
# HOUSE OF REPRESENTATIVES

## STANDING COMMITTEE ON BANKING, FINANCE AND PUBLIC ADMINISTRATION

**Reference: Aspects of the national competition policy reform package**

**CANBERRA**

**Thursday, 23 November 1995**

(OFFICIAL HANSARD REPORT)

**CANBERRA**

HOUSE OF REPRESENTATIVES
STANDING COMMITTEE ON FINANCIAL INSTITUTIONS AND PUBLIC ADMINISTRATION

Members:

Mr Hawker (Chair)

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| Mr Albanese | Mr McMullan |
| Mr Anthony | Mr Mutch |
| Mrs Bailey | Dr Nelson |
| Mr Causley | Mr Pyne |
| Mrs Gallus | Mr Willis |
| Mr Hockey | Mr Wilton |
| Mr Latham | |

Matter referred to the Committee:

The aspects of the national competition policy reform package. The major issues the Committee has been requested to inquire into are:

(1) the appropriate means, including review processes, for applying the 'public interest' tests included in the Competition Principles Agreement:

These tests are a critical feature of this Agreement. They are described in Principle 1(3), which provides that:

without limiting the matters that may be taken into account, where this Agreement calls:

(a) for the benefits of a particular policy or course of action to be balanced against the costs of the policy or course of action; or

(b) for the merits or appropriateness of a particular policy or course of action to be determined; or

(c) for an assessment of the most effective means of achieving a policy objective;

the following matters shall, where relevant, be taken into account:

(d) government legislation and policies relating to ecologically sustainable development;

(e) social welfare and equity considerations, including community service obligations;

(f) government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;

(g) economic and regional development, including employment and investment growth;

(h) the interests of consumers generally or of a class of consumers;

(i) the competitiveness of Australian businesses; and

(j) the efficient allocation of resources.

(2) the impact of competition policy reform on the efficient delivery of community service obligations including an assessment of:

(a) existing government policies relating to community service obligations and

(b) options for the delivery and funding of these services;

(3) the implications of competition policy reform for the efficient delivery of services by local government, including arrangements that have been developed between State Governments and local government authorities for the implementation of the Competition Principles Agreement.

## WITNESSES

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON BANKING, FINANCE AND PUBLIC ADMINISTRATION

(Subcommittee)

*Aspects of the national competition policy reform package*

CANBERRA

Thursday, 23 November 1995

Present

Mr Simmons (Chair)

Mr Martyn Evans — Mr Thomson

Other committee members

Mr Bradford — Mr Braithwaite

The subcommittee met at 10.46 a.m.

Mr Simmons took the chair.

**DAVIS, Mr Robert Brent, Director, Trade and Policy Research, Australian Chamber of Commerce and Industry, PO Box E14, Queen Victoria Terrace, Canberra, Australian Capital Territory 2600**

**CHAIR**—Welcome. The evidence that is given here today is considered to be part of the proceedings of the parliament and, accordingly, I advise that any attempt to mislead the committee is a very serious matter and could amount to a contempt of the parliament.

The inquiry is now in full swing, with four hearings conducted and more than fifty submissions received. As well, members of the committee have travelled extensively to hold informal discussions with local government bodies in rural and non-metropolitan areas of New South Wales and Queensland. A major issue emerging from the submissions, hearings, and meetings has been community service obligations—their definition, identification, funding and delivery, and the oversight of performance and accountability of CSO providers. The committee has heard the views of community organisations and local government on the subject and today looks forward to hearing the perspective of the business sector.

The committee has received the submission from the ACCI and it has been authorised for publication. Before we begin our questions, I invite you to make an opening statement.

**Mr Davis**—Part of the responsibilities of the ACCI covers our economics work, which includes national competition policy. National competition policy has been a matter of great importance to the chamber as part of our work on micro-economic reform. We are very pleased to see that it is an issue that is being embraced with great support by both sides of the political process in Canberra. We are very pleased to have seen the legislation passed before the end of the last financial year and now look forward to the many challenges of putting it in place.

The chamber has had a long involvement in the process. We made an extensive submission to the original Hilmer inquiry. We made two extensive commentaries on the various packages when they came out, and we have had a great many meetings with the Treasury, the Prime Minister's department and many people in Parliament House involved in the process.

