National Competition Council

National Competition Policy and Related Reforms

Supplementary Assessment of First Tranche Progress

30 June 1998

CONTENTS

ABBREVIATIONS

CPA	Competition Principles Agreement
FAGs	Financial Assistance Grants
NCP	National Competition Policy
NEM	National Electricity Market

BACKGROUND

On 11 April 1995, the Commonwealth, State and Territory governments signed three agreements underpinning the National Competition Policy (NCP). These agreements, together with the specific agreements on electricity, gas, water and road transport, set a number of reform objectives for the period to the year 2000.

To ensure the benefits of reform are shared amongst all governments, the Commonwealth agreed to make payments to those States and Territories making satisfactory progress in implementing the agreed reforms. As part of this process, the National Competition Council is to assess, prior to 1 July 1997, 1999 and 2001, the reform progress of each jurisdiction.

On 30 June 1997, the Council provided its first tranche assessment to the Commonwealth Treasurer. In its document, *Assessment of State and Territory Progress with Implementing National Competition Policy and Related Reforms*, the Council detailed the first tranche reform obligations established by the NCP agreements, together with its assessment of the progress achieved by each jurisdiction.

The Council concluded that each jurisdiction had achieved substantial progress in meeting its first tranche reform commitments. However, there remained some areas where progress had not been sufficient to meet first tranche commitments.

Accordingly, the Council recommended that:

- each jurisdiction receive in full the first part of first tranche payments due in 1997-98; and

- the second part of first tranche payments, due in 1998-99, be dependent on satisfactory resolution of the matters outstanding at June 1997.

The outstanding first tranche matters identified in the 1997 assessment are summarised in the following table.

Summary of June 1997 Recommendations: First Tranche NCP Payments

State/Territory	Outstanding First Tranche Issues, June 1997	Recommendations
New South Wales	Review progress with legislation review and reform obligations re domestic arrangements for rice marketing for compliance with clause 5 of the CPA prior to July 1998. Review progress with legislation review and reform obligations re casino control legislation for compliance with CPA clause 5 prior to July 1998. Review progress with legislation review and reform obligations re legislation for the privatisation of the NSW TAB for compliance with CPA clause 5(5) prior to July 1998. Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Payment due in 1998-99 dependent on evidence of CPA clause 5 compliance for domestic rice marketing arrangements and casino control legislation, compliance with CPA clause 5(5) for TAB privatisation legislation and progress with the application of competition principles to local government.
Victoria	Review progress with application of the uniform National Gas Access Code prior to July 1998. Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of the National Gas Access Code and with the application of competition principles to local government.
Queensland	Review progress with application of the uniform National Gas Access Code prior to July 1998. Review progress with legislation review and reform obligations re casino agreement legislation for compliance with CPA clause 5 prior to July 1998. Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of the National Gas Access Code, compliance with CPA clause 5 for casino agreement legislation and progress with application of competition principles to local government.

State/Territory	Outstanding First Tranche Issues, June 1997	Recommendations
Western Australia	Review progress with the national gas reform commitments re tender process for a second Dampier/Perth natural gas pipeline. Review progress with application of the uniform National Gas Access Code prior to July 1998. Review progress with review and reform of agreement legislation prior to July 1998. Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on commitment to implementation of the National Gas Access Code, and satisfactory progress with national gas reform commitments in respect of removing regulatory barriers to free and fair trade in gas, with review of agreement legislation and with application of competition principles to local government.
South Australia	Review progress with application of the uniform National Gas Access Code prior to July 1998. Review progress with legislation review and reform obligations re casino control legislation for compliance with CPA clause 5(5) prior to July 1998. Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of the National Gas Access Code, evidence of clause 5(5) compliance for *Casino Act 1997*, and the application of competition principles to local government.
Tasmania	Review progress with application of competition principles to local government prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of competition principles to local government.
Australian Capital Territory	Review progress with application of the uniform National Gas Access Code prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of the National Gas Access Code.
Northern Territory	Review progress with application of the uniform National Gas Access Code prior to July 1998.	Full payment of first part of first tranche payment due 1997-98. Second part of payment due in 1998-99 dependent on satisfactory progress with application of the National Gas Access Code.

SUMMARY AND RECOMMENDATIONS

Over the past 12 months, all State and Territory governments have worked with the Council to seek to resolve the reform implementation matters identified in the Council's 1997 assessment. The Council considers that progress consistent with first tranche NCP obligations has been achieved in several areas.

However, the Council considers that New South Wales has not complied with its NCP obligations in relation to its domestic rice marketing arrangements. In addition, Western Australia has not enacted legislation to apply the National Gas Access Code by 30 June 1998, as set out in the Inter-Governmental Agreement on gas.

THE NATIONAL GAS ACCESS CODE

In June 1997, the Council concluded that New South Wales and Tasmania were the only jurisdictions to have met their first tranche commitments in respect of the National Gas Access Code. The objective of the Code is to establish a uniform national framework for third party access to natural gas pipelines. For other jurisdictions, the Council noted that the date agreed by COAG for implementation of the Code was not going to be met, but that jurisdictions were working to develop a new timetable for national gas reform through the Gas Reform Implementation Group. The Council recommended that progress be re-assessed prior to July 1998.

In November 1997, the Commonwealth, State and Territory governments agreed to take all reasonable measures to have the National Gas Access Code enacted, proclaimed and commenced by 30 June 1998.[1]

South Australia, as lead legislator, enacted the *Gas Pipelines Access (South Australia) Act 1997* in December 1997. Since then, all States and Territories, with the exception of Western Australia, have enacted legislation giving effect to the Code. In the case of Western Australia, the relevant legislation has been introduced into State Parliament.

