwealth OCRP was launched in November 2010 and the National OCRP in December 2010. A 2012 evaluation of the OCSF found it had improved cooperation and information sharing between agencies, but that stronger partnerships were required beyond government, including with private industry.

The ACC-led National Criminal Intelligence Fusion Capability, launched in 2010, expanded the Financial Intelligence Assessment Team established in 2003. It brings together analysts, investigators and technical experts from a range of federal law enforcement, intelligence and regulatory agencies and state law enforcement, and combines their respective information holdings. By September 2012, the Fusion Capability had identified 70 high threat criminal targets not previously known

to national law enforcement, some of whom were identified as laundering over \$100 million annually in suspected criminal proceeds.

The Criminal Assets Confiscation Taskforce was established in 2010 (permanent since 2012) to facilitate a more coordinated and integrated approach to federal criminal asset confiscation. The Taskforce is led by the Australian Federal Police (AFP) and includes officers from the ACC and the Australian Taxation Office. It both investigates and litigates proceeds of crime matters. In 2011–12, \$97 million in criminal assets was restrained, more than double the previous year, an increase the AFP states was assisted by the creation of the Taskforce.

Significant legislation passed in the 43rd Parliament included reforms to prevent and detect organised crime infiltration of law enforcement and the private sector supply chain. The reforms included the introduction of integrity testing of AFP, ACC and Customs employees; expanding the Australian Commission for Law Enforcement Integrity's jurisdiction; and changes to strengthen the aviation and maritime security card regimes and security obligations of some private sector organisations. Other amendments improved the ACC's ability to share information, including with the private sector, increased regulation of the alternative remittance sector to better prevent money laundering, and enhanced investigative powers and international cooperation in relation to cybercrime and electronic evidence.

Unfinished business and future challenges

Unexplained wealth laws are a powerful tool against organised crime. They allow authorities to restrain assets that appear to exceed a person's legitimate wealth, and if that person cannot demonstrate the assets were in fact acquired legitimately, to confiscate them. This enables targeting of those who profit from crime without being directly involved in the commission of an offence. Commonwealth unexplained wealth laws have been in place since 2010. However, due to the need for a connection with a constitutional head of power, their application is limited to instances where a connection can be established to a Commonwealth or foreign offence, or a state offence with a

Commonwealth aspect. This has hampered the operation of the provisions to the extent that a parliamentary committee recommended in March 2012 that the Commonwealth seek a referral of powers from the states and territories in order to legislate for a broader based national unexplained wealth scheme. Despite assurances they would still retain proceeds seized under their own laws, the states and territories have consistently rejected this proposal. In June 2013, former police commissioners Mick Palmer and Ken Moroney were appointed to negotiate with jurisdictions and 'break the deadlock', something yet to be achieved.

Draft legislation to extend the coverage of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act) to designated non-financial businesses and professions, was released for public consultation in 2007. However, the process was put on hold to allow time for recovery from the Global Financial Crisis and appears not to have recommenced. While other improvements have been made in the meantime, these outstanding reforms represent a significant gap in Australia's AML/CTF regime. These businesses and professions are being exploited in Australia to launder criminal proceeds. Further, international standards to which Australia has committed require such professions to be regulated by member countries, and Australia's compliance will be assessed in the next round of country evaluations due to begin in late 2013.

While organised criminal activity has increased in both scope and sophistication, law enforcement agencies have been operating in a fiscally constrained environment. This resource imbalance deserves consideration by the new Parliament in the face of the persistent and evolving threat presented by transnational organised crime.

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Copyright in the digital world

Mary Anne Neilsen, Law and Bills Digest

KEY ISSUE

The challenges the digital world presents to copyright are far-reaching. The Australian Law Reform Commission is conducting an inquiry into copyright and the digital economy. Depending on the Government's response to this inquiry, the new Parliament may be faced with the complex task of considering legislative reform to modernise copyright law so it is more suited to a digital environment.

Much has been happening in the world of copyright.

At an international level, Australia has been part of the negotiations for a new copyright treaty to facilitate access to published works by visually impaired people.

In Australia, there have been a number of recent challenging decisions, where courts have had to grapple with issues such as cloud computing, time shifting, web-based retransmission of broadcasts and liability of Internet Service Providers (ISPs) for copyright infringement.

The Attorney-General's Department is conducting a review of the exceptions to the technological protection measures (TPMs) provisions in the Copyright Act 1968. TPMs are technical locks copyright owners use to stop their material being copied or accessed without permission. In certain circumstances, the Copyright Act allows circumvention of TPMs.

Perhaps of greater significance, the Australian Law Reform Commission (ALRC), at the request of the Gillard Government, is in the midst of an inquiry into copyright and the digital economy.

Copyright: a delicate balance

Copyright law has long sought to create an appropriate balance between competing

interests. Copyright is concerned with encouraging the creation and dissemination of works of art and intellect, but it also acknowledges that there are appropriate limits to the rights of copyright holders. Retaining the correct balance has always been difficult; it has become more so in the digital age.

Undoubtedly, the challenges that the digital world presents to copyright are far-reaching, and will continue to be part of the political landscape for years to come. It is quite likely that the legislators in the new Parliament will face a major challenge of drafting copyright laws that keep up with the pace of technological change and suit products that have not yet been thought of.

Court decisions: copyright and the Internet

In the last few years, Australian courts have had to make important decisions concerning who is liable for Internet copyright violation. Two of the more high-profile decisions are *Roadshow v iiNet* and the *NRL v Optus TV Now* case.

Roadshow v iiNet concerned the liability of an ISP, iiNet, for copyright infringements its customers had committed using peer-to-peer file-sharing technology to upload and download copyright films. The High Court found the ISP not liable, as it had not authorised the copyright infringement of its users. However, the judgment leaves open questions about the scope of authorisation liability under the Copyright Act, and its applicability to modern technological contexts.

In the *NRL v Optus TV Now* case, the High Court refused to revisit a full Federal Court ruling that Optus, the provider of a cloud-based television recording service (TV Now), infringed the copyright in the broadcasts on the service. This decision is the first occasion an Australian court has considered copyright issues arising in cloud-based services and it raises important questions of whether the time-shifting exceptions in the Copyright Act should be extended to cloud storage platforms.

ALRC reference: copyright and the digital economy

On 29 June 2012, the ALRC received terms of reference for an inquiry into copyright and the digital economy. The ALRC was asked to consider whether exceptions and statutory licences in the Copyright Act are adequate and appropriate in the digital environment and whether further exceptions should be recommended.

The inquiry is ambitious and the issues being considered by the ALRC cover a broad range of topics from caching and indexing to cloud computing, online use for social, private or domestic purposes, transformative use, such as mash-ups or sampling in music and retransmission of free-to-air broadcasts. The inquiry is also looking at issues affecting libraries and cultural institutions, such as preservation and digitisation, contracting out of copyright exceptions and orphan works (that is, works where the owner of copyright cannot easily be established).

The ALRC has determined that its inquiry into these issues should be conducted according to five framing principles, namely:

- acknowledging and respecting authorship and creation
- maintaining incentives for creation of works and other subject matter
- promoting fair access to, and wide dissemination, of content
- providing rules that are flexible and adaptive to new technologies and
- providing rules that are consistent with Australia's international obligations.

The ALRC has so far released an Issues Paper and a Discussion Paper in relation to the inquiry.

One of the more significant of the 42 proposals in the Discussion Paper is the introduction of a new broad exception for fair use of copyright material. The fair use defence would replace most of the more specific exceptions in the Copyright Act and would be applied on a case-by-case basis according to fairness factors. Some argue a fair use exception is better able to be applied flexibly to changes in technology in the digital age. Others oppose it on the grounds there is no evidence that it would assist innovation and that an open-ended fair use exception would result in the balance between the interests of copyright owners and the interests of copyright users being tipped too heavily in favour of users.

There is significant interest in the inquiry, with 295 submissions made to the earlier Issues Paper and 860 to the Discussion Paper. These submissions will help shape the final report, which is to be submitted to government by the end of November 2013. Depending on the government response, the new Parliament may be faced with the complex task of considering legislative reform to modernise copyright law so it is more suited to a digital environment.

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Same-sex marriage

Mary Anne Neilsen, Law and Bills Digest

KEY ISSUE

The right to marry is the one significant difference between the legal treatment of same-sex and heterosexual relationships in Australia. Although same-sex marriage remains controversial, there has been a shift in community and political opinion and the issue is likely to be on the new Parliament's agenda.

Background

Same-sex marriage has been on the political agenda in Australia for several years, as part of the broader debate about the legal recognition of same-sex relationships.

The expansion of legal rights and protections afforded to same-sex couples in Australia is well developed at both federal and state level. For example, legislation now exists in New South Wales, Victoria, Tasmania, Queensland, and the Australian Capital Territory that provides for the legal recognition of relationships, including same-sex unions.

At the federal level, in 2008 and 2009, there was a wide-ranging suite of reforms to provide equal entitlements and responsibilities for same-sex couples in areas such as social security, employment, taxation and superannuation. However, there remains one significant area of difference between the treatment of same-sex and heterosexual relationships, and that is in relation to the institution of marriage. While there are fewer and fewer rights and obligations attached to married couples which do not attach to de facto couples – a status currently encompassing same-sex couples in most legal contexts – supporters of gay rights argue this is not enough, and that the remaining differences are unacceptable.

Thus, civil unions and domestic partner registries are regarded as insufficient and, for true equality, same-sex couples must have the right to marry. Undoubtedly, for some in the

community, the concept of same-sex marriage is complex and controversial, raising social, religious, moral and political questions.