Our interest in this inquiry very much comes back, as you said in the outset, to the question of community service obligations. Let me just state our position very simply. We have no problem with governments providing CSOs. Our concerns come down to how they are provided and the accountability of that process. We believe that there is a significant gap between best practice in providing CSOs and how they are currently provided, partly by the federal government, but probably more importantly by the sub-national governments, especially at the state level where there is, again, a variety of performance.

We believe the current New South Wales government—an initiative of former premier Greiner, and I think it was carried forward by Mr Fahey and now by Mr Carr, so there is bipartisan support—is a model which warrants consideration by the federal government, the other state and territory governments and the local governments. In many respects, the reforms that we are proposing to the CSO provision processes in this country reflect the initiatives and the practices of the New South Wales government.

In simple terms, we believe that CSOs are the prerogative of governments to provide. They should be provided quite simply by a line entry or line entries of the relevant minister rather than basically overcharging one group of consumers, which more often than not is business, and undercharging another group of users, which more often than not is householders.

We do not see any particular reason that all CSOs have to be provided by the public sector. There is a possibility under competitive tendering arrangements that a government may wish to provide a CSO, open it to a competitive tender and the private sector may well provide it. The critical determinant in our mind is having the CSO provided in the most efficient and cost-effective way for the taxpayer, regardless of who

provides it. We think many of the elements of the new national competition policy, especially access to essential facilities and the structural reform of the public sector monopolies, will encourage governments to go that track.

**CHAIR**—You mentioned the example in New South Wales. I am wondering if you might state the essential elements of that model for the benefit of the committee.

**Mr Davis**—About seven or eight years ago the then Greiner government looked at the question of CSOs and how they were provided. Before that, they were generally provided in the more conventional way in that basically a government business enterprise was directed by its minister to provide a community service obligation to one or other group in the community. The GBE then had to go away and work out how it did it, what the objectives were to be, and then put it in place.

There were generally two options that they could exercise. One was basically to undercharge one group, more often than not householders and consumers, and overcharge another group, generally business users. The other option that tended to be used was that of basically accepting a lower rate of return on an asset. With some of the more capital intensive industries such as electricity, water, sewerage, and so on, the rate of return was below what would be expected in a comparable private sector enterprise.

The Greiner government initiated a package of reforms which quite simply said that, if the government wanted a community service obligation to be provided, the line minister—in the case of railways, the transport minister—would have a line entry in his budget saying, 'This year it will cost us X hundred million dollars to have this done.' There was a ministerial statement to the parliament about what was expected and there was a very transparent process, sometimes even contracts between senior management of the agency with the line minister. That situation has worked reasonably well. It is not fully developed and there is an incremental process still in place. No one expected one arrangement to cease on the Sunday and the new arrangement to begin on the Monday. Our understanding was that it was a three-year rolling program, which, we think, for most elements of the New South Wales system, especially the transport system, comes to an end reasonably soon. So there was a phased transition rather than a quantum leap exercise. We are aware that Mr Fahey continued it as a matter of policy. We are not aware that Mr Carr has got any intention of changing policy.

**CHAIR**—Given the New South Wales government's decision to split up Pacific Power, would the ACCI see that as a continuing sign of micro-economic reform at the state level in line with the previous decisions of Premier Fahey and Premier Greiner?

**Mr Davis**—Are you talking about electricity reform or CSOs here, Chairman?

**CHAIR**—I suppose essentially the issue of micro-economic reform, in the first instance.

**Mr Davis**—We have got an extensive background in electricity reform. We are part of the market steering committee actually guiding the break-up of many of the systems in the new national framework. You would appreciate we are bound under some rules of confidentiality there. What Mr Carr has done in New South Wales is consistent with the national competitive market. The two plus one option that he has outlined—that is the two large groupings plus Eraring on its own, potentially joined to the Queensland system—is certainly a step in the right direction. We probably would have liked to have seen them go more to a five or six option but, again, it is a step in the right direction, of course, and it is not final. They can go steps further.

The question that really remains in New South Wales is when do they connect with Queensland. I know that is subject to another inquiry in this place. I think we will be getting a call for that reasonably soon. We will express views about joining the two systems. I think what Mr Carr has done is a positive development and hopefully he can be encouraged to go a little bit further. If there is a change of government

then similarly, when it is Mr Collins's turn, he may be encouraged equally to go one step further.