The legislation enacted by the States and Territories does not become operational until the Commonwealth enacts its own legislative amendments. To date, the Commonwealth has not fulfilled this commitment.

The Council is satisfied that all States and Territories, with the exception of Western Australia, have now taken all reasonable measures to meet their commitments in relation to the National Gas Access Code.

[1] Tasmania is not required to comply with the obligations of the Inter-governmental Agreement until a time sufficiently before the first natural gas pipeline in that State is approved or any competitive tendering process for a new natural gas pipeline is approved (Clause 4.3, Inter-governmental Agreement).

Western Australia is yet to enact legislation supporting the National Gas Access Code, although the legislation has been introduced into State Parliament and the WA Premier has committed the Government to doing all in its power to ensure the legislation is passed before the end of September 1998. However, the fact that the Commonwealth has not enacted its own legislation necessary for the Code to become operational means that Western Australia's not having enacted its legislation has no practical implications at this time. Accordingly, the Council relies on the assurance of the WA Premier and recommends that a financial penalty not be imposed on Western Australia at this time.

APPLICATION OF COMPETITIVE NEUTRALITY PRINCIPLES TO LOCAL GOVERNMENT BUSINESSES

In June 1997, the Council indicated some concern about the extent of progress in applying competitive neutrality principles to local government business activities in all jurisdictions (except the ACT and Northern Territory).[2] Specifically, on the basis of the evidence available at the time, the Council could not be confident that jurisdictions had identified significant local government business activities and sufficiently advanced the implementation of competitive neutrality principles in these activities.

The Council considers that subsequent to June 1997, all jurisdictions have demonstrated that they have made progress consistent with their first tranche commitments in this area.

MONOPOLY LICENCING PROVISIONS CONTAINED IN GAMBLING LEGISLATION

In June 1997, the Council raised a number of questions about various governments' compliance in relation to existing and proposed monopoly licensing arrangements contained in casino control legislation and in proposed legislation enabling the privatisation of the NSW TAB. Since then, Queensland and South Australia have examined their casino legislation and New South Wales has examined the laws supporting the TAB monopoly. The Commonwealth has also announced that it will sponsor a wide-ranging inquiry by the Productivity Commission into the social and economic effects of gambling.

In the view of the Council, the work that has been undertaken to date by governments has highlighted the complexities and sensitivities associated with the economic and social impacts of gambling and wagering. In addition, the proposed Productivity Commission inquiry is likely to advance community consideration of the costs and benefits of restrictions on gambling activity. Given these circumstances, the Council considers that the monopoly licensing arrangements contained in South Australian and Queensland casino legislation, and the legislation supporting the privatisation of the NSW TAB, are better addressed outside the first tranche assessment process.

[2] The ACT has no local government sector. The Northern Territory has virtually no significant local government business activities.

Notwithstanding this, clause 5 obligations with respect to gambling legislation will be a relevant consideration in future assessments.

WESTERN AUSTRALIA'S REVIEW OF ITS AGREEMENT ACTS

At the time of the June 1997 assessment, Western Australia had listed just three of its 84 agreement Acts in its legislative review timetable in accordance with clause 5 of the Competition Principles Agreement (CPA). In subsequent discussions with the Council, Western Australia undertook to review a sample of three additional agreement Acts by July 1998, and to ascertain the degree to which these Acts restrict competition and the extent to which reviews of other agreement Acts might be necessary. The Council indicated it would re-assess progress in this area by July 1998.

Consistent with its undertakings, Western Australia has completed reviews of the three resource development agreement Acts nominated by the Council, and is finalising the review of the *Northwest Gas Development (Woodside) Agreement Amendment Act 1994*, as scheduled in its legislation review timetable. Western Australia reported that the finding of the independent reviewer is that the three agreement Acts are generally pro-competitive and provide significant benefits to the State. On this basis, Western Australia is of the view that there would be little benefit in conducting a wholesale review of all existing State agreement Acts.

Western Australia has acted quickly to examine a sample of its resource development agreement legislation in line with the undertaking given in June 1997. Thus, the Council considers that Western Australia has met its first tranche commitments. The Council is yet to receive the review reports, and will consider these, together with Western Australia's decision following the review process, in future assessments.

WESTERN AUSTRALIA'S SECOND NATURAL GAS PIPELINE

In June 1997, the Council identified concerns regarding the process for considering an application for the construction of a second pipeline from the north-west shelf to the State's south-west as a regulatory barrier to free and fair trade in gas.

In order to demonstrate to the Council that its processes are not anti-competitive, Western Australia agreed, in the course of the 1997 assessment process, to conduct an open and transparent competitive process to determine whether anyone wishes to build a second pipeline.

The WA Premier has provided the Council with a written assurance that there are no legislative, regulatory or informal barriers to the construction of a second pipeline in Western Australia. Further, the Government has committed to an open and competitive expressions of interest process for the construction of a second pipeline, with the expressions of interest process to commence early in the September quarter 1998.

On the basis of the assurance by the Premier, together with Western Australia's intention to proceed with an expressions of interest process in the near future, the Council is of the view that Western Australia has met its first tranche commitment to ensure there are no regulatory barriers to free and fair trade in gas.

RICE MARKETING ARRANGEMENTS IN NEW SOUTH WALES

In June 1997, the Council identified New South Wales' decision not to reform its domestic rice marketing arrangements as inconsistent with the State's obligations under clause 5 of the CPA. This decision by New South Wales was taken despite an independent NSW Review Group concluding in 1995 that reform would be to the benefit of the community, and that the domestic rice market should be deregulated (with the single desk for exports of rice being retained).