Parliamentary reform

The 43rd Parliament saw an increased focus on the subject of same-sex marriage, with a flurry of legislative activity, including three Bills designed to amend the Marriage Act 1961 in order to allow people the right to marry, irrespective of their sex (one Bill was introduced by Labor backbencher Stephen Jones, one by Greens MP Adam Bandt and Independent MP Andrew Wilkie and one by Greens Senator Sarah Hanson-Young). The Bills, if enacted, would also have removed the prohibition on the recognition of marriage between same-sex couples solemnised in a foreign country. These Bills were the subject of two parliamentary committee inquiries, but were not passed by the Parliament.

Opinion polls

The Parliamentary Library's chronology of selected polls states that the outcomes of several polls from a variety of groups conducted over the years 2004 to 2010 may suggest a shift in public opinion in favour of same-sex marriage. However, in an August 2013 Fairfax Nielsen Poll 57% of respondents said that same-sex marriage was 'not important at all' in deciding how they would vote in the coming election.

Position of the political parties

The 43rd Parliament saw a shift in political party attitudes to same-sex marriage. In December 2011, the Labor Party's platform was amended to support same-sex marriage, but to allow Labor MPs to have a conscience vote on the issue. Kevin Rudd reversed his opposition to gay marriage in May 2013, shortly before regaining the Labor leadership. During the election campaign, Rudd promised that if re-elected, his Government would introduce marriage equality legislation within one hundred days of taking office, and Labor MPs would be allowed a conscience vote on the issue.

Tony Abbott has traditionally opposed same-sex marriage, and in the 2012 parliamentary debates on the same-sex marriage Bills, Coalition MPs were not allowed a conscience vote. In the election campaign, Abbott reaffirmed that he would not support legislation to allow gay marriage. He did not see the issue as a priority for a Coalition Government. A number of Coalition members have indicated however that they would support marriage equality if the party room determines a conscience vote is available.

The Australian Greens have consistently supported same-sex marriage and have sought to legislate in support of their position in both the 42nd and 43rd Parliaments.

International developments

Attention to the issue of same-sex marriage in Australia often follows developments overseas. A growing number of countries allow same-sex marriage (currently 16) with New Zealand, parts of the United Kingdom and France most recently joining the ranks. There is an argument that the Hague Marriage Convention requires signatory countries (Australia is one) to recognise overseas same-sex marriages. In May 2013, Senator Hanson-Young introduced legislation which, if enacted, would have given recognition to valid same-sex marriages entered into overseas. The Bill was a specific response to the changes in New Zealand and would have allowed Australian same-sex couples planning to marry in New Zealand to have their marriage recognised on return to Australia.

There have also been significant developments in the United States where the Supreme Court recently gave two decisions which have had an impact on same-sex marriage. One of them cleared the way for same-sex marriage in California, the 12th state to recognise same-sex marriage, and the other struck down the Congress' Defense of Marriage Act, which provided that in all federal rules and rulings, the word 'marriage' means only a legal union between one man and one woman as husband and wife. According to civil rights lawyer, Father Frank Brennan these decisions will have an impact beyond the United States.

Constitutional issues and state same-sex marriage laws

Introducing same-sex marriage at a state and territory level has been seen as a fall-back position for marriage equality advocates. New South Wales, Tasmania, South Australia and the Australian Capital Territory have all indicated a willingness to introduce same-sex marriage laws.

State same-sex marriage laws raise the question of whether state parliaments have the power to pass such laws. According to constitutional lawyer, Anne Twomey, the short answer is yes; the more difficult question is whether that law will be effective or whether it will be inoperative because it is inconsistent with a Commonwealth law, namely the Marriage Act. Twomey argues that the answer to this question is unclear and unknowable until the High Court decides. Furthermore, she argues that even if operative, a state marriage law would do little more than facilitate the holding of a ceremony. It might confer on the parties to a same-sex marriage the status of 'married' for the purposes of a specific state, but it is most unlikely that the parties would be regarded as legally 'married' for the purposes of Commonwealth law, or under the law of any other state. It would therefore not attract any legal benefits or status accorded to a married couple.

The legal uncertainty is not limited to the states. The Constitution gives the federal parliament power over 'marriage', but the High Court has not said what this term means. The key question is whether federal power is limited by the view of the 19th century framers of the Constitution that 'marriage' means a union between a man and a woman, or has it evolved to encompass other relationships. George Williams, professor of law at the University of New South Wales, says the bottom line is that whichever parliament first legislates for same-sex marriage, a High Court challenge will likely follow.

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The Royal Commission into Institutional Responses to Child Sexual Abuse and related inquiries

Kirsty Magarey, Law and Bills Digest

KEY ISSUE

The Royal Commission into Institutional Responses to Child Sexual Abuse was announced in 2012 and its interim report is due in June 2014. The states and territories will be intimately involved in developing responses and while the timelines for the Royal Commission are long, controversies have already arisen.

Royal Commission into institutional responses to child sexual abuse

The establishment of the Royal Commission into Institutional Responses to Child Sexual Abuse was announced by then Prime Minister Gillard on 12 November 2012. Historically, the Commonwealth has not played a significant role in the handling of sexual abuse issues, as this is the responsibility of state and territory governments. It was, however, deemed appropriate to obtain a national perspective on this matter.

The processes establishing the Royal Commission have been consultative and have generally received bipartisan support, despite some initial concerns in the broader community that the Australian Government was not best placed to manage such issues.

Before issuing the Letters Patent with the final terms of reference and the appointment of the six-member Royal Commission on 11 January 2013, the Government conducted a brief consultation, issuing a discussion paper on 19 November 2012, with submissions accepted to 26 November 2012.

The Royal Commissions Amendment Bill 2013 was passed through the Parliament with no dissenting voices, with the then Opposition expressing the 'Coalition's wholehearted support'. The Bill received Royal Assent on 28 March 2013.

The Royal Commission will work closely with the states and territories. All states have issued their own complementary Letters Patent to allow the Royal Commission to function effectively throughout Australia. Two current state inquiries have been given the power to cooperate with the Royal Commission:

- the Victorian Inquiry into the Handling of Child Abuse by Religious and Other Organisations being conducted by the Victorian Parliament's Family and Community Development Committee (due to report, with an extension, on 15 November 2013) and the
- New South Wales (NSW) Special Commission of Inquiry Concerning the Investigation of Certain Child Sexual Abuse Allegations in the Hunter Region, with a reporting date extended to 28 February 2014.

Challenging authority

The Chair of the Royal Commission, Justice McClellan, observed at an early stage that the Royal Commission would stand ready 'to challenge authority and the actions of those in power'.

The Royal Commission has already identified over 40 relevant inquiries, mostly undertaken at a state and territory level, which preceded its establishment and will inform its initial research.

The Royal Commission will consider not only the effectiveness of measures suggested earlier, but also the extent to which such measures have been successfully implemented and the advisability of introducing them into other jurisdictions.

It will be difficult to identify which issues — such as 'working with children' checks — need to be addressed at a national level.

The Royal Commission has commenced an extensive research program. It has released several issues papers and called for submissions on Working with Children Check, Towards Healing and Child Safe Institutions.

Bearing witness

It has been observed with respect to the establishment of the Royal Commission: 'The Government cannot undo the past. It cannot take away the pain. But we can listen and we can bear witness'. Extensive private hearings are already underway.

Justice McClellan has remarked on the need to listen and on the lack of community understanding regarding the effect of sexual abuse on children and the extent to which it impacts on their lives. The hearings process will, in part, attempt to address this ignorance.

The amendment Bill passed by the Parliament was strongly focussed on protecting victims by providing for small private hearings and the confidentiality of information provided. It also allows victims to choose appropriate methods of communication.

It has been observed that the need to protect alleged perpetrators is also a concern, although it was not the focus of the amendment Bill. The Royal Commission will not directly be making individual findings; however, it has the power to refer matters to the relevant authorities without the evidence of witnesses being tested through traditional legal methods. Both Justice McClellan and Gail Furness, Counsel Assisting, have commented that evidence given in private hearings will have limited evidentiary use.

In a widely reported comment, the Chief Executive Officer of the Royal Commission, Janette Dines, observed the Royal Commission was not established to examine individual cases of alleged abuse but to identify where institutions have gone wrong and what can be done to protect children in the future.

Survivors of child sexual abuse – both those who choose to appear before the Royal Commission and those who may be affected by its media coverage – require appropriate support. Accordingly funding of \$434.1million over four years provided for the Royal Commission in the 2013-14 Budget included \$45 million for expert support services. These services include the provision of free legal advice and counselling, support and case management services.

Timeframes and coverage

As noted above, the deadlines for both the Victorian and NSW inquiries have been extended. NSW Premier Barry O'Farrell commented:

... it is obviously more important that the relevant matters are properly and thoroughly investigated ... No-one wants any shortcuts when it comes into matters as serious as these.

An early concern regarding the Royal Commission was the length of time it might take to address the issues. It has been noted with concern that a comparable Irish Commission took nine years to conduct its inquiry.

Timelines may extend not only because the labour involved has been more than expected, but also because the terms of reference may be expanded. Interestingly, the Mullighan Inquiry in South Australia initially investigated children in state care. However, it was subsequently found necessary to extend the Inquiry to children on the APY (Anangu Pitjantjatjara Yankunytjatjara) Lands. The question as to whether it is appropriate to extend the Royal Commission to investigate abuse in a domestic setting, as well as within institutional settings, has already arisen. It has been noted that abuse in a family is even more pervasive and pernicious than abuse in an institutional setting.

The Royal Commission is required by its terms of reference to prepare an interim report by 30 June 2014, although this could be renegotiated. The final reporting date is currently scheduled for no later than 31 December 2015.

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AUSTRALIA IN THE WORLD

The background of the page is composed of several overlapping, semi-transparent geometric shapes in various shades of light blue and cyan. These shapes create a modern, abstract design that occupies the lower half of the page, while the upper half is a plain, light blue gradient.

Multilateral engagement—Australia's role in the United Nations Security Council and the G20

Nicole Brangwin, Foreign Affairs, Defence and Security and Tarek Dale, Economics

KEY ISSUE

Australia is well positioned on the global stage at two major international forums after winning a non-permanent seat on the United Nations Security Council (UNSC) and agreeing to host the Group of Twenty (G20) meetings in Australia in 2014.