**CHAIR**—What about then in the case of Victoria where there has been extensive micro-economic reform? Has that been operating in a similar way to the New South Wales model with respect to the delivery of CSOs? Perhaps if I could use the example of the distribution system which has actually been sold to the private sector. I understand that implicit in that sale to the private sector is an obligation for the new buyers to continue to provide those CSOs.

**Mr Davis**—In one respect, if that was written into the terms and conditions of the contract, then the cost of the CSO would have been passed back to the public sector because the price would have been discounted accordingly. The key point to remember with any CSOs is eventually somebody pays somewhere. It is not a free gift, coming like manna from heaven. The option that must have been exercised in that case, following your example—I am not aware of the details to the extent that you must be—is that effectively the cost of the CSO was passed back to the taxpayer through consolidated revenue by a reduced sale price.

**CHAIR**—Does the ACCI have a view about cross-subsidies as opposed to CSOs at times being a more appropriate way of meeting those sort of obligations, or are you opposed in principle to cross-subsidies and totally in favour of the transparency of CSOs being provided as a line item on budgets?

**Mr Davis**—Life is never black and white, as you will appreciate, Chairman. As a general preference, we prefer to see that dealt with as a line item. Where there is need for a cross-subsidy arrangement then obviously it would have to be very transparent. Many of the problems that have come through the cross-subsidies process in the past have been that most people have been aware that they exist. Any small business person will know that they overpay for electricity. You only have to go to somebody, say, in a delicatessen and they know that their electricity bill is higher than it should be. What we have never really known is how much. There is still a lack of transparency in there.

Providing a cross-subsidy is one form of providing a CSO. The other form identified is a line item entry or a payment from consolidated revenue. Another form we have identified is accepting a lower rate of return. There are any number of ways of providing a CSO. Our view is, again, a maximum transparency and where possible take it away from being a cross-subsidy in any other distortion, like reduced rate of return, and put it onto the public sector revenue.

Equally, if the government decides it wants to have an agency provider CSO, for example, Telecom, to provide services to rural Australia, or Optus for that matter, then it should be a matter of contract between, say, the communications minister and those two agencies. They provide him a bill to do this and that is it. It is paid for by the taxpayer. At the moment what you are really doing is concentrating on one group of users as distinct from, in social equity terms, sharing it across everybody who should contribute.

**CHAIR**—The danger in that particular analogy—it is not a bad one to use, I guess, because it has been around for some time with a suggestion that there is possibly a cross-subsidy of up to half a billion dollars for telecommunications services for rural and provincial Australia—is that if, in fact, that was provided on budget, then at a time of pruning and expenditure restraint it would be a relatively easy thing to chop back on that and say, 'It's half a billion dollars. Let's make it $450 million. It's still very generous,' and so on, which is the argument that I guess a lot of consumer interest groups would use. How would you respond to that?

**Mr Davis**—Obviously, government is about determining these priorities. That would be a matter for the communications minister to work out how that fell with his other priorities.

**Mr THOMSON**—Determining or ruining them, occasionally.

**Mr Davis**—That is a matter of judgment. Many hard decisions have to be made by government. What is the alternative, that you will continue to basically overcharge one group of users? In Telecom's case,

basically we have seen a system of untimed local calls. So how is that paid for? Generally it has been paid for by the STD system. The federal government, quite rightly, has been promoting Australia as a platform for regional headquarters in Asia-Pacific.

One of our great assets is our relatively inexpensive Telecom system. So what we are really doing is saying we are not making ourselves uncompetitive internationally in Telecom's based system to provide support for rural users. We could become more competitive in our Telecom based system—say, the financial institutions—if we just brought those expenses away from high volume Telecom users onto the public account.

The other side of the equation, of course, is with the Hilmer reforms and competition. Many of these areas which have traditionally been overpriced will probably be the first to be subject to new competition. For example, railways have been a traditional monopoly. One part subsidised the other. Although it is a bit hard to say, you could say broadly suburban passenger services have subsidised non-urban freight activities. If we get an open system in railways under the Track Australia reforms that are coming through then you could well see private providers running their rolling stock in peak hours. The derogatory term is 'cherry picking'. It means going after the most profitable segments, but that is how the market works. Therefore, you will have to find a mechanism if you want to subsidise non-urban services.