Following an undertaking from New South Wales to enter into 'meaningful discussions' on reform of domestic rice marketing arrangements, the Council agreed to re-assess progress on this matter prior to July 1998.

Despite extensive discussions with the Council since then, New South Wales has offered no substantive additional information or justification for its decision. On this basis, the Council assesses New South Wales as not having met its first tranche commitments under clause 5 of the CPA with respect to domestic rice marketing. The Council's recommendation relates only to domestic rice marketing arrangements; it does not relate in any way to the single desk arrangement for exports of rice, which the NSW Review Group found provided a net public benefit.

In an effort to achieve an outcome consistent with the findings of the Review Group, the Council has proposed the establishment of a working group involving the NSW Government, the NSW rice industry and Council representatives to examine the recommendations of the 1995 review and all aspects of implementing those recommendations; and in particular, the deregulation by 31 January 1999 (the date recommended by the review) of domestic rice marketing arrangements and the retention of the single export desk.

RECOMMENDATIONS

The Council recommends that all States and Territories, with the exception of New South Wales, receive the full allocation of NCP payments from the Commonwealth.[3] (Attachment A contains details of the maximum payments to States and Territories for 1998-99.)

With respect to New South Wales, the Council recommends that $10 million be deducted from the 1998-99 component of the NCP payments otherwise due to New South Wales,

[3] 'NCP payments' refers to the real per capita FAG guarantee and to the specific competition payments.

but that the deduction not take place until after 31 January 1999 — the date for domestic market deregulation as recommended by the 1995 independent review. The Council will make a subsequent recommendation that the $10 million deduction not be imposed if, prior to 31 January 1999, New South Wales deregulates the domestic rice market as recommended by the 1995 review.

Of course, it is always open to New South Wales to seek to demonstrate to the satisfaction of the Council that, contrary to the finding of the 1995 review, there is a net community benefit justification in support of retention of the domestic rice marketing arrangements and that such benefits cannot be achieved by less anti-competitive means.

DEVELOPMENTS AGAINST OUTSTANDING ISSUES IDENTIFIED IN JUNE 1997

This section has two parts. Part A covers the matters outstanding at June 1997 common to jurisdictions. Part B covers matters specific to particular jurisdictions.

PART A ISSUES COMMON TO JURISDICTIONS

A.1 UNIFORM NATIONAL GAS ACCESS CODE

Outstanding issue, June 1997:

In the June 1997 assessment, the Council concluded that New South Wales and Tasmania were the only jurisdictions that had met their first tranche commitments in respect of the National Gas Access Code:

- New South Wales had established a State access regime for the services of gas distribution pipelines that was closely modelled on the draft National Gas Access Code then being finalised.

- The Inter-governmental Agreement then being developed (and subsequently agreed in November 1997) provided that Tasmania would not be required to comply with the obligations of the Agreement until a time sufficiently before the first natural gas pipeline in that State is approved or any competitive tendering process for a new natural gas pipeline is approved.

For other jurisdictions to be assessed as having met their first tranche commitments, the Council recommended that they would need to implement the Code in accordance with the timetable in the Inter-governmental Agreement.

Developments since June 1997:

In November 1997, the Commonwealth, State and Territory governments signed the Inter-governmental Agreement. Each jurisdiction agreed to take all reasonable measures to have the National Gas Access Code enacted, proclaimed and commenced by 30 June 1998.

South Australia, as lead legislator, enacted the *Gas Pipelines Access (South Australia) Act* in December 1997. All other jurisdictions, with the exception of Western Australia, have since enacted legislation giving effect to the Code. In the case of Western Australia, the relevant legislation has been introduced into State Parliament.

The legislation enacted by the States and Territories does not become operational until the Commonwealth enacts its own legislative amendments. To date, the Commonwealth has not fulfilled this commitment.

Assessment:

The National Gas Access Code has not commenced by the target date of 30 June 1998. However, this is largely due to the Commonwealth failing to enact the legislative amendments necessary for the Code to become operational. Accordingly, the Council considers that all States and Territories, with the exception of Western Australia, have now taken all reasonable measures to meet their commitments in relation to the National Gas Access Code.

Western Australia is yet to enact legislation supporting the National Gas Access Code, although the legislation has been introduced into State Parliament. The WA Premier, in a letter to the Council, has committed the Government to doing all in its power to ensure the legislation is passed before the end of September 1998. The fact that the Commonwealth has not enacted its own legislation necessary for the Code to become operational means that Western Australia's not having enacted its legislation has no practical implications at this time. Accordingly, the Council relies on the assurance of the WA Premier and recommends that a financial penalty not be imposed on Western Australia at this time.

A.2 COMPETITIVE NEUTRALITY REFORM AND LOCAL GOVERNMENT

In the June 1997 assessment, the Council recognised that all relevant jurisdictions[4] had made some progress towards implementing the required competitive neutrality reforms in co-operation with local governments, particularly in undertaking necessary preparatory work. Jurisdictions had published policy statements outlining their proposals for applying competition principles (including competitive neutrality principles) to local governments, and were developing guidelines to assist the application of competitive neutrality principles. These guidelines cover matters such as competitive neutrality pricing and how to apply the public interest test.

Some jurisdictions were simultaneously undertaking other local government reforms, such as council amalgamations, that have the potential to complement competitive neutrality reforms in the longer term.

However, the Council's view at the time was that all jurisdictions needed to demonstrate greater substantive progress in order to be assessed as having met their first tranche commitments. In particular, the Council sought evidence from jurisdictions that local governments had identified their significant business activities and determined how competitive neutrality would be applied to those activities. Accordingly, the Council undertook to re-assess jurisdictions' progress prior to July 1998.