United Nations Security Council (UNSC)

On 1 January 2013, Australia commenced a two-year term as a non-permanent member of the UNSC. This is the fifth time Australia has sat on the UNSC since the organisation held its first session in January 1946, over which Australia presided.

As part of this role, Australia chairs three Security Council subsidiary committees (until 31 December 2013) on Iran, al Qaeda and the Taliban. Australia is also the 'pen holder' for Afghanistan—'pen holders' take the lead in preparing UNSC resolutions.

Each UNSC member rotates through the presidency role on a monthly basis. For the month of September 2013, it was Australia's turn to preside over the UNSC. As President, Australia was responsible for 'convening and chairing Security Council meetings, managing the agenda, and facilitating the work of the Council'. Many commentators viewed the presidency as an opportunity for Australia to influence the agenda, particularly on the situation in Syria. Australia is expected to return to the UNSC Presidency near the end of next year.

Australia's presidency came at a volatile time in international affairs, with the response to the escalating situation in Syria deadlocked among the veto-wielding permanent members of the UNSC. While Syria did not feature prominently in the September Programme of Work, which was discussed and agreed to by UNSC members on 4 September, UNSC President,

Australia's Ambassador, Gary Quinlan, told reporters that 'discussion among the P-5 went nowhere' on the issue of Syria. Consequently, it was decided that convening a formal meeting on Syria would be pointless at that time, especially since the UN team investigating the alleged 'chemical attack' in Syria had not yet reported its findings.

Australia's presidency also aligned with the opening of the United Nations General Assembly's (UNGA's) 68th session. World leaders took part in the general debate, including Foreign Minister Julie Bishop.

Traditionally, the President of the UNSC promotes an issue of particular importance. On 26 September 2013, Australia initiated a high-level meeting on small arms, which was chaired by Foreign Minister Julie Bishop. Consequently, the UNSC adopted its first resolution (2117) solely dedicated to small arms and light weapons. By promoting this issue, Australia sought to capitalise on the momentum gained from the UNGA's adoption of the Arms Trade Treaty (ATT) on 2 April 2013. The issue of small arms had not been discussed in the UNSC since 2008.

Last year, the UNSC adopted 53 resolutions, of which 50 were unanimous. Thirty-two of the resolutions were Chapter VII mandates, shoring up peacekeeping and political missions in countries such as Afghanistan, Mali and Somalia. Two draft resolutions on Syria were vetoed by China and Russia. At the time of writing, the UNSC had adopted 33 resolutions this year.

Following recent discussions at the G20 Leaders' Summit in St Petersburg, Russia and United States' (US) President Barack Obama's 10 September 2013 speech on Syria, the UNSC achieved consensus on the Syria issue and unanimously adopted Resolution 2118, requiring the Assad regime to surrender its chemical weapons.

G20

Hosting the Group of Twenty (G20) in 2014 is a significant opportunity for Australia. A year of meetings by senior officials and ministers will culminate in a Leaders' Summit in Brisbane in November 2014. Australia, as the chair, has a unique opportunity to shape the outcomes of the summit that has been labelled the world's premier economic policy forum.

Australia has been involved since the start of the G20. The forum was established in 1999 after the Asian financial crisis, when G7 finance ministers and central bank officials agreed on the need to extend economic policy coordination to a larger group that included key developing nations. From 1999 onwards, finance ministers and central bankers have met to coordinate economic policy and regulation (including a 2006 meeting in Melbourne). The group includes members of 19 countries and the European Union. Together, the G20 nations represent approximately 80% of international economic activity and 90% of global trade.

Following the 2008 financial crisis, Prime Minister Rudd was influential in promoting the G20 as a forum of choice for international coordination. In 2008 when US President George W Bush convened a meeting of heads of state in Washington, Australia's inclusion in the forum represented a new and important opportunity for middle-power diplomacy.

The period during and after the financial crisis was a major success for the G20. International leaders at the London summit in 2009 committed to a combined US\$5 trillion fiscal stimulus and US\$1 trillion in additional resources for the International Monetary Fund, multilateral development banks and increased support for trade finance. Amidst the confusion of the financial crisis, this represented clear coordinated policy action. Since then, G20 heads of government have met annually (twice in 2009), with senior officials and ministers meeting prior to the Leaders' Summit. There is no dedicated secretariat for the G20—each host country is responsible for coordination and administration.

As chair in 2014, Australia is now a member of the Troika; a group that includes previous (Mexico), current (Russia) and future chairs (Australia). Following its success after the 2008 financial crisis, commentators have argued that more recent G20

summits lack clear outcomes and commitments, and the forum's consensus approach means that difficult policy issues may be avoided or left unresolved. Although hosting the G20 represents an enormous logistical challenge for Australia, the harder task may be ensuring that the forum lives up to its early promise.

APEC

Australia is one of the founding members of Asia-Pacific Economic Cooperation (APEC), which formed in 1989. APEC's aims are predominantly trade and investment focused; trying to promote 'economic growth and prosperity for the region and strengthen the Asia-Pacific community'. APEC consists of 21 member economies.

APEC's Gross Domestic Product (GDP) in terms of Purchasing Power Parity has almost tripled over the last two decades—from \$14.8 trillion in 1992 to \$43.9 trillion in 2011 (calculated in international dollars). Australia's trade with the APEC region in 2011 saw an average increase of 7.5% per annum since 2006 and accounted for 71% of Australia's total goods and services trade (A\$431.5 billion).

The most recent APEC Economic Leaders' Week meetings took place on 1-8 October 2013 in Bali, Indonesia.

To date, 12 APEC countries have joined the Trans Pacific Partnership (TPP), which is separate to APEC and seeks to eliminate or reduce 'barriers to trade and investment' in the Asia-Pacific region. Australia joined the TPP in 2008. Negotiations are continuing on the development of a 'high-standard regional trade and investment agreement' among members.

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The Australia-United States defence alliance

Dr Nathan Church, Foreign Affairs, Defence and Security

KEY ISSUE

An enduring alliance with the United States (US) remains Australia's most important defence relationship and continues to act as a crucial force multiplier for Australian Defence Force (ADF) capability. However, increasing financial constraints, the rise of China and the uncertain nature of the US rebalance within the Pacific all pose important questions about how Australia will further consolidate its relationship with the US across the next decade and beyond.

Financial constraints

The Australia-US alliance is often described as being founded on shared values and bonds of friendship, but this ultimately means little without tangible evidence of collaboration. One of the clearest examples of Australia and the US working together has been the defence relationship, the symbiotic nature of which ensures an increasing array of information sharing, personnel exchanges, combined exercises and shared engagement with partner nations across the Indo-Pacific. These, among others, are clear advantages to Australia which flow from the defence relationship with the US.

Yet despite the Australian public's continued enthusiasm for such collaboration, the alliance is fundamentally unequal, with the US shouldering a far heavier financial and operational burden by virtue of its size. The Global Financial Crisis and resulting sequestration of the US defence budget has further highlighted this point as, over the coming years, Australia is likely to be asked to do even more as a US partner. However, the ADF will almost certainly struggle to absorb any new demands without additional resources.

To engage with some of these challenges, Australia and the US have made recent progress in finding new collaborative efficiencies, evident in the Defence Trade

Cooperation Treaty ratified on 16 May 2013. Only the United Kingdom has a similar arrangement with the US, and its benefits are substantial – reducing red tape, minimising procurement delays and improving data sharing. Such arrangements also make it easier for Australia to gain access to advanced defence technologies, which it would be unable to develop domestically.

Although such initiatives will continue to provide Australia with unique levels of access and engagement with the US, this will not change the fact that Australia will continue to leverage US defence capabilities unevenly, no matter how politically unpalatable this notion may seem. Expectations management will be crucial in navigating the alliance relationship in the future, but increases to Australia's defence budget would probably do much to increase US confidence as well.

Rise of China

Over the past decade, Australia's need to contextualise its alliance with the US appropriately has come into stark focus, because of China's increased economic power and strategic influence. Australia's enduring diplomatic ties with the US and increasing economic links with China have led some commentators to question whether Australia will eventually have to choose between them. Although the Australian Government's answer has been a resounding 'no', China's growing dominance, particularly in Southeast Asia, will undoubtedly challenge the status quo, and accordingly, have an impact on the Australia-US alliance.

The biggest challenge for Australia will arguably be whether it is sufficiently adaptable to respond to whatever the US (and China) determine as the way forward in their own diplomatic relationship. Although the Australia-US alliance has effectively served the interests of both nations for decades, the US will continue to prioritise its own intrinsic national interests, and it is these (largely strategic) factors that will determine its future dealings with China.

Accordingly, commentators have contended that the US alliance will be forced to evolve, whether Australia likes it or not, especially as the Asia-Pacific is in 'a state of strategic flux'. But with expanding roles in key multilateral regional forums, Australia and the US also have strong opportunities to engage with China – and other regional partners – to work through this uncertainty and strengthen areas of cooperation.

Implications of the US rebalance

Australia's welcoming of a rotational deployment of US Marines to Darwin as part of the US rebalance into the Asia-Pacific provides a further example of the growing US alliance and highlights the geographical significance of Australia for the US. This deployment will likely benefit the Australia-US defence relationship through exposing the respective militaries to combined training and interoperability. However, the question of how this ongoing (and expanding) deployment will be financed in the long-term remains unresolved, which potentially risks complicating any political goodwill created.

The Darwin deployment poses further questions as to the extent to which the US rebalance into Southeast Asia will be fully implemented. For example, the US could attempt to further leverage Australian bases to deploy additional military personnel and capabilities within the Indo-Pacific region. Although studies have shown that the current Marines deployment to Darwin has had no adverse social or economic impact, any substantial expansion could change this – and make it harder for the Australian Government to demonstrate a net benefit.