**Mr BRADFORD**—What are the arguments against transparency? The point you are making, at least from my point of view, is quite well taken. Other than the option of putting it as a budget item, which the chairman said has the possible downside of it being subject to reconsideration from time to time, what other arguments are there against transparency?

**Mr Davis**—The most obvious one is confidentiality. If the government is entering into a contract with someone, being required to disclose the final amount could breach confidentiality. We have seen the government argue that with the sale of the airports. If we wrote into the budget what we expected to get, that would be what we would get. So we would be on the defensive in the transaction. There are counterarguments against that too. Not every contract that the government enters into should necessarily be secret for all time but, at the end of the day, it becomes a balance of forces. If you have only got two or three players, then a contract with one would automatically alert the others but, if you get into a very competitive market with many players, then maybe confidentiality is not so important.

**Mr MARTYN EVANS**—I was interested in your argument that in future you might drift towards the situation where the private sector itself, the tenderers, provide the CSO. As you went on to recognise in a later answer, that inherently implies that that CSO would still be funded by the taxpayers at large because it would have to be passed back to the taxpayers through a reduced tender price. If that did not occur in the initial phase, there would subsequently be a temptation by the private sector providers to employ their own cross-subsidy. If they were committed to providing a certain CSO, say, as a condition of the contract in rural areas, and they overprice their bid when they made the initial bid—they failed to correctly understand what the CSO would cost them and in fact it cost them more—they would still be obligated to provide it anyway. They would then have to engage in their own cross-subsidies, would they not?

**Mr Davis**—Not unless they have something to cross-subsidise with.

**Mr MARTYN EVANS**—They would go bankrupt otherwise. Let us say you are providing a telecommunication service—Optus, for example—in Sydney and in the country areas. You would almost be compelled to cross-subsidise between the city and the country to meet your CSO obligation.

**Mr Davis**—It depends. The assumption in that is that basically one segment is uncompetitive, that there is lack of competition in the part where you can maintain the cross-subsidy. It would be inappropriate for me to say, as a representative of business, that every time the private sector puts in a government tender it

makes a profit. In business you make errors. Sometimes you make a bad quote, and you are stuck with it and you wear it. You will either suffer the wrath of the shareholders or, in an extreme case, you might go out of business. But in the long-run average, if you survive, you have tendered correctly. In terms of the ability of the private sector to cross-subsidise itself, it would depend if it was operating in areas where there was a lack of diminished competition. That is essentially what sustains a cross-subsidy: you can basically over charge in one part because of an absence of competition. Under the Hilmer regime, many areas have traditionally been the 'honey pot' from where the money has been taken and they will now be exposed to competition. So the ability to provide a cross-subsidy will disappear quite quickly.

**Mr MARTYN EVANS**—There are a lot of attractions to that system of providing CSOs through the private sector in the process, in comparison with having it on budget. It is very hard for us, as a parliament and a government, to determine just what it does cost Telecom to cross-subsidise some of those rural telecommunications areas, and there would be many other similar examples. It is perfectly feasible to provide on-budget subsidies for these things. If you do that, there are two problems: firstly, you cannot define exactly what the cost is because you are not providing the service, you are one step removed from it; and, secondly, to some extent, you encourage inefficiencies in the provision of that service because they have got a lump sum with which to provide the service. So there is no internal efficiency driving, to some extent, that cost reduction. It would be more efficient, I would suspect, overall, to provide that through the private sector tender process than it would to provide it through an on-budget fixed subsidy negotiated with someone who was not the service provider.

**Mr Davis**—The on-budget cost is not necessarily just a subsidy, it could in fact be the tender amount. You might tender, say, for 1998-99 and the amount would in fact be the contract price. It is not a matter of saying, 'Here's $600; now pack your costs up so that you can justify $600 to provide phones for everybody outside the CBD.' In fact, the cost should be the tender price. The other side of the inefficiency argument is to point out that it is very inefficient at the moment because often the GBE does not know what it is supposed to do. It is told, 'Go away and provide phones to these people.' They have to find out whether these people want a gold plated one or a silver plated one or a brass one or a basic one. What does it mean to provide a phone to someone 300 kilometres west of Mt Isa? Does it mean running a cable all the way out there? Does it mean somebody driving out there and giving them a satellite pod with a container and some batteries? Is it microwave? What is a phone? Does it mean that the person gets a fax phone or just a box or a mobile phone? The whole thing is totally ill-defined at the moment and that is the problem.