All jurisdictions have since provided evidence of progress against their NCP obligations, although it appears that progress has been faster in some than in others. The Council

[4] 'Relevant jurisdictions' in this context refers to New South Wales, Victoria, Queensland, Western Australia, South Australia and Tasmania.

does not regard this as constituting a compliance failure by those jurisdictions where 'on the ground' reforms are taking more time. Implementing competitive neutrality reform with respect to local government business activities is a complex and involved task:

- State governments must work in co-operation with many local governments, rather than implement reform unilaterally;
- skills and resources are not always available to local governments — some local governments, particularly the smaller ones, need to develop new skills and processes for effective competitive neutrality reform;
- the size and nature of local government business activities vary considerably both within and between States;
- there are often significant public interest considerations associated with local governments, particularly in remote locations where regional development and employment factors may be important;
- the process of corporatising local government businesses has been complicated by negotiations with the Commonwealth on taxation issues;
- in some jurisdictions, local governments are simultaneously implementing reforms required by State governments, such as compulsory competitive tendering; and
- processes such as council amalgamations that are underway in several jurisdictions have delayed NCP reform programmes, but potentially will see more rapid reform later in the process.

While noting there is some variability in outcomes across jurisdictions, the Council is now satisfied that all jurisdictions have demonstrated progress sufficient to meet their first tranche commitments. The Council accepts the above factors mean that in the early stages of implementation, the pace of competitive neutrality reform, as well as the types of business activities identified for reform, will vary among jurisdictions (and even within jurisdictions). Notwithstanding the complexities involved, the application of competitive neutrality principles to local government business activities is an important and potentially fruitful area of reform. Continuing implementation and application of competitive neutrality reform will be important in the Council's second and third tranche assessments.

Each jurisdiction's progress in this area is considered in turn.

New South Wales

Outstanding issue, June 1997:

In the June 1997 assessment, the Council acknowledged that New South Wales had approached reform in this area in good faith, and that important preparatory work had been undertaken. However, the Council indicated that New South Wales needed to

demonstrate that significant business activities are being identified and are having competitive neutrality principles applied to them.

Developments since June 1997:

In 1997, New South Wales issued local councils with various guidelines on competitive neutrality. One set of guidelines, *Pricing and Costing for Council Businesses: A Guide to Competitive Neutrality*, included a timetable for applying competitive neutrality principles to significant business activities.

For 'Category One' activities (with a turnover of at least $2 million), the implementation timetable requires councils to:

- implement separate internal reporting for the business activity from July 1997;
- apply full cost attribution from July 1998; and
- make subsidies an explicit transaction from July 1998.

For 'Category Two' activities (with a turnover of less than $2 million), there is more flexibility. Councils are to:

- determine the extent of separate internal reporting for the activity from July 1997;
- adopt full cost attribution, where practicable, from July 1998; and
- make subsidies an explicit transaction from July 1998.

In January 1998, New South Wales surveyed all local councils to assess progress in applying competitive neutrality principles to their significant business activities. The survey returns received by early March indicated that 56 councils had completed the task of identifying their significant business activities, and a further 44 had partially completed the exercise.[5] A 'substantial majority' of both those councils that had only partially completed and of those that had not yet identified any business activities indicated that they plan to have the process completed by the end of June 1998.

By early March 1998, councils had identified 90 Category One business activities and 318 Category Two business activities. Of the 90 Category One activities identified, 71 have established separate internal reporting for the activity. For some Category One activities, full cost attribution and identification of subsidies are already in place to varying degrees. Of the 318 Category Two activities identified, 39 already have full cost attribution applied to them (with a further 68 having partial cost attribution) and 151 already have their subsidies, if any, made explicit.

[5] The survey was issued to 177 councils and a further 20 'special purpose councils', giving a total of 197 local government bodies.

New South Wales indicated to the Council that it intends to conduct a follow-up survey of local councils as soon as practicable after 1 July 1998 to gauge the extent of implementation at that time. Moreover, New South Wales has undertaken to provide the Council with a further, more complete report by around September 1998.

Assessment:

The detailed information provided by New South Wales indicates that the identification of local government business activities, and the application of competitive neutrality principles to those activities, is progressing. The Council is satisfied that New South Wales has met its first tranche commitments.

Victoria

Outstanding issue, June 1997:

At the time of the 1997 assessment, Victoria indicated that:

- councils are required to have identified their significant business activities by June 1997;
- councils are to apply full cost pricing (where appropriate) to these activities from July 1997;[6] and
- where an activity had been approved for formal corporatisation (generally only suitable for large activities), that activity is to be corporatised by July 1998.

Victoria also indicated that by June 1997, five local government business activities had already been approved for corporatisation.

Whilst considering that Victoria had substantially met its first tranche reform commitments in this area, the Council sought information from Victoria, by July 1998, on the practical application of competitive neutrality principles (including full cost pricing).

Developments since June 1997:

Victoria stated that since June 1997, a further five local government business activities have been approved for corporatisation.

In addition, Victoria confirmed that local councils have applied competitive neutrality pricing principles (including, where appropriate, full cost pricing) to their significant business activities from July 1997. Reporting on the application of competitive neutrality principles will be contained in the councils' annual reports for 1997-98, which are due to the Minister by 30 September 1998.

[6] Victoria's policy is that in circumstances where the costs of applying full cost pricing outweigh the benefits, any subsidies are to be made explicit.