Conversely, other global foreign policy challenges could work to dilute the rebalance, or at least limit its progress. The continued conflict in Syria has emerged as a further complication to US foreign policy plans. Other similar flashpoints in the future could continue to divert further resources and momentum from the overall rebalance mission.

Australia cannot take US engagement in the region for granted. As such, commentators have called on the Australian Government to take a proactive approach, especially in the realm of humanitarian and disaster response (HADR) capability. Through emphasising HADR as a regional engagement tool (or even establishing a regional HADR centre) Australia could provide leadership and experience – while partnering with the US – to provide productive and non-threatening multilateral regional engagement opportunities.

Further benefits to Australia would include the ability to build on momentum from previous HADR successes (such as the response in 2011 to the Japanese earthquake and tsunami) and maximise use of new ADF procurements – particularly the two soon-to-be-delivered landing helicopter docks (LHD).

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Australia's economic relationships with China

Dr Anne Holmes, Economics

KEY ISSUE

As the Chinese economy moves from a focus on investment in physical infrastructure to developing social infrastructure, and as it moves from export driven growth to consumption driven growth, there will be changes in what it imports from other countries. Australia will look to maintain and build upon the trading partnership it has had with China in recent years.

Background

China's growth since the 1970s has entailed urbanisation, growth in manufacturing and investment in infrastructure. This created demand for building materials, energy for electricity and transport and raw materials for manufacturing.

Australia was well placed to meet a lot of this demand, and it was a ready market for Chinese manufactured goods.

Today, China is Australia's largest trading partner in terms of both imports and exports. Australia is China's sixth largest trading partner; it is China's fifth biggest supplier of imports and its tenth biggest customer for exports. Twenty-five per cent of Australia's manufactured imports come from China; 13% of its exports are thermal coal to China.

A two-way investment relationship is also developing.

As China moves into its next phase of development, its demand will shift from raw materials to elaborately transformed manufactures, services, and expertise. Australia has some potential advantages in the supply of these, but they are not the clear advantages possessed by the resources sector. Few other countries had Australia's huge supplies of iron ore, which were close to the sea and easily developed, and proximity to China for shipping minerals (of which transport costs are

up to 10% of the value). But many developed countries have the education and technical expertise to meet China's new demands.

China as a market for our commodities

As the drivers of China's growth change from urbanisation and basic manufactured goods to domestic consumption and more complex goods and services, the growth in demand for Australia's resources will moderate. Australia's resource exports to China are likely to continue to grow, but at a slower rate, with natural gas to some extent supplanting coal. Other commodities, such as wool and wheat, and other minerals will probably also do well as incomes in China rise.

Australia's terms of trade are likely to fall as new coal, iron ore and gas capacity in both Australia and the rest of the world comes on stream. A probable result is that the Australian dollar will fall. This will mean a partial reversal of the huge rise in living standards which (contrary to popular perception) Australia has experienced in the last ten years. At the same time, it will improve the competitiveness of other traded goods and services industries which have suffered from the strength of the currency. China may be a market for some of them.

China as a market for more complex goods and services

The Chinese market for more complex goods and services will expand in two ways. First, rising wages and consumer demand will increase demand for more sophisticated manufactured goods (where Australia has some niches of excellence, for example, in medical devices) and for services such as tourism (where China is already an important market).

Second, as China moves production to more sophisticated goods and services, it will require high quality human resources, well-developed infrastructure, a well-developed financial sector and a good regulatory system. Australia has the expertise to help to develop these. Australia's public sector works very efficiently;

in a number of areas such as budgeting, health administration and social security, it is a world leader. Already, China is the biggest market for Australian education services. Australia's financial sector is well regarded internationally for its efficiency and effectiveness, and its banks are among the most sound and stable in the world. This expertise in government and services can be exported. Indeed, Australian banks are already operating in China and Australian experts have advised in a range of areas, for example, in urban development and health financing.

China as a competitor

The development of manufacturing in Asia has been a major reason for Australia's failure to compete in many areas of manufacturing. As China moves up the value chain, more industries will be subjected to this competition. This may be ameliorated by a shift in the focus of the Chinese economy away from exporting to domestic consumption.

Ninety per cent of Australia's merchandise imports are from China and, of those, 90% are elaborately-transformed manufactures. The initial imports of textiles, clothing and footwear were replaced by household appliances in the 1990s; today 50% per cent of Australian merchandise imports from China are engineering products, including office and telecommunications equipment.

Australia has niches where it can compete with the best in the world. It will be important to retain what lead it has in education and in the sophistication of the workforce.

China as an investor

Australia relies heavily on foreign investment. China ranks only ninth as an investor in Australia, with a 3% share of total foreign direct investment. That investment has grown rapidly in the past few years, but China's foreign investment is likely to fall as its savings rate falls. On the other hand, there is evidence that Chinese businesses are keen to invest in Australia, particularly in infrastructure projects.

Australian businesses have benefited from low interest rates worldwide which have been driven by the large amount of Chinese

savings available for lending, both directly to Australia, but also internationally. As these are reduced, interest rates will rise, putting downward pressure on the profits of Australian businesses, revenue and growth.

China as a destination for investment

While Chinese savings will probably remain high enough to fund domestic expansion, there will be room for Australian companies to invest in China. This would be a useful way for business to learn about Chinese tastes and preferences, as well as business culture.

One great advantage Australia has in industries providing sophisticated goods and services is the large number of Australian speakers of Mandarin. Another is the base of knowledge and contacts built up through the trade in resources.

Conclusion

The adjustment from the resources boom may be, as economist Ross Garnaut predicts, 'costly and difficult', but there are opportunities for Australia in the growing Chinese market.

In April 2013, the Australian and Chinese Governments agreed to establish a new diplomatic architecture for the relationship which would consist of an annual leaders' meeting and ministerial-level economic and foreign and strategic dialogues. This new architecture will provide an important platform for the government to progress negotiations surrounding the Free Trade Agreement, to build other trade and investment links and to resolve disputes.

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Australia and Indonesia: from good neighbours to strategic partners?

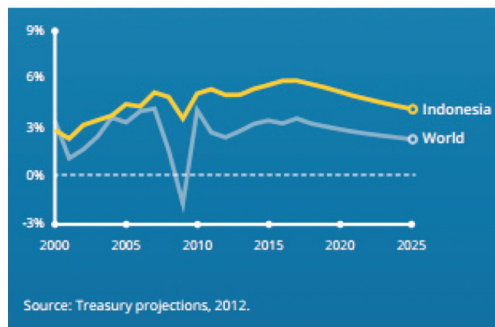
Dr Cameron Hill, Foreign Affairs, Defence and Security

KEY ISSUE

As Indonesia becomes bigger and more powerful, many argue that Australia needs to re-frame its relationship with its largest neighbour.

Australia's relationship with Indonesia remains at the centre of ongoing debates regarding our future strategic and economic prospects in the Indo-Pacific region. Australia's ability to forge a resilient 'strategic partnership' with a dynamic (Figure 1), democratic and increasingly self-confident Indonesia was a prominent feature of policy debate during the 43rd Parliament, with both major parties keen to display their credentials with regard to the bilateral relationship.

Figure 1: Indonesia and world economic growth (GDP, PPP)



Source: Department of Foreign Affairs and Trade

Significant developments: 2010–2013

The period 2010–2013 saw a continued increase in the tempo and scope of relations. The structures surrounding the relationship were strengthened through several new dialogue mechanisms:

- annual Leaders' Meeting, since 2010

- Australia-Indonesia Dialogue, since 2011 and
- annual '2+2' meeting of Foreign and Defence Ministers, since 2012.

These build on existing dialogues, such as the Australia-Indonesia Trade Ministers' Meeting.

Issues and events, however, sometimes overwhelmed formal structures. Debates over irregular maritime arrivals from Indonesia, live cattle exports, the ongoing conflict in Papua, and consular issues revived negative and populist narratives in both countries. More importantly, they demonstrated the increasingly close and complex connections between domestic and foreign policy considerations in two democratic, albeit very different, societies.

In July 2013, the Rudd Government elaborated some of these connections through its 'Indonesia Country Strategy'. This Strategy attempts to outline a long-term vision for relationship and 'identify opportunities for communities, business and government to participate in and contribute to the process of deepening and strengthening our regional engagement'. The Strategy, the first of its kind, is an explicit recognition of the centrality of Indonesia to Australia's interests, as well as an implicit acknowledgement of several important policy debates concerning the bilateral relationship.

Current policy debates

Politicians in Australia now regularly state that Indonesia is one of Australia's most important strategic partners. What this actually means in terms of Australia's foreign policy priorities and practices is, however, contested. In November 2012, former Prime Minister Paul Keating argued that, since 1996, successive Australian Governments have not fully appreciated Indonesia's strategic significance:

...policy towards our nearest, largest neighbour, Indonesia, has languished, lacking framework, judgments of

magnitude and coherence. It is as if Indonesia remains as it was before the Asian Financial Crisis—before its remarkable transition to democracy and before the re-firing of its wealth machinery.

The Labor Government was quick to reject Mr Keating's criticisms, arguing that the contemporary relationship with Indonesia was close and comprehensive. The Coalition defended its record in similar terms, and Tony Abbott made Indonesia his first overseas visit as Prime Minister.

One of the most frequent mantras surrounding the relationship is that Australia needs to be more 'consultative' with Indonesia in areas of mutual interest. One positive example of this was the agreement, in April 2013, to designate Indonesia as one of only several countries with which Australia reciprocally consults in the preparation of Defence White Papers.

The Gillard Government's mid-2011 decision, without consultation, to suspend live cattle exports to Indonesia temporarily and the Coalition's stated policy of turning back asylum-seeker vessels that originate from Indonesia (despite Jakarta's repeated objections to this policy) suggest, however, that a genuinely consultative partnership sometimes remains more rhetoric than reality.