At the end of the day, the way we envisage the process working in a competitive market is that the government would just simply let a tender as it does for the way it buys chairs, gifts for foreign dignitaries, aeroplanes or whatever they like. 'We want this.' With a standard public sector tender it is just, 'Here are the terms and conditions; put in your bid.' You might well find—and let us use Telecom's example—in three or four year's hence, when it is open slather, that somebody might decide that they will only bid for New South Wales. Eleven people might bid for rural Queensland. Nobody might be interested in Victoria, for whatever reason. You might find that there are 17 bids for the southern part of the Northern Territory. Basically, it is just like any other product or service. The government calls tenders to purchase services; this would be another one. It would just be a question of precision. The inefficiency would be if the government is incompetent in setting out the tender process or the officials are incompetent in managing the process, in which case it is a matter for the parliament to hold the minister accountable.

**CHAIR**—Recently the committee spent some time in outback Queensland. A fear was expressed to us that with competitive tendering, for example, in local government, there would be a temptation for the private sector to perhaps underbid for particular road building contracts that were traditionally performed by local

government authorities in reasonably remote areas, on the basis that once they got that bid and had undercut people for a couple of years—and therefore there was no effective local operation to tender against—then in fact the price could go up substantially, firstly, to recover losses, and secondly, to have those sort of windfall profits continue ad infinitum. What would your response be to that sort of criticism?

**Mr Davis**—No-one in business would deny that loss leading is a part of business strategy. Going in too low and carrying a loss in the short term is quite a common business practice. One can see it opening a magazine for the Christmas sales; there are loss leaders in there. The flaw in that argument is that it assumes that no-one else will come back in the market. At every point that that price goes up it will re-trigger interest by somebody. No-one may do it at a dollar, no-one will do it at $1.10, but hit $1.15 and you get a whole raft of people who come back and say, 'Right, that is profitable for me to do again.' In terms of the provision of road construction services, one of the first things you will see from work done by the industry commission and others when you look at competitive tendering, is there is a massive great wedge between publicly provided and constructed road facilities and those done by the private sector. It could be up to 70 per cent.

The second point is that the great majority of local government roadworks are constructed by the private sector under contract anyway. The third point is that many of those who are engaged in the construction of road facilities used to be GBE employees, who have effectively privatised themselves and become players. At the end of the day, you will always see that, through a competitive tendering process, if the price does go back up again after a loss leading period, new interest will come back and say 'Hey, this is worth me being in this,' and so back they come. The ability to trough is always the prerogative of the company. The ability to claw it back through peaking will always be subject to the degree of competition in the market.

**CHAIR**—That is a perfectly rational argument, I guess, when you apply it in an economic sense. In some of the more remote parts of Queensland, a local government authority may have a reasonable supply of equipment—bulldozers, earthmoving equipment—that is on hand for an emergency such as a flood or a fire. If the work is being performed by the private sector and that equipment is then needed in the case of an emergency, it is often impossible to get it in for days. That is where I guess the rational side of the argument breaks down compared with the obligation to provide something like that on hand to serve the needs of the community in an emergency situation.

**Mr Davis**—It can be part of the tender contract—that in the event of an emergency your graders, et cetera, et cetera, are to be made available for use on a cost recovery basis. If you are 100 kilometres from somewhere, you do not drive your tractors home every night, you leave them in situ. Part of the contract may be that there is that CSO function written in to it that they have to do that. There may be the direct CSO function plus ancillary fire fighting activities. In an emergency I should not think the private sector would be standing back saying, 'Well, you give me the money before I do it'. They generally dive in, in the Australian way, do it, and if there is any cost to be borne—more often or not it is waived from my experience—they would probably talk about it privately. But, again, you can write that into the contract if that is what you want: have resources available for emergencies. Most of our emergency facilities outside the CBD are effectively privately provided anyway.