In September 1997, the Office of Local Government distributed to all councils its *Draft Guidelines for Implementing Competitively Neutral Pricing Principles in Local Government*.

Assessment:

The information provided by Victoria has confirmed that the State is well advanced in applying competitive neutrality principles to local government business activities. All necessary processes appear to be in place, appropriate guidelines have been distributed to local councils, and the practical application of competitive neutrality principles appears to be ahead of most other jurisdictions.

Details of the extent of application of competitive neutrality principles to local government business activities will be available in September 1998. The Council is satisfied that Victoria has met its first tranche commitments.

Queensland

Outstanding issue, June 1997:

In the 1997 assessment, the Council was satisfied with Queensland's intended approach. However, the Council considered that to meet its first tranche commitments, Queensland needed to provide evidence that local councils had identified their significant business activities and determined the competitive neutrality principles to apply to them.

Developments since June 1997:

Queensland's approach is to prioritise its reform effort to the 17 larger local councils. By the end of 1997, Queensland's 17 large councils had completed competitive neutrality 'public benefit assessments' of their significant business activities and decided on the type of reform to be implemented (that is, corporatisation, commercialisation or the application of full cost pricing).[7] All councils have decided to implement at least full cost pricing, with commercialisation being the most common type of reform. Councils have generally supported the recommendations of the public benefit assessments, although some have qualified their decision because of the uncertainty about the taxation of local government owned enterprises.

In total, 26 council businesses (with a combined annual expenditure of more than $700 million) are to have competitive neutrality reforms applied from July 1998 (although implementation will be staged in some instances; for example, a council might implement full cost pricing by 1 July 1998 and commercialisation one year later).

[7] As for other jurisdictions, councils may still provide subsidies to their activities, provided that the subsidies are made explicit.

In addition, all councils are to identify their smaller business activities that compete directly with the private sector and decide whether to apply a voluntary Code of Competitive Conduct. The Code is based on the principle of full cost pricing.

Assessment:

Queensland has identified 26 significant business activities in the State's 17 largest councils for competitive neutrality reform and has developed a reform agenda. The Council considers that Queensland's progress is sufficient to meet its first tranche commitments.

Western Australia

Outstanding issue, June 1997:

In the 1997 assessment, the Council considered there was insufficient evidence that application of competitive neutrality reforms to local governments had progressed to the extent required for the first tranche. In particular, the Council requested that Western Australia identify the significant business activities of local governments and determine reform outcomes.

Developments since June 1997:

Western Australia has embarked upon a comprehensive competitive neutrality review programme with respect to local government. A large number of activities, many of which are relatively small, have been subject to the review process.

Western Australia's requested its largest 54 local councils to complete competitive neutrality reviews of their significant business activities by 1 June 1997. By April 1998, 24 councils had completed their reviews or decided to implement competitive neutrality without conducting reviews, seven councils had completed reviews but were still to determine the extent of reform arising, and 10 councils were still in the process of undertaking reviews. A further 13 councils had no significant business activities.

Of the 83 reviews of business activities completed by local councils at April 1998, competitive neutrality is to be applied in 44 cases. (That is, for the remaining 39 business activities, it was concluded that implementing competitive neutrality was not in the public interest.) The most common form of implementation is the application of full cost pricing. For some activities, commercialisation models will be adopted and separate business units established.

Western Australia indicated that a further 90 smaller local councils have been requested to complete their competitive neutrality reviews by 1 June 1998. Western Australia expects that very few of these will have any significant business activities.

Assessment:

Western Australia has made some progress towards identifying significant local government business activities for the purpose of competitive neutrality reform. At April 1998, competitive neutrality principles have been or will be applied to 44 business activities.

However, a significant percentage of the larger councils had not completed their competitive neutrality reviews by April 1998. The Council understands that since April significant further progress has been made by the local councils in completing their competitive neutrality reviews.

In several cases, completed reviews recommended that competitive neutrality principles not be applied to the business activity under review. Western Australia indicated that there are some public interest reasons for this outcome. The State imposes a lower threshold for determining whether a business is significant for competitive neutrality purposes than States such as New South Wales and Queensland. Consequently, a large number of the activities reviewed had revenues of less than $300 000. Moreover, 30 of the 54 large councils are in fact relatively small non-metropolitan bodies, meaning that public interest factors associated with isolated rural communities become relevant. The consequence of all this is that the potential benefits of applying competitive neutrality principles to these activities may be lower, and the associated costs may be higher.

The Council is satisfied that Western Australia has adopted a broad-based investigation of the case for applying competitive neutrality principles to the significant business activities of local governments. The Council considers that Western Australia has made satisfactory progress in meeting its first tranche commitments.

South Australia

Outstanding issue, June 1997:

Arising from the 1997 assessment, the Council sought evidence from South Australia that the State had sufficiently advanced its competitive neutrality reform agenda, including identifying the significant business activities of local governments to which competitive neutrality principles are to apply. The Council noted that the local government amalgamations programme in South Australia had delayed the implementation of competitive neutrality reform.

Developments since June 1997:

In 1997, the Local Government Association prepared a set of guidelines to assist local governments to identify significant business activities and apply competitive neutrality principles to those activities.

As at December 1997, local councils had identified all their significant business activities and determined which competitive neutrality principles to apply to 'Category One' business activities (those with an annual revenue over $2 million or deploying assets with

a value over $20 million). Six Category One business activities were identified, five of which are conducted by the Adelaide City Council and are to have full cost pricing applied. The remaining Category One business activity already operates on a fully commercial basis.