Despite the fact that Indonesia's economy is forecast to be the world's tenth largest by 2025, bilateral trade and investment links have not matched the growth in political and security ties over the last decade.

In an effort to address this imbalance, both major parties have committed to finalising the proposed Indonesia-Australia Comprehensive Economic Partnership Agreement. This may prove challenging, at least in the short-term, given Indonesia's preference for increased protectionism over recent years and the growing domestic attraction of economic nationalism as it approaches its 2014 elections.

Injecting more ballast in the relationship, in the form of greater people-to-people links that improve mutual understanding, also remains an important objective given the misconceptions, particularly among Australians, that endure in public polling on the relationship.

There is a related concern about the ongoing decline of Australia's Indonesia 'literacy'. Both Labor and the Coalition have sought to address this decline through schemes designed to send young Australians to Indonesia, as well as other Asian countries, as part of their tertiary education, and policies to boost the study of Asian languages, including Indonesian, in schools.

Looking ahead

Indonesia's 2014 national election will see its current President, Susilo Bambang Yudhoyono, step down. The election will be a watershed, both in terms of Indonesia's democratic consolidation and the bilateral relationship. The departure of 'SBY', who has been generally accommodative of Australia's interests, is seen by some analysts as likely to make the relationship more difficult. At the least, a growing and more powerful Indonesia means that Australia will need to make sound choices about what it requests of its neighbour. In the words of the current Secretary of the Department of Defence, Dennis Richardson:

It is only a matter of time before we have a neighbour in Indonesia which has a bigger economy in nominal terms than our own. We are not used to that. As Indonesia grows wealthier and more confident it will become increasingly difficult for Australia to gain the attention of Indonesian decision makers to the extent that we think our interests might warrant. In other words, we may need to become more selective in what we push and what we ask for.

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Australia in the 'Indo-Pacific' century: rewards, risks, relationships

Dr Cameron Hill, Foreign Affairs, Defence and Security

KEY ISSUE

Navigating the 'Indo-Pacific' century will require ongoing adjustments in policies, both foreign and domestic, that will allow Australia to take advantage of new rewards and prepare for new risks. Business and civil society, as well as government, will have important roles to play in constructing strengthened relationships across the region.

The Gillard Government's October 2012 *Australia in the Asian Century White Paper* played an important role in helping focus ongoing policy debates surrounding Australia's regional engagement. The White Paper presented a framework for this engagement that spanned domestic and foreign policy reforms, as well as a range of actions across government and non-government (business, civil society) sectors.

While the Opposition criticised the White Paper as lacking 'strategic vision', it conceded that the document contained 'laudable goals and aspirations'. Indeed, the Coalition has maintained that it will enhance Australia's standing in the region by pursuing a foreign policy that is 'more Jakarta, less Geneva' and that this approach will see 'new free trade agreements concluded, existing security relationships strengthened and more people-to-people exchanges'.

'Asian', 'Asia-Pacific' or 'Indo-Pacific' century?

One of the most immediate questions raised by this debate is how Australia should conceptualise the emerging centres of power in the region and its place in these – are they best conceived of in terms of 'East Asia' (Northeast + Southeast Asia), the 'Asia-Pacific' (East Asia + Pacific + the United States), or the 'Indo-Pacific' (the Asia-Pacific + Indian Ocean states)?

Many commentators and policy makers have now shifted to using the more expansive 'Indo-Pacific' definition, recognising that:

The Indian Ocean is now surpassing the Atlantic and Pacific oceans as the world's busiest trade corridor. Rapid economic growth in South, Northeast and Southeast Asia is driving stronger economic links with the resource-rich Middle East and Africa. One-third of the world's bulk cargo and around two-thirds of global oil shipments now pass through the Indian Ocean.

Rewards

The fact that Australia and its closest neighbours are positioned at the nexus of the Indo-Pacific offers well-documented opportunities.

According to the 2012 White Paper, the (re)coupling of the major centres of global population (China and India) and the major centres of global economic growth means that 'Australian businesses and their employees can be big winners from the Asian century, with new and expanding opportunities for our miners, manufacturers, farmers and a broad range of service providers'.

...and risks

However, some analysts have argued that despite growing middle class affluence, the strategic outlook in the Indo-Pacific may be more hazardous. They have also criticised both major parties for failing to adequately prepare Australia for a 'less rosy Asia'.

Possible scenarios might involve making very hard choices about how to accommodate China's growing power, managing intensified maritime and territorial conflicts that threaten vital shipping lanes, or dealing with a new Indonesian leadership that will, potentially, be more self-confident and less positively predisposed to Australia's interests (see separate brief on Australia's relationship with Indonesia).

Relationships

The White Paper nominated five priority regional relationships for Australia—China, Japan, India, Indonesia and South Korea. In mid-2013, the Rudd Government released new Country Strategies aimed at providing a long term vision (to 2025) for each of these relationships.

Australia has also pursued a closer strategic relationship with Vietnam, a country which continues to feel the direct impact of China's growing power in the region in the form of an intensified maritime and territorial dispute in the South China Sea. Myanmar has also been a focus, as this country attempts to re-engage with the West and the broader international community as part of its recent political and economic reforms.

Beyond these bilateral relationships, it has been argued that Australia needs to have a distinct strategy to guide our emerging relationship with the Association of Southeast Asian Nations (ASEAN) because it is this grouping that 'is now widely acknowledged as a leader in developing broader regional planning and institution building'.

While highlighting the importance of government-to-government relationships, both Labor and the Coalition have also focused on building strengthened people-to-people links across the region. In the case of the Coalition, this has centred on a \$100 million 'new Colombo Plan' which will provide financial support for young Australians to study in the region. Business has also been a focus, with renewed efforts by government and the private sector to develop an 'Asia-capable' workforce able to support Australia's commercial engagement with a dynamic and ever-changing region.

Despite these new promises, neither Labor nor the Coalition has given a firm commitment regarding future resourcing for the Department of Foreign Affairs and Trade, funding for which is now at historic lows.

While the Coalition has committed to a review of Australia's diplomatic resources, it is not clear whether it will support the White Paper's (unfunded) commitment to increase Australia's representation in the region through the establishment of new diplomatic missions in China, Indonesia, Thailand, and Mongolia.

Like all areas of public policy, Australia's future regional engagement will involve important judgements and trade-offs. Given that the region did not feature prominently in the 2013 election campaign, the Government's challenge will be to convey these judgements and trade-offs to the Australian public in a clear and frank manner, explaining both the long-term rewards and the risks.

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Australia's relations with the European Union: towards a deeper regional engagement

Nina Markovic, Foreign Affairs, Defence and Security

KEY ISSUE

Australia and the European Union (EU) expanded their bilateral cooperation during the 43rd Parliament, especially in the areas of targeted development assistance, human security and environmental affairs.

In June 2013, the President of the European Commission, José Manuel Barroso, remarked during the Australian Governor-General's visit to Brussels that bilateral relations between Australia and the EU were moving to a 'much higher degree of cooperation and political alliance'. On this occasion, the Australia-EU Leadership Dialogue was launched.

Australia cooperates with the EU through a high-level institutional and sectoral dialogue, with information exchanges occurring with relevant security organisations, such as Europol. Dialogue between Australia and the EU is facilitated through: diplomatic ties, cultural and education institutions, business councils and global forums, including the United Nations and Asia-Europe Meeting (ASEM). Australia's chairing of the G20 Leaders' Summit in 2014 offers a further opportunity for advancing bilateral dialogue, especially on the provision of official development assistance (ODA) in the Asia-Pacific region.

The population of the EU is approximately 507 million across 28 countries. People-to-people links constitute the historical bedrock of Australia-EU relations. Every year, over one million EU citizens and Australians visit each other's region and about 30,000 EU citizens migrate to Australia annually. Since 70% of Australians claim European heritage, rich historical and cultural connections exist between the two regions. A shared military history is, for example, a very important aspect of Australia's relationship with several EU countries.

For over three decades, Australia has built a productive working relationship with the European Parliament, the only directly-elected EU institution. The Secretary-General of the European Parliament, Klaus Welle, visited Australia in May 2011. Official exchanges of parliamentary delegations and party meetings between like-minded Australian and EU parliamentarians take place on a regular basis. Increasing numbers of high-ranking EU officials have visited Australia in recent years, including the Presidents of the European Council and the European Commission, the EU's foreign policy chief and a large number of EU ministers.

Key areas of cooperation

Political dialogue

The 2008 Australia-EU Partnership Framework, which forms the basis for political dialogue, was updated in 2009. Guided by this document, Australia and the EU have expanded political and sectoral dialogue in education, science and research, innovation, environmental matters and nuclear energy. The Framework allowed for the broadening of consultations within the United Nations and other global forums on security issues of international importance.

In October 2011, Australia and the EU began negotiations on a treaty-level Framework Agreement. Described by Prime Minister Rudd as a 'significant milestone in the Australia-EU relationship', the EU's High Representative for Foreign Affairs and Security Policy noted that the proposed agreement 'provides a firm basis for expanding our practical collaboration in areas such as foreign affairs and security, ODA, climate change, research, science and education'. Negotiations are ongoing and it is likely that the agreement will necessitate legislative scrutiny and ratification from both Parliaments.

Trade in goods and services

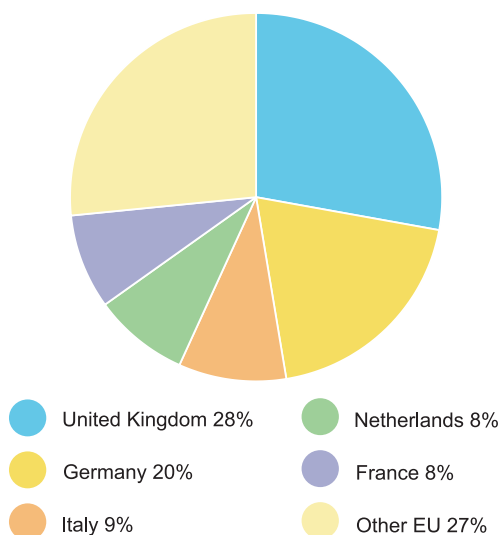
Trade and investment are pivotal aspects of the bilateral relationship. The EU is among

Australia's most significant economic partners and the largest single source of Foreign Direct Investment (FDI).