**CHAIR**—There are CSOs, if you like, of a lesser order which I guess are provided, not as a result of specific direction by a state or national government, but because, firstly, they have always done that within the local community, or secondly, there is an implicit suggestion that those sorts of services may be provided—a library, a swimming pool, or whatever. Does the chamber have any particular view about CSOs in terms of that dimension of the discussion on competition policy?

**Mr Davis**—It is not something we have directly concerned ourselves about. Our main priorities have

obviously been in those areas that have really impacted upon the national competition framework and the great majority of elements of local government have not been caught up in some of the more critical areas like the access to essential facilities. Most areas of local government are probably reasonably contestable anyway. They tend not to have the authorities lock out people from doing things. If someone wants to put up another swimming pool they are generally able to if they meet the requirements.

Again it is the same sort of thing. A local government may just wish to say, 'We want this provided' and open it to tenders. Maybe the local government next door decides to actually bid for the task. There is an assumption, say, within a 100 kilometres radius of Sydney, that each individual municipality will provide the swimming pool and do it all themselves.

Why do we not open it up to competition so that the municipality next door might do it? In fact, you might find one municipality on the south side of Sydney which is very good at building swimming pools and ends up making a commercial activity out of building public swimming pools all around the Sydney area. Again, they just might open it to competitive tender and say, 'We want a swimming pool. This is where it is to go. We want a diving board. We want this, this and this. Tender for it.' It comes back to the same thing. Local government can operate a competitive tender just as well, I think, as the state or the federal government.

**CHAIR**—In Victoria we have seen the introduction of compulsory competitive tendering in local government. I think at the moment 50 per cent of all tendering is compulsory competitive tendering which will probably go, I presume, to a 100 per cent position. Does the chamber have any view on that?

**Mr Davis**—No. We just believe it is really up to governments concerned. At the end of the day it is the taxpayer who will have the decision in the matter. If they are seeing that in one local government area their administration is competitive tendering and they are getting services much cheaper than the chap across the next local area, then the council will pay the consequence—competitive federalism or competitive local government, I guess. The mayor who can stand up and say, 'I charge $3.50 to get into the swimming pool because my government built it' will have to look askance at the bloke next door who has got a bigger swimming pool and says, 'I only charge $1.80 because the private sector built it'. That is democracy at work.

**Mr THOMSON**—To make some comment about the notion of local government competing for what struck me as commercial endeavours, even if the client is another local government, is it not strange, or unfair, that an outfit with a vastly higher credit rating, that is, a revenue base there with taxpayers or ratepayers, should be allowed to compete with a private enterprise that has to depend on a credit rating that is obviously going to be lower than that and that, therefore, it is an unfair advantage.

**Mr Davis**—What you have touched on is one of the five principles of the Hilmer report which is competitive neutrality. Under the competitive neutrality arrangements all play is expected to move towards a level playing field. You have seen the state governments moving towards paying tax equivalents and their GBEs and you are going to see other states and neutralising activities come on stream. There is no reason that could not be extended in time to the local governments paying what effectively are neutralising adjustments so that they all start at the same point.

**Mr THOMSON**—Earthmoving and road building seems a bit vulnerable to this, where you could have a rather gung-ho local government with its own plant and so forth go in and just knock out all the local rivals and competitors over a period with the loss leading tenders and it can be very destructive.

**Mr Davis**—If the ratepayers in their home municipality are prepared to wear the longer term costs of higher rates, or they are ignorant, or what other reason, that is their prerogative.

**Mr THOMSON**—Bismarck said that universal suffrage is government of the house by its nursery and some people say the same about proportional representation with what we go through with the Senate and

minor parties here. I think there is a role for the national parliament to have some say in that before it gets to such a potentially destructive thing. I will be interested in your—

**Mr Davis**—As Mr Simmons has pointed out, in many respects, the functioning of local government is a prerogative of the states. I guess some would argue constitutionally, but I do know that it is as black and white as that. But, at the end of the day, you are applying principles of competitive federalism down to local government. We would like to see a very good outcome. And, to follow through your example, there should be no reason why one local government could not become a player in providing certain services or functions from goods.