In addition to these six businesses, the District Council of Coober Pedy listed its electricity undertaking as a Category One business activity, but determined that the costs of applying competitive neutrality principles would outweigh the benefits. South Australia stated that it considered the electricity undertaking to fall outside the definition of 'business activity' set out in its policy statement on clause 7 of the CPA.

Thirty local councils identified 49 'Category Two' business activities. The councils have until June 1998 to consider how competitive neutrality is to be applied to these activities.

Assessment:

South Australia has now identified the local government business activities to which competitive neutrality principles will be applied. The Council is satisfied that the business activities identified and the reform programme to be implemented are consistent with South Australia's first tranche commitments.

Tasmania

Outstanding issue, June 1997:

In the 1997 assessment, the Council considered that Tasmania had not demonstrated sufficient progress against its first tranche commitments. In particular, the Council noted that the process of local government amalgamations had delayed the implementation of competitive neutrality reform in the short term. The Council accepted that progress with competitive neutrality reform is likely to increase following the completion of the amalgamations programme.

Developments since June 1997:

Progress in implementing competitive neutrality reform has continued to be delayed by the council amalgamations programme.

The Local Government Board has been reviewing all council boundaries, with a view to reducing the number of councils from 29 to not more than 15. At the time of the June 1997 assessment, Tasmania advised that the Board would report to the Minister for Local Government by the end of October 1997. However, after receiving the Board's report in February 1998, the Minister asked the Board to reconsider its recommendations. The Board reported to the Minister at the end of May 1998. Elections for the new councils have been set for August 25.

Given these developments, Tasmania temporarily suspended its timetable for applying competitive neutrality principles to local government.

Tasmania indicated it intends to re-commence implementation of competitive neutrality reform as soon as the amalgamations programme is completed. The State proposes to seek the agreement of new councils to apply full cost pricing to their significant business activities from September 1998. Further, Tasmania indicated it planned to review its corporatisation process with the objective of completing the programme by July 1999, twelve months earlier than originally envisaged.

Assessment:

The Council accepts that council amalgamations are likely to lead to a wider and more timely application of competitive neutrality principles. Nonetheless, the Council is concerned at the delay in commencing Tasmania's competitive neutrality programme for local government business activities.

In view of the commitments given by Tasmania to seek the agreement of new councils to apply full cost pricing from September 1998 and the anticipated earlier completion of the corporatisation programme, the Council is satisfied with Tasmania's progress against its first tranche commitments. The Council notes that progress in line with the timetable Tasmania has set for itself will be important for the second tranche assessment.

A.3 GAMBLING LEGISLATION

Outstanding issue, June 1997:

In the 1997 assessment, the Council identified legislation providing exclusive licences for the operation of casinos and TABs as a restriction on competition and therefore warranting examination in jurisdictions' legislation review programs. The Council identified instances where governments had:

- failed to schedule for review existing legislation which restricts competition by providing geographic and/or game exclusivity in casino licensing arrangements (as required by clause 5(3) of the CPA); and

- failed to examine proposals for new legislation providing exclusive licensing arrangements for casinos and TABs (as required by clause 5(5) of the CPA).

The Council considered that failure to review this legislation is inconsistent with the intent of the CPA. However, the Council recognised that review of the legislation is likely to involve complex social and economic issues (including an assessment of community attitudes to gambling and casinos). Consequently, the Council decided not to provide a negative assessment, in respect of the first part of the first tranche payments, for jurisdictions that had not scheduled the legislation for review. Rather, if the relevant jurisdictions agreed, prior to July 1998, to a process for considering the anti-competitive elements of the legislation, then the Council would provide a positive assessment for the purpose of the first tranche payments.

Developments since June 1997:

In response to the Council's 1997 assessment, South Australia and Queensland examined their casino licensing arrangements and New South Wales undertook to address casino licensing in its 1998 annual report. New South Wales also examined the net public benefit associated with the monopoly licensing arrangements for the NSW TAB. (Other jurisdictions had already programmed reviews of their casino licensing arrangements and other gambling legislation in their June 1996 timetables.)

Assessment:

Relevant jurisdictions have complied with the Council's June 1997 recommendation that the gambling legislation be scheduled for review. The Council has considered the (confidential) South Australian and Queensland reports on casino monopoly licences and the NSW report on the TAB monopoly. The Council has also had more general discussions with jurisdictions on these and related gambling legislation matters.

More recently, the Commonwealth has announced a national review of the economic and social implications of gambling arrangements to be undertaken by the Productivity Commission. (New South Wales has since announced its own review of gambling in that State.) The Council supports such an approach, which would allow for systematic consideration of broader social and economic issues associated with all forms of gambling including casinos and TABs. This would be consistent with the intent of the CPA.

The Council's discussions with jurisdictions on the monopoly licence question have highlighted the complexities and sensitivities associated with the social and economic impacts of gambling and wagering. In addition, the proposed Productivity Commission inquiry is likely to advance community consideration of the costs and benefits of restrictions on gambling activity. In these circumstances, the Council considers it would be counter-productive to conclude an approach in respect of gambling legislation, and particularly the monopoly licence questions, in the context of the first tranche assessment process.

Notwithstanding this, clause 5 obligations with respect to gambling legislation will be a relevant consideration in future assessments.

PART B JURISDICTION-SPECIFIC ISSUES

B.1 WESTERN AUSTRALIA'S REVIEW OF ITS AGREEMENT ACTS

Outstanding issue, June 1997:

In the 1997 assessment, the Council noted that Western Australia had 84 agreement Acts in place, of which only three were scheduled for review. The Council sought, and received, a commitment from Western Australia to examine a small sample of its resource development agreement legislation over the next 12 months and ascertain the degree to which these Acts restrict competition. Where non-trivial restrictions imposing a net cost to the community are identified, the Council would expect the relevant legislation, and other Acts similar in effect, to be examined in more detail.