In 2012, the value of trade in goods and services between Australia and the EU was \$81.6 billion. The EU accounted for 13.2% of Australia's total trade in goods and services. The balance of trade on goods and services with Europe recorded a deficit of \$34.4 billion.

Key imports from the EU included medicinal substances, passenger motor vehicles and civil engineering equipment. Australia's main exports to the EU were gold, coal and agricultural products. The graph below shows Australia's main individual trading partners from the EU in 2012, the largest being the United Kingdom.

Australia's main trading partners in the EU, 2012



Source: Department of Foreign Affairs and Trade

The EU and Australia are also promoting closer collaboration in the education sector (including joint degrees), as well as jointly funded science and research projects. In 2009, the European Commission became a founding member of the Global Carbon Capture and Storage Institute in Melbourne. In 2011, both parties agreed to explore linking carbon pricing mechanisms for greenhouse gas emissions. These discussions continue.

Agricultural matters

In December 2008, Australia and the EU signed a new agreement on trade in wine. This agreement, which came into force in September

2010, is particularly significant for Australian exporters, as Europe is the biggest market for Australian wine.

The 2008 agreement replaces a 1994 arrangement; it is intended to protect the 'geographical indicators' of both parties on the basis of non-discrimination and reciprocity. As a result, Australian wine producers are no longer able to sell products labelled as 'champagne' or 'sherry', for example, whilst Australia has obtained protection for over 100 of its own geographical indicators.

Many European regional foods are also protected under EU law by geographical indication, designation of origin or under traditional speciality (such as feta cheese). Australia is therefore likely to be involved in further negotiations on any agreement covering agricultural products.

Development cooperation

In 2011, Australia and the EU established mechanisms of delegated cooperation arrangements for aid delivery. Under exploratory arrangements, the EU has agreed to deliver Australian aid to South Sudan, while Australia agreed to deliver a component of the EU's assistance to Fiji. The Pacific headquarters in Sydney of the European Investment Bank has facilitated trilateral dialogue between Australia, the EU and a third recipient country in the region.

Following the 2013 federal election, the presidents of the European Council and the European Commission issued a joint statement which noted:

Australia and the European Union, as like-minded partners, share an increasing political dialogue. Our cooperation on foreign and security policy, as well as on economic and development policies and on climate change, contributes significantly to addressing global challenges. The conclusion of negotiations on the Framework Agreement will make our partnership stronger, more comprehensive, and effective.

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Official Development Assistance: Australia's aid program

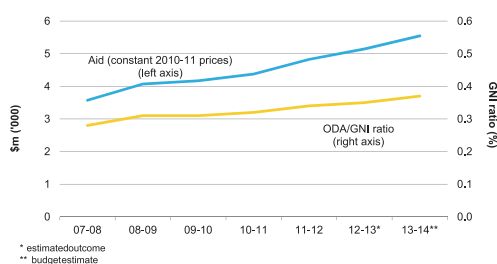
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KEY ISSUE

Australia's Official Development Assistance (ODA) has increased consistently in real terms during the past few years. This trend may not continue.

Australia's ODA has witnessed a consistent increase over the past six years, increasing from 0.28% of Gross National Income (GNI) in 2007–08 to an estimated 0.37% in 2013–14. The graph below illustrates this trend.

Figure 1: ODA growth 2007-08 to 2013-14



Source: Parliamentary Library

The budgeted outlay on Australia's International Development Assistance Program 2013–14 is estimated at \$5.7 billion at current prices, an ODA/GNI ratio of 0.37%. The 2013–14 Budget's statement on aid noted that 'the Government expects to increase Australian aid to around 0.39 per cent in 2014–15, 0.41 per cent in 2015–16 and 0.45 per cent in 2016–17'.

The Department of Immigration and Citizenship (DIAC) will manage the largest amount of Other Government Departments (OGD) expenditure – \$436.2 million in 2013–14. This includes up to \$375.0 million for 'costs associated with the sustenance of asylum seekers on residence determinations or bridging visas class E during their first 12 months in Australia'.

On 17 December 2012, Foreign Minister Bob Carr announced that the Government would

report up to \$375 million of its aid budget as support for asylum seekers waiting to have their claims heard in Australia. In effect this meant that \$375.1 million would be diverted to DIAC from the overall aid budget for 2012–13.

Additional aid to PNG

On 18 July 2013, the prime ministers of Australia and PNG signed a 'Joint understanding between Australia and Papua New Guinea on further bilateral cooperation on health, education and law and order'.

The Australian Government's Economic Statement in August 2013 included details of this additional ODA to PNG, which amounts to \$420 million over four years:

- health (\$207 million over four years)
- education (\$62 million over four years)
- justice (\$19 million over four years)
- transport (\$0.8 million over four years) and
- law and order (\$132 million).

The August 2013 Economic Statement

The August 2013 Economic Statement announced that the ODA growth would be slowed, but the target of 0.5% of GNI by 2017–18 would still be met. The measure was 'expected to decrease payments by \$879 million over the four years to 2016–17' but the aid budget would 'increase by around 26% over this period'.

Coalition policy

On 5 September 2013, the Coalition released its policy on foreign affairs that included foreign aid. While the Coalition remains committed to the 0.5% of GNI target, the policy states that 'it is not possible to commit to a date', and that growth in ODA will be restricted 'to increases in the consumer price index over the forward estimates'. This amounts to a \$4.5 billion reduction in Australia's planned aid budget in the forward estimates, including an immediate cut of \$656 million.

According to analysis by Stephen Howes from the Development Policy Centre at the Australian National University:

... adjusting for inflation, aid in 2015–16 will be \$5.6 billion (in 2011–12 prices) which is back to its 2012–13 level. As a percentage of GNI, aid will decline from .35% of GNI in 2012–13 to .32% of GNI in 2016–17, its lowest level since 2000–01. This makes it hard to take seriously any statement that the Coalition is still committed to 0.5% ... The cuts also imply \$656 million being taken from the aid budget this current year.

The Coalition's policy also emphasises that it will 'review the priorities within the existing foreign aid budget to consolidate our aid efforts on the Asia Pacific-Indian Ocean region and to focus on the quality and rigorous administration of that effort'. It should be pointed out that the existing top five bilateral recipients of Australian aid in 2013–14 are all from the Asia-Pacific region, to which 86% of Australian aid is currently provided.

Non-government organisation (NGO) reactions to the Coalition's policy

NGO reactions to the Coalition's policy announcement on aid have been unanimous and predictably negative.

The Australia Council for International Development, Australia's peak body for not-for-profit overseas aid and humanitarian agencies, expressed 'shock and distress' at the Coalition's proposed cut to the ODA budget.

Criticising both major political parties, Oxfam Australia's Chief Executive, Helen Szoke, said:

The aid budget is Australia's commitment to the world's poor and vulnerable, and is not an ATM for political parties in search of cash to prop up their bottom line.

World Vision Australia's Chief Executive Officer, Tim Costello, described the Coalition's decision as 'a tragedy for the world's poorest people' and 'truly devastating'.

UNICEF Australia's Chief Executive Officer, Norman Gillespie, said the 'costings are at the expense of children's lives'.

In its Social Justice Statement 2013–14, the Australian Catholic Bishops Conference called on Australia to do more to alleviate poverty in the region.

Referring to Australia's seat on the United Nations Security Council and Australia's hosting of the G20 Summit in 2014, the Chairman of the Australian Catholic Social Justice Council, Christopher Saunders stated:

Our nation has a historic opportunity to be a force for peace and generosity. The government's proposal to cut \$4.5 billion from the forward estimates for foreign aid represents a serious departure from Australia's commitment.

New administrative arrangements

On 18 September 2013, Prime Minister Abbott announced that he intended to integrate the Australian Agency for International Development (AusAID) into the Department of Foreign Affairs and Trade, thus 'enabling the aid and diplomatic arms of Australia's international policy agenda to be more closely aligned'.

This move attracted more criticism than it did support. As Annmaree O'Keeffe, Lowy Institute Fellow and former AusAID Deputy Director-General, observed:

... the temptation to use AusAID as a diplomatic ATM will be greater than ever. And the cost won't be registered against the Foreign Affairs budget or DFAT's reputation but against the effectiveness of the development program and the contribution it has made as one of Australia's most potent soft power tools.

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Defence: strategic policy and procurement

David Watt, Foreign Affairs, Defence and Security Section

KEY ISSUE

There is an ongoing tension in the history of Australian Defence White Papers between capability needs and the financial means required to pay for them. This has been particularly true in the post-global financial crisis world and will remain an issue of importance for the new government.

Ends and means

During the life of the 44th Parliament the Department of Defence will take possession of a number of major defence capabilities including the Canberra Class Landing Helicopter Docks (LHDs), the Hobart Class Air Warfare Destroyers (AWDs), the Growler variant of the F/A-18F Super Hornet and the first two of Australia's F-35 Joint Strike Fighters. The Government will also make decisions regarding a number of other defence acquisitions including the replacement for the Collins Class submarines.

The planning, development and funding of projects of this magnitude can take decades and requires long term commitment. Inevitably this puts significant pressure on governments to properly fund defence acquisition across a much longer time scale than the regular four-year budgetary cycle.

White papers: guidance or wish lists?

Australian governments have set out defence policy in a series of White Papers containing analysis on Australia's strategic situation and the defence needs which flow from it.