**CHAIR**—We have looked at examples in some of the more remote areas and, indeed, examples have been given to us in Victoria where the government has decided to amalgamate local government. They have reduced the number from 220 to about 80. Except in the case of one council, they are currently governed by a set of appointed commissioners. The concern has been expressed to us that, with all the rationalisation and making operations more efficient in country shires, that it could also have some pretty traumatic social effects. For example, a shire based around a town of two or three thousand people may also have an important input into the economy of some surrounding villages with 200 and 300 people.

If you take out a local government function, such as the positioning of some of the road building equipment and therefore the loss of one or two staff, it may impact on the size of the school in that situation resulting perhaps in a reduction of teaching staff. It could affect a police service operation. In other words, trying to balance out what is a plausible economic scenario with a position that perhaps also raises an issue of the social make-up of a community. Is the chamber looking at this from a purely economically driven approach or do you take into account those sorts of impacts? Do you think it can be resolved simply by way of straight out market forces?

**Mr Davis**—There is always a balance or argument in these things and, as you would appreciate in the political process, it is never purely anything. There is always political, social, industrial, economic and foreign affairs arguments in many decisions taken in this place. In the social sense, you can also find winners out in the local government areas. If you get a more effective system of providing CSOs, you might find many small enterprises are now willing to go to the country when they had not been willing to before. You can pay a CSO and say, 'The government wants to develop the Bathurst and Orange areas'—and we have seen that in the past—'therefore, we will provide you with cheaper facilities.' You can have CSOs that are job creating and out developing rural areas. So it can cut both ways. Yes, there will be some winners and, yes, there will be some losers. But it depends how they are all structured.

**CHAIR**—But it is very dangerous for governments to try and pick winners in that situation, is it not?

**Mr Davis**—The examples I have used were not what you would call roaring successes.

**CHAIR**—Selective decentralisation proposals, for example.

**Mr Davis**—Yes. But, again, if governments decided to make them generally available, they might have a zone A and zone B in a general tax system. In that way, those who live in certain areas can get lower rates of personal income tax. It is quite plausible that government might decide that they want to encourage business development a certain distance outside of the coastal areas and that companies that go there will get 5c knocked off their company tax rate. You can have a CSO that is job creating and does the world of good for rural Australia. I was raised in the country so I have a lot of empathy for it.

**CHAIR**—I want to move now to another situation. In recent times, we have seen a lot of government business enterprises become privatised. I want to explore some of the implications of CSOs in that position. What sorts of mechanisms should be adopted where you have a business enterprise which has CSOs, and is privatised for the future delivery of those CSOs, for their funding and importantly for the monitoring of their

performance in their delivery.

**Mr Davis**—You can go one of two tracks when you privatise an agency. You can either continue to provide a CSO or not continue it. If they decide not to, it just junks all those activities. It would go on regardless and take commercial decisions on the ebb and flow of business life. If the governments want this agency to provide CSOs for the future, the obvious question any competent board will ask is, 'What do you actually want us to do?' Then the government would have to be very clear because the board would say either, 'Yes, we will' or 'No, we won't'.

If they say no, then in a true privatisation the government would have no recourse, unless it wanted to legislate and then a political risk comes into future privatisations. If they say, 'Yes, we are willing to talk to you about it,' it becomes just another contract with government. The government would specify what it wants and the management of the former GBE would say how much it would cost. It would all be broken down nice and clearly. The minister would then sign off knowing precisely what he is up for. That is effectively allowing the privatised body to enter into a normal contract. The cost of providing the CSO would then have to show up in the public accounts.

For example, Telecom is asked to do these eleven things. They bid $400 million for it. The minister for communication signs off the $400 million. It shows up in the budget papers and it is there for everybody to see. The other option is that when Telstra is privatised, it is written into the sale document that it will be expected to do this, this and this—all these eleven tasks. All the bidders will then say, 'Okay, that is fine. We will value them this way,' and they will be reflected in the sale price. So, in both ways, it tracks back to the taxpayers in the end.