Developments since June 1997:

On 30 January 1998, Western Australia commenced independent reviews of three resource development agreement Acts nominated by the Council.

The respective parties to the three agreements and relevant government agencies were consulted during the review process. However, the Council accepted Western Australia's position that it would be inappropriate for the reviews to be opened to public comment because of the contractual nature of the legislation and the effect on industry confidence of an implication of unilateral amendments to State agreements.

The three sample reviews have been completed. Western Australia reported that the finding of the independent reviewer is that the agreement Acts are generally pro-competitive and provide significant benefits to the State by reducing risk and transaction costs.

Western Australia stated that a few provisions with anti-competitive effects were identified but their effects were not considered significant. In addition, Western Australia considered that unilateral changes to State agreement Acts could incur high sovereign risk costs, with respect both to the companies involved and to future dealings other companies have with the State.

On the basis of the sample reviews, Western Australia argued that there would be little benefit in conducting a wholesale review of all existing State agreement Acts, particularly when compared with the costs arising from such a review programme.

In addition, the review of the *North West Gas Development (Woodside) Agreement Amendment Act 1994* is currently being finalised as scheduled in Western Australia's legislation review timetable.

In 1997-98, a number of other agreement Acts were repealed or scheduled for repeal. A further six agreement Acts have also been added to the legislation review timetable for review in 1999.

Assessment:

Western Australia has acted quickly to examine a sample of its resource development agreement legislation in line with the undertaking given in June 1997, thus meeting its first tranche commitment in this area.

The Council is yet to receive the review reports. The Council will consider the reports, together with Western Australia's decision following the review process, in future assessments.

B.2 WESTERN AUSTRALIA'S SECOND NATURAL GAS PIPELINE

Outstanding issue, June 1997:

In the 1997 assessment, the Council identified concerns regarding the process for considering an application for the construction of a second pipeline from the north-west shelf to the State's south-west as a regulatory barrier to free and fair trade in gas. The Council was concerned that Western Australia's decision to refuse the licence placed barriers on the development by industry participants of the gas market in that State.

Whilst the Council recognises the Government's important role in approving pipeline licences to ensure that any development meets the needs of the State without imposing undue costs, the Council is of the view that the licensing process should be conducted in an open and transparent way. Applicants should be able to address themselves to known criteria, with licensing acceptance or refusal being based on sound economic, environmental and social considerations. The market should be able to develop naturally, rather than through artificially imposed timelines.

In order to demonstrate to the Council that its processes are not anti-competitive, Western Australia agreed, in the course of the 1997 assessment process, to conduct an open and transparent competitive process to determine whether anyone wishes to build a second pipeline.

Developments since June 1997:

Western Australia has informed the Council that prior to seeking formal expressions of interest for a second pipeline, it sought to establish a framework that would encourage private investment, and that it considers land access essential to this process.

Western Australia has enacted legislation and regulations to establish a Dampier to Bunbury Natural Gas Pipeline corridor, which may contain other pipelines to transport gas. The Act also establishes a Land Access Minister to manage the corridor and access to it. Currently, the corridor is being expanded from 30m to 100m to accommodate

additional pipelines as well as the expansion of the Dampier to Bunbury National Gas Pipeline.

The Premier has provided the Council with a written assurance that there are no legislative, regulatory or informal barriers to the construction of a second pipeline in Western Australia. Further, the Government has committed to an open and competitive expressions of interest process for the construction of a second pipeline, with the expressions of interest process to commence early in the September quarter 1998. The Premier has indicated that the same principles would continue to apply if there was no interest in construction of a second pipeline following the 1998 expression of interest process.

Assessment:

On the basis of the assurance by the Premier, together with Western Australia's intention to proceed with an expressions of interest process in the near future, the Council is of the view that Western Australia has met its first tranche commitment to ensure there are no regulatory barriers to free and fair trade in gas.

B.3 RICE MARKETING ARRANGEMENTS IN NEW SOUTH WALES

Outstanding issue, June 1997:

In June 1997, the Council identified New South Wales' decision not to reform its domestic rice marketing arrangements as an outstanding first tranche issue. This decision by New South Wales was taken despite a recommendation by the 1995 New South Wales Rice Review Group (the Review Group) supporting deregulation of domestic rice marketing (with retention of the single export desk). The Review Group proposed this be done by not renewing the vesting powers of the New South Wales Rice Marketing Board (the Board) when they expired after 31 January 1999. In essence, the Council was not satisfied that New South Wales had complied with its obligation under clause 5 of the CPA to retain an anti-competitive arrangement only where a net community benefit can be demonstrated.

Following an undertaking from New South Wales to enter into 'meaningful discussions' on reform of domestic rice marketing arrangements, the Council agreed to re-assess progress on this matter prior to July 1998.

Background:

In November 1995, the Review Group reported to the New South Wales Government on arrangements for rice marketing in that State as provided in the *Marketing of Primary Products Act 1983*.

The Review Group concluded that reform of existing arrangements would be to the benefit of the community. It recommended, among other things, that:

- the single desk exporting of rice be retained via Commonwealth regulation of rice exports through the grant of a single Australian export licence (should the Commonwealth not agree to this, the Review Group proposed that New South Wales put in place arrangements to effectively maintain a single export desk); and

- the domestic rice market be deregulated through discontinuing vesting beyond the expiration of the (then) current proclamation on 31 January 1999.