2000

The Howard Government's Defence 2000: Our Future Defence Force (the 2000 Defence White Paper; DWP) set out three guiding principles:

- self-reliance—Australia had to be able to defend itself from direct military attack 'without relying on the combat forces of other countries'
- a maritime strategy—'to control the air and sea approaches to our continent' and
- proactive operations which, if necessary would 'seek to attack hostile forces as far from our shores as possible'.

These principles, alongside an assessment of Australia's strategic environment, would help determine future capability choices, an appropriate ADF structure and an industry policy designed to underpin the identified capability needs. Defence 2000 also set out a funding plan for the next decade and synchronised with the publication of the first Defence Capability Plan.

Significant capability choices included a new Armed Reconnaissance Helicopter (the Tiger ARH), an additional squadron of troop-lift helicopters (a role eventually fulfilled by the MRH-90), a replacement for the de Havilland Canada Caribou and the acquisition of up to 100 new combat aircraft to replace both the F/A-18 and F-111 fighter aircraft. The 2000 DWP also noted the need for what will be the Air Warfare Destroyers, and replacements for the Royal Australian Navy's (RAN) supply ships HMAS Westralia and HMAS Success. Some of these projects have been delivered, some have suffered serious delays and some will come to fruition in the coming years—but all require long-term funding.

Defence 2000 provided a total cost for the capability enhancements contained therein (\$21 billion) and described a funding model to enable their fulfilment. The Government committed to increase spending by 3% annually in real terms, as measured by reference to the Non-Farm GDP Implicit Price

Deflator. The problem with this was (and is) that, in general, military costs increase faster than the rate of inflation. In 2010, the Australian Strategic Policy Institute (ASPI) estimated that in order for Australia to substantially improve its defence capabilities, a minimum of 3.1% annual growth in the Defence budget would be required. Even during the decade of the 2000 DWP, the cost of maintaining ageing aircraft was rising annually by 7%, well ahead of the Government's GDP growth prediction. Although the Howard Government grew defence spending by an average of 3.7% during the rest of its time in office, it also greatly expanded the list of required capabilities.

2009

By the time the Rudd Government released its Defence White Paper, *Defending Australia in the Asia Pacific Century: Force 2030*, the global strategic situation had undergone a substantial transformation. This was primarily due to the post 9/11 'war on terror' and the economic impact of the 2008 Global Financial Crisis (GFC). However, the 2009 DWP largely repeated the same key strategic objectives as the 2000 DWP.

At a conceptual level the 2009 DWP emphasised that Australia must be able to act with a degree of independence, and accordingly, its capability choices were comprehensive.

Given the similar objectives and the long time frames necessary for the delivery of complex capabilities, it is unsurprising that the 2009 DWP repeated many of the capability requirements of its 2000 predecessor. However, it also added some new and substantial requirements. In particular, it called for the acquisition of 12 submarines to replace the six Collins Class and new frigates to replace the Anzac Class; naval combat helicopters (a serious capability gap following the failure of the Super Seasprite project); as well as deciding the F-35 Joint Strike Fighter would replace the F/A-18 Hornets and the venerable F-111s.

Paying for such an extensive list (the cost of which Defence put at more than \$200 billion) would prove to be a difficult task. The 2009 DWP contains a more complicated formula

than its predecessor: 3% real growth to 2017–18, and 2.2% real growth from 2018–19 to 2030. Funding would also move to 2.5% fixed indexation (instead of continuing to use the Non-Farm GDP Implicit Price Deflator). However, the impact of the GFC required the Rudd and Gillard Governments to make difficult choices about expenditure and Defence was not granted the funding levels expected in 2009.

2013

Given the new economic circumstances, it is unsurprising that the 2013 Defence White Paper takes a more circumspect approach to funding defence acquisition. The 2013 DWP repeats almost all of the 2009 capability choices but uses a funding model which only spans the four-year forward estimates cycle and then provides six-year 'funding guidance'. While the Government added significant additional funding to Defence in the 2013–14 Budget this does not resolve the tension between the extensive capability plans and the cautious approach to funding.

The next defence white paper

The Coalition has committed to producing a new Defence White Paper within 18 months, which will have 'an alignment of the government's defence policy with a clear military strategy and an affordable ADF structure designed to achieve that policy'. How the new Government reconciles Australia's defence needs with its financial means will be a key test for the success of the new White Paper—and the Government.

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Afghanistan: drawdown and future prospects

Dr Nathan Church, Foreign Affairs, Defence and Security

KEY ISSUE

Although their combat mission in Afghanistan will soon be concluded, Australian Defence Force (ADF) personnel will probably have a presence there beyond 2014, predominantly in training and mentoring. However, the ADF will ultimately follow the United States' (US) lead in Afghanistan—which is critically dependent on the political relationship between the US and the fledgling Afghan Government.

Australia's changing role

The ADF's incremental transition in Afghanistan has evolved through both political and military initiatives. Key summits in Lisbon, Bonn and Chicago have facilitated resolutions regarding the International Security Assistance Force (ISAF) mission in Afghanistan and have generated a strategic framework for transition to Afghan-led security arrangements.

A key requirement for all these plans has been the transformation of the Afghan National Security Forces (ANSF) into a legitimate and credible security force. Although this has been slow, uneven, and at times significantly challenging – particularly with the instances of 'insider threats' against ADF personnel – there has been a demonstrable improvement in the quality of the ANSF.

Accordingly, the ANSF began taking the lead for security in Uruzgan province in July 2012 and by the end of that year the Afghan National Army's (ANA) 4th Brigade took charge of operational bases and was conducting independent patrols. Australia's main operational hub in Tarin Kowt will be closed at the end of 2013, which will signal the end of Australia's combat role in Afghanistan. At that time more than 1,000 ADF personnel will return to Australia, with the remainder (including a Special Forces contingent) to continue training the ANSF and building their capabilities throughout 2014.

Future commitments

The ISAF mission has fundamentally sought to achieve the conditions where Afghanistan is never again a safe-haven for international terrorism. Although ISAF will no longer have an operational mandate to influence this post-2014, many of its contributing nations – including Australia – have pledged ongoing commitments to train and finance the ANSF to reinforce the gains made so far.

On 5 June 2013, Defence Ministers from ISAF-contributing nations endorsed a future framework for training, advising and assisting the ANSF post-2014. This training mission will be 'significantly' smaller than the existing ISAF force and its regional focus will prioritise enabling national institutions and up-skilling senior commanders. The United States, Germany and Italy are likely to be significant contributors to this training mission, while an Australian contingent will, at a minimum, probably include trainers at the Kabul-based ANA officer training academy.

Also in June 2013, Australia's Defence Minister Stephen Smith indicated that Australia would provide \$100 million annually for three years to support the ANSF, starting in 2015. This funding would complement other nations' contributions, amounting to more than \$13 billion over three years, most of which will come from the United States. However, there is a strong expectation that Afghanistan will increasingly fund its own security forces, and by 2024 that it will do so independently of external support.

Potential risks and challenges

Despite Australia's best intentions, the correlation between its proposed commitments in Afghanistan and the reality that will play out on the ground remains a great unknown. The destabilising effects of the Taliban remain a very real concern in the short-to-medium term. However, the larger strategic challenge will surely be the crucial political relationship between the United States and Afghanistan.

The US will require a bilateral security deal with Afghanistan in order to maintain its presence there. However, this is a problematic challenge fraught with many potential obstacles, including the political uncertainty internally within Afghanistan and the contentious issue of negotiating with the Taliban. The US was unable to secure a similar deal following the conclusion of combat operations in Iraq, and while the two scenarios are far from identical, it does highlight the innate difficulty in such negotiations where Afghan and American expectations are not likely to always align.

As a US ally, Australia will necessarily wait on the eventual outcome of any Afghan-US deal in order to gauge the extent of any potential post-2014 involvement in Afghanistan. For example, in June 2013 the Australian Defence Minister signalled the possibility of a Special Forces role post-2014 if there were a required mandate, but this would again be contingent on the willingness and legal authority of other partners, especially the United States, to do similar.

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Mental health of military personnel and veterans

Nicole Brangwin, Foreign Affairs, Defence and Security

KEY ISSUE

The prioritisation and implementation of mental health strategies has become a critical issue for the Australian Defence Force (ADF) and the Department of Veterans' Affairs (DVA).

Attempts to de-stigmatise and appropriately address mental health issues in the military and veteran communities have been given greater priority over the last decade. Concerns surround the ADF's recent high operational tempo and the number of personnel who have experienced multiple operational deployments.

But how critical is the situation? DVA's Deputy President, Shane Carmody, told the online journal Crikey that he is not sure there will be a 'tsunami' effect, but incidents of anxiety, post-trauma stress and alcohol abuse are on the rise, particularly among younger veterans.

Mental health initiatives and studies

A significant focus on mental health issues in the military and veteran communities began in the early 2000s when DVA launched its Towards Better Mental Health for the Veteran Community in 2001 and the ADF launched its Mental Health Strategy (MHS), Work Well, Live Well, Be Well, in 2002. Both strategies were developed from the broader National Mental Health Strategy.

DVA's approach sought to incorporate a broader understanding of mental health issues, as part of veterans' overall health care needs, in an effort to provide better services to the veteran community.

The ADF's MHS predominantly aimed to raise awareness about suicide prevention, alcohol management and post-trauma stress. The MHS was established following a recommendation from the Australian Defence Force health status report (August 2000).

The 2002 MHS was reviewed by Professor David Dunt in January 2009 as part of the Review of Mental Health Care in the ADF and Transition Through Discharge. Dunt noted that while the 2002 MHS was far-sighted and in some respects, more developed than other countries' military mental health care initiatives, the roll-out of the MHS had been patchy and underfunded in other respects.

Over the last few years, numerous studies have been undertaken and initiatives put in place to provide military members and veterans with appropriate access and tools to assist in improving mental health and wellbeing. Regardless of study outcomes, initiatives and strategies, the greatest challenge still needs to be overcome—the stigma attached to mental disorders.