There are advantages and disadvantages in each option. Where the CSO requirement is written into the sale document, it is rigid. If the government wants to change the terms and conditions, it is rather difficult. They might decide in five years time that they want this former GBE to do more. The former GBE says, 'No, we do not have to. It is all there as part of the prospectus.' Anybody who knows company law knows about the discipline of a prospectus document; they can just dig in their heels and say no. If you go with the other option which says it is a contract between the former GBE and the government then it can have the terms and conditions that are agreeable between the parties. One does not necessarily have to be so concerned with ASC rules and requirements and, of course, you get much greater flexibility.

The advantages of allowing the thing to be privatised and then going into contract arise from the flexibility in the terms and conditions. The disadvantage for government is that the former GBE may not want to cooperate. The countervailing argument is to impose the CSOs in it and you get locked into a more rigid position. At the end of the day it becomes a matter of judgment. The other option is that if a new player comes on to the scene, it means that the earlier body may be less competitive against a more nimble player, especially if it is an agency that is required to provide a CSO on an umbrella basis. Most competitors—you have already seen this with Optus and you will probably see it with the others after July l997—will come into segments of the market so it will become rather hard for the monolithic or the umbrella player. Those who are stuck with a rigid system may find themselves ultimately uncompetitive and in the long run government may lose the vehicle that really wants to provide the CSO. They may end up having a two-tiered system where this agency is stuck with things that were decided five years ago yet it has to go on contract with all these other players.

**CHAIR**—Are there any further questions? I am wondering perhaps if I could just explore one other issue. Your submission concentrated a fair bit on CSOs. It has been very useful both from the submission and our discussions this morning but one of the other issues that we are asked to address is how governments go about applying the so-called public interest test. Would you give us the views of the chamber of the sorts of

consultation processes that should be adopted if we are looking at this issue of the public interest test.

**Mr Davis**—As a matter of fact, Mr Chairman, it exercised our minds greatly. As we went through the Hilmer process, every so often we would trip over the words 'national interest' or 'public interest' and, I must say wryly, all we could remember when we saw the national interest was Jim Hacker's view, 'I am the national leader. It is in my interest, therefore it is in the national interest'. I am glad to see our political friends have the same wry sense of humour we have.

**CHAIR**—We are a bit like public servants though. We often laugh at different times when that show is on.

**Mr Davis**—Defining the public interest is a matter of great difficulty. I guess what we would really like to see is some written definition somewhere of what it actually means. When we were in the Hilmer process and we sought that, we were told that it was one of those concepts that is best left vague. The key point is that when one exercises the public interest or the national interest test in any of this, we would like to see something like a judicial need to explain the reasons for the decision, so there is transparency in what is meant by the public interest or the national interest in the specific case.

Regrettably, those two terms have become a catch-all flexibility, if you like, a bit of a bolt hole, when something that, on criteria, should happen, is not wished to happen for a whole variety of other reasons and it becomes an escape hole from objectivity. All we would say to this inquiry is that we recognise that the public interest and national interest are in there. We would like to see certainty and transparency in how they are defined and applied because vicarious use of them does nothing for business confidence in any of these matters.

**Mr THOMSON**—What about the charter of the Reserve Bank and the goals set out there? That is about as close as I have seen it to being reduced to mere text but I take your point. What do you think of those, for instance, low inflation, full employment?

**Mr Davis**—I know that that has been a matter of some discussion elsewhere in this building. I have a colleague who handles some of our interests in this area. I might just bite my tongue and defer to his expertise. We were aware of the debate as to what is the greater public interest in the Reserve Bank's various requirements? Is it keeping interest rates low or is it keeping employment up, et cetera? It becomes a relative trade-off and the relative mix is a movement over time.

We have traditionally had some sympathy in giving the Reserve Bank the overriding obligation to pursue a very low inflation rate, although to the best of my knowledge we have not committed ourselves to calling for them to emulate the New Zealand model.

**CHAIR**—Do you have any further comments you would like to leave before we finish, Mr Davis?

**Mr Davis**—No, except to say that at the end of the day somebody pays for a CSO. What we would be reminding the committee is to work out who should be paying it and how they should pay it, whether it is different classes of users in the same group or whether it should be paid by taxpayers as a whole.

**CHAIR**—Thank you. If we have any further questions we will write to you so you can respond.

Resolved (on motion by Mr Martyn Evans):

That this committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at public hearing this day.

**CHAIR**—I declare this public hearing closed.

**Subcommittee adjourned at 11.30 a.m.**