Contrary to the recommendations of the Review Group, New South Wales decided to retain the existing vesting arrangements until 31 January 2004, with a review of the vesting arrangements in 2002 to consider whether changed market conditions justify any alterations.

In support of its decision to retain existing domestic rice marketing arrangements until 2004 the New South Wales Government stated:

- it believes the benefits from deregulation for domestic arrangements to be small;

- that deregulation poses a risk to the substantial benefits to the State and to the national economy; and

- that there is no feasible means of deregulating domestic market arrangements while maintaining the Rice Board's export monopoly, which is considered to deliver an unambiguous benefit.

Developments since June 1997:

Despite extensive discussions with the Council since June 1997, New South Wales has offered no substantive additional information or justification for its decision. As a result, the matter has not advanced from the position at June 1997.

Assessment:

Two key issues remain unresolved to the Council's satisfaction:

- a failure by New South Wales to demonstrate a net community benefit justification in support of the retention of the domestic rice marketing arrangements despite the recommendation of an independent review to deregulate; and

- a failure by New South Wales to adequately explain why reform of the domestic rice marketing arrangements cannot be decoupled from retention of the export monopoly arrangements (as recommended by the Review Group).

In the Council's view, the arguments put forward by New South Wales in support of retaining domestic rice marketing arrangements, neither individually or collectively, constitute a substantive net community benefits justification.

The Review Group's preferred mechanism for securing the benefits arising from the single export desk was via the granting of a single Commonwealth export licence for rice. If this did not eventuate, as is the case, the Review Group recommended that a State-based approach to retaining the single export desk should be provided and that the domestic market be deregulated by not renewing the Board's vesting powers. The Council acknowledges that decoupling the export and domestic arrangements using state legislative powers presents some difficulties due to Constitutional constraints. However, in its view, New South Wales has demonstrated a lack of willingness to discuss alternative regulatory options.

This is highlighted by New South Wales' lack of interest in two suggestions put forward by the Council, which could preserve the benefits accruing from single export desk arrangements as demonstrated by the 1995 Review Group, while achieving domestic market reform. Specifically:

- a voluntary grower arrangement to collectively market rice exports made under section 51(2)(g) of the *Trade Practices Act 1974* (the Act) which is exempt from the restrictive trade practices provisions of the Act; or

- a right for rice producers to "opt-out" from having their rice automatically vest with the Board such that they can sell to any buyer anywhere in Australia while ensuring that, by contractual means, export sales are traded through the Board as a single export desk.

The Council's view is that New South Wales has not engaged in 'meaningful discussions' on the issue of domestic rice marketing despite numerous opportunities over the past two years. On this basis, the Council assesses New South Wales as not having met its first tranche commitments under clause 5 of the CPA with respect to domestic rice marketing.

The Council will recommend to the Commonwealth Treasurer that the Commonwealth deduct $10 million from the 1998-99 component of the NCP payments otherwise due to New South Wales, but that the deduction not take place until after 31 January 1999 — the date for domestic market deregulation as recommended by the 1995 Review Group. The costs imposed on the Australian community by the current domestic rice marketing arrangements (as estimated by the 1995 Review Group) have been used to help determine the quantum of this deduction.

The Council will continue to seek to achieve an outcome that is consistent with the findings of the 1995 Review Group and is in the interests of the Australian community. The Council will make a subsequent recommendation that the $10 million deduction not be imposed if, prior to 31 January 1999, New South Wales deregulates the domestic rice market as recommended by the 1995 Review Group.

To this end, the Council has proposed the establishment of a working group involving the NSW Government, the industry and Council representatives to examine the recommendations of the 1995 review and all aspects of implementing those recommendations (including any appropriate structural adjustment measures); and in particular, the deregulation of domestic rice marketing arrangements and the retention of the single export desk.

A prime focus of the activities of the working group will be to examine alternatives for retaining an effective single export desk while achieving domestic market deregulation as recommended by the 1995 Review Group. The aim of this is to give rice growers a right of free choice as to whether or not they should be bound to market their rice crop on the domestic market through the Board, while at the same time preserving the single export desk benefits that were judged by the 1995 Review Group to flow to the Australian community.

Of course it is also always open to New South Wales to seek to demonstrate to the satisfaction of the Council that, contrary to the finding of the 1995 review, there is a net community benefit justification in support of retention of the domestic rice marketing arrangements and that such benefits cannot be achieved by less anti-competitive means. To this end the Council would consider any evidence provided to the working group of a net community benefit provided by existing arrangements.

ATTACHMENT A PAYMENTS TO STATES AND TERRITORIES UNDER THE NATIONAL COMPETITION POLICY FOR 1998-99

Total payments available to States and Territories in 1998-99 for satisfactorily progressing competition reform obligations are estimated to be around $391 million, comprising a per capita growth in FAGs element of $174 million and Competition Payments of $217 million. The estimated maximum amount that could be received by each State and Territory is shown below.

MAXIMUM PAYMENTS TO STATES AND TERRITORIES UNDER THE NATIONAL COMPETITION POLICY, 1998-99 ($ MILLION)

	FAGs (per capita growth component)	Competition payment	Total
New South Wales	51.6	73.4	125.0
Victoria	38.0	53.8	91.8
Queensland	32.9	40.2	73.1
Western Australia	16.7	21.2	38.0
South Australia	16.8	17.2	34.0
Tasmania	6.7	5.4	12.2
ACT	2.7	3.6	6.3
Northern Territory	8.7	2.2	10.9
Total	174.3	217.0	391.3

Note: The figures in the table may differ from those in the 1998 Federal Budget due to updated Consumer Price Index and population estimates.

Totals may not add due to rounding.

Source: Commonwealth Treasury.