One of the more recent studies undertaken into mental health in the military, the 2010 ADF Mental Health Prevalence and Wellbeing Study (2010 study), interviewed up to 49% of ADF members and reported that within a 12 month period:

- 17.9% of 'ADF members sought help for stress, emotional, mental health or family problems'
- 27.6% were concerned that reporting a mental disorder might result in being treated differently
- 26.9% feared their career might be harmed and
- 36.9% stated the 'highest rated barrier to seeking help was concern it would reduce deployability.'

While the key findings showed the prevalence of mental disorders in the ADF is similar to rates encountered in the general Australian population, the 'profiles of specific disorders' varied.

Of the 22% of ADF members who 'experienced a mental disorder', anxiety disorders rated highest, particularly among female members. Male members reported a higher rate of affective (mood) disorders, such as 'depressive episodes',

than the general population. Alcohol disorders for both males and females were much lower in the ADF than the general community.

At the time the study was conducted, around 43% of ADF members had been deployed multiple times, 19% deployed on one occasion and 39% had never deployed. Although the study did not find that deployed personnel were any more likely to suffer mental disorders than those who had not deployed, it did find that respondents who had deployed were 10% 'more likely to seek care for mental health or family problems'. The 2010 study did suggest a trend in 'greater levels of traumatic symptomatology with each trauma or combat exposure on deployments', but further studies should be undertaken.

The 2010 study considered the rates of suicidality (instances where suicide is being contemplated and/or a suicide attempt is being planned) in the ADF over a 12-month period and found them to be more than double the general population: 4.0% in the ADF as opposed to 1.8% of the general population. However, the study found that the number of suicide attempts in the ADF was similar to that of the general population: 0.4% in the ADF compared to 0.3% of the general population. The number of actual suicide fatalities in the ADF was also reportedly lower than in the general population, but figures were not provided in this study. The study suggested that the suicide prevention strategies implemented by the ADF may have reduced the number of suicides.

Initiatives for serving members

In October 2011, findings from the 2010 study (previously discussed) led to the release of the ADF Mental Health and Wellbeing Strategy. The strategy seeks to improve a number of priority areas including mental health screening, peer support, service delivery and access to care. The implementation of the strategy is guided by the ADF Mental Health and Wellbeing Action Plan 2012–2015. Defence might be called upon to provide updates to Parliament on the progress of these initiatives, particularly the ADF Suicide Prevention Program.

Initiatives for veterans

In 2001, DVA launched its mental health strategy, *Towards Better Mental Health for the Veteran Community*. At that time, 22% of DVA's treatment population of 350,000 (around 73,000 veterans) 'received some form of mental health treatment within any given year'.

As at March 2013, around 148,700 veterans with service-related disabilities were being supported by DVA and of these, up to 46,400 had 'an accepted mental health disorder'. Common conditions include anxiety disorder, depression, stress disorder and alcohol dependence.

On 27 May 2013, the *Veteran Mental Health Strategy (VMHS)* was released by the Labor Government. The strategy pledged to provide 'a ten year framework for mental health care in support of current and future veterans and their families'. The 2013–14 Budget committed \$26 million over four years towards the VMHS, commencing in July 2014. The VMHS includes the families, carers and organisations that support veterans in its definition of 'veteran and ex-service community'.

DVA is developing an action plan to guide the implementation of the VMHS. The plan may be subject to updates over the next ten years.

Further reading

ADF Mental Health Reform Program website includes links to the 2010 ADF mental health prevalence and wellbeing study and the three Middle East Area of Operations (MEAO) health study reports.

Department of Veterans' Affairs (DVA), *Veteran mental health strategy: a ten year framework 2013–2023*, DVA, 27 May 2013.

Asylum seekers and the Refugee Convention

Harriet Spinks, Social Policy and Ian McCluskey, Law and Bills Digest

KEY ISSUE

Increasing numbers of asylum seekers arriving by boat has led to stronger deterrence policies by both major parties but many complex considerations remain.

Australia's humanitarian program

Australia maintains a humanitarian program comprised of two parts. Under the offshore component, refugees and others in humanitarian need are resettled in Australia from overseas. Under the onshore component, people already in Australia may apply for protection and, if successful, be granted a permanent visa. The total number of visas granted annually under both components was steady at around 13,000 for many years, but in 2012–13 it was increased to 20,000.

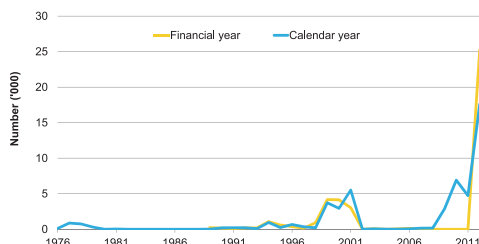
Increasing numbers of asylum seekers arriving unauthorised by boat (irregular maritime arrivals, or IMAs) have led to much public and political debate concerning the make-up of the humanitarian program. In 2011 – 12, for the first time more visas were granted in the onshore component of the program than the offshore component.

Responding to irregular maritime arrivals

In 2012, 17,202 asylum seekers arrived in Australia by boat. While this number is low compared to many other countries, it is a significant increase from the 2,726 arrivals in 2009 and the 161 arrivals in 2008 (see Figure 1).

The Coalition has consistently maintained that boat arrivals have increased due to Labor Government policy changes, which it argues encouraged people to attempt to reach Australia this way. These changes included winding back some of the deterrence measures created by the Howard Government, such as ending offshore processing (the 'Pacific Solution'), and abolishing temporary protection visas (TPVs).

Figure 1: IMAs by calendar year 1979 to 2012 and financial year 1989-90 to 2012-13



Source: Parliamentary Library, Canberra 2013.

The first Rudd Government initially argued that numbers were increasing due to changes in 'push factors', such as increased global conflict, rather than 'pull factors', such as domestic policy changes. This argument was supported by the fact that Australia was not alone in seeing increasing numbers of arrivals. Arrivals increased across many destination countries in the same period. Labor recently acknowledged however, that it was slow to respond to increasing arrivals, and that an earlier return to tougher policies could have helped to reduce them.

In 2011, an attempt to transfer IMAs to Malaysia in exchange for resettling increased numbers of refugees out of Malaysia was prevented by the High Court, which found the arrangement was invalid. In 2012, following months of political deadlock, the Government created an expert panel on asylum seekers. This panel was charged with recommending policy measures to reduce the number of IMAs. The Government implemented a suite of measures in line with the panel's recommendations which were aimed at removing incentives for asylum seekers to travel to Australia by boat. The most significant of these was the reinstatement of offshore processing in Nauru and Papua New Guinea (PNG) in August 2012.

In July 2013, the second Rudd Government announced that IMAs would not only be processed in Nauru and PNG, but they would also be resettled there (or in a third country) should their asylum claim be successful. No IMA arriving after 19 July 2013 would be settled in Australia.

Offshore processing has been strongly criticised by refugee and human rights advocates, as well as the Australian Greens. The primary concerns of these groups relate to the adequacy of facilities in Nauru and PNG where centres lack suitable accommodation, health care and recreational facilities. There are further concerns over the feasibility of resettling refugees in small developing nations. Additionally, it may take many years for people to be processed and resettled. Critics also argue that offshore processing places Australia in breach of its international obligations.

The Refugee Convention

Australia is a party to the 1951 Convention relating to the Status of Refugees and its 1967 Protocol, which defines a refugee as a person who has a well-founded fear of persecution for reasons of race, religion, nationality, membership of a particular social group or political opinion.

The primary obligation under the Convention is that of non-refoulement – that is, refugees must not be expelled or returned to places where they would face persecution based on one or more Convention grounds. This covers both the refugee's country of origin and third countries. Given practical difficulties in both the processing and settlement of refugees in Nauru and PNG and concerns over the rigour of their refugee status determination processes, it has been argued that offshore processing could amount to refoulement.

In addition, it has been argued that offshore processing may constitute a penalty in breach of Article 31 of the Convention, which prohibits imposing penalties based on a refugee's mode of arrival. Similarly, it could amount to expulsion in breach of Article 32, which provides that refugees shall not be expelled save on grounds of national security or defence.

Future outlook

It is too early to say if arrangements with Nauru and PNG have had the desired effect of reducing arrivals, especially in light of growing humanitarian crises around the world. While the Labor Government pointed to the fact that arrivals in August 2013 were significantly

lower than in July 2013, it is uncertain whether this was indicative of a long-term trend. What is certain, however, is that issues concerning asylum seekers arriving by boat will continue to be of significance to the new Parliament.

A legal challenge to offshore processing has commenced in the High Court, with lawyers for an Iranian asylum seeker on Manus Island seeking to have the declaration of PNG as an offshore processing country under the Migration Act set aside. The case will argue that offshore processing is unconstitutional and places Australia in breach of its international obligations. A decision in the plaintiff's favour would have far-reaching implications for asylum policy in Australia.

While the Coalition supports offshore processing, it is sceptical about the prospects for permanent resettlement of successful asylum seekers in Nauru and PNG. It has been critical of the Labor Government for not putting in place measures to resolve the backlog of IMAs who arrived prior to the introduction of the new offshore processing arrangements.

Coalition policies for reducing IMAs include: ramping up border protection measures, reintroducing TPVs and turning back boats – 'where it is safe to do so'. The Coalition has indicated that under its leadership details of boat arrivals may not be made public, which would reduce the level of scrutiny in this contentious policy area. While many of these measures will not require legislative change, they are issues which will nonetheless need careful attention by the Parliament.

Further reading

J Phillips and H Spinks, *Boat arrivals in Australia since 1976*, Background note, Parliamentary Library, Canberra, updated 23 July 2013.

J Phillips, *Asylum seekers and refugees: what are the facts?*, Background note, Parliamentary Library, Canberra, updated 11 February 2013.

R de Boer, *Health care for asylum seekers on Nauru and Manus Island*, Background note, Parliamentary Library, Canberra, 28 June 2013.

