State Government of Victoria

NATIONAL COMPETITION POLICY AND LOCAL GOVERNMENT

A STATEMENT OF VICTORIAN GOVERNMENT POLICY

Competition Policy

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FOREWORD

This statement fulfils Victoria's obligations under the National Competition Policy *Competition Principles Agreement* to publish, by June 1996, a statement prepared in consultation with local government on the application of competition principles to local government.

The statement has been prepared by a Joint State/Local Government Working Group comprising representatives of both metropolitan and non-metropolitan Victorian municipalities, the Municipal Association of Victoria and relevant Victorian Government agencies. A consultation draft of the statement was distributed to all local councils and other key stakeholders in April 1996. Comments received on the draft have been taken into account in the finalisation of the statement.

"Competition policy is not about the pursuit of competition for its own sake. Rather, it seeks to facilitate effective competition in the interests of economic efficiency while accommodating situations where competition does not achieve economic efficiency or conflicts with other social objectives."

National Competition Policy
Report of Independent Committee of Inquiry, 1993 p.6

"....the process of exposing services to competitive tendering does not imply that services will cease, nor does it diminish Council's responsibility for managing the provision of services. On the contrary, it encourages Council to clearly articulate its wants, needs and desires through the preparation of specifications. It makes Council more accountable by showing how it is to measure its success in delivering these services to its community and at what cost".

Port Phillip City Council
Submission to Industry
Commission Inquiry
Competitive Tendering and Contracting
By Public Sector Agencies (1995)

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Competition and public sector reform

Recent years have seen the introduction of competition into a variety of public sector activities with the aim of delivering higher quality services at least cost to service users and taxpayers.

Competition can be a powerful tool not only for fostering increased efficiency, but also for encouraging innovation and greater responsiveness to customer preferences. In the contest to win and retain business, rival service providers face strong incentives to offer the highest quality, most reliable and most cost effective services to their customers.

Effectively managed, the introduction of competition into both user and taxpayer funded public sector activities can therefore help to ensure that resources are put to their best use and not dissipated through inefficient operations or over-investment in underutilised assets.

Through the implementation of compulsory competitive tendering, Victoria is already setting the pace for the rest of Australia in the introduction of competition into the supply of a wide range of local government services. Victorian councils, ratepayers and the community at large are now beginning to see the material benefits of competitive tendering, which is contributing to lower rate levels and the provision of more efficient and effective services.

Competition policy is not intended to override any other social, economic or environmental policy objectives. Rather, it aims to foster better informed public policy choices based on a more transparent assessment of welfare costs and benefits in the development of government regulation and the provision of services.

National Competition Policy

In recognition of the increasing importance of competition policy to the achievement of improved productivity and enhanced international competitiveness, the Commonwealth and all States and Territories agreed in April 1995 to the implementation of a National Competition Policy.

This agreement followed the report of the independent National Competition Policy Review Committee, chaired by Professor Hilmer. The Hilmer report found that, while there had been significant progress towards improving the competitiveness of the trade exposed sectors of the Australian economy, many restrictions on competition remained within the domestic economy. These restrictions protect inefficiencies which, in the public sector, can result in higher than necessary costs of infrastructure and of government services and can result in a less internationally competitive economy.

"If Australia is to prosper as a nation, and maintain and improve living standards and opportunities for its people, it has no choice but to improve the productivity and international competitiveness of its firms and institutions. Australian organisations, irrespective of their size, location or ownership, must become more efficient, more innovative and more flexible."

National Competition Policy
Report of Independent Committee of Inquiry, 1993, p.1

National Competition Policy represents a commitment by all Australian governments to reduce or remove many of these restrictions on competition with a view to enhancing the nation's economic performance and improving the welfare of the Australian community.

National Competition Policy involves a commitment by the Commonwealth, States and Territories to apply uniform competition laws to all market participants, to apply a common set of competition principles to the reform and restructure of public monopolies and to remove unwarranted statutory restrictions on competition.

Governments also agreed to the establishment of two new national competition bodies:

- the Australian Competition and Consumer Commission (ACCC), which combines the functions of the former Trade Practices Commission and Prices Surveillance Authority. The ACCC will oversee compliance with uniform national competition laws, make determinations under the new national third party access regime and be responsible for prices surveillance and monitoring; and
- the National Competition Council (NCC), a new national advisory body which will make recommendations on whether a facility should be declared an essential service for purposes of the national third party access regime, will monitor compliance with the National Competition Policy Agreements and will advise the Commonwealth on whether States and Territories have satisfied the conditions for receipt of Competition Payments.

Application to Local Government

It was agreed by the Council of Australian Governments that National Competition Policy would also apply to local government. Recent reforms to the structure and operations of local government in Victoria mean that councils in this State are particularly well placed to respond to the National Competition Policy agenda.

Competition laws

While there has in the past been some doubt whether the prohibitions on anti-competitive conduct contained in Part IV of the *Trade Practices Act* 1974 applied to local government, the National Competition Policy agreement to extend uniform national competition laws to all market participants will remove that doubt. From 21 July 1996, Part IV of the TPA (or the Competition Code) will apply to local government, as it will to all other statutory authorities, government business enterprises and to Crown entities so far as they engage in business. In preparation for this, in the latter half of 1995 all councils were advised to conduct an audit of their activities to identify any conduct which may contravene competition law and to develop appropriate trade practice compliance programs.

Competition principles

The principles set out in the *Competition Principles Agreement* will also apply to local government, with each State and Territory having the discretion to specify the application of the principles to particular local government activities and functions within its jurisdiction.

These principles commit each government to:

- consider the establishment of independent sources of prices oversight of government monopolies where such oversight does not already exist;
- apply competitive neutrality policies and principles to all significant government business activities;
- adopt certain structural reform principles before introducing competition into markets traditionally supplied by public monopolies;
- adopt the guiding principle that legislation should not restrict competition unless it can be demonstrated that the benefits to the community as a whole outweigh the costs and the objectives of the legislation can only be achieved by restricting competition; and
- facilitate access to essential facilities where such access is required to permit competition in upstream or downstream markets.

Having been divested of water and sewerage services and electricity distribution businesses as part of the State's wider public sector reform program, local government in Victoria is unlikely to be significantly affected by the structural reform and essential services access provisions of the *Competition Principles Agreement*.

Similarly, the agreement to consider independent prices oversight mechanisms for public monopolies will not generally be applicable since Victorian councils have few, if any, significant business enterprises that are monopoly or near monopoly suppliers of goods or services.

On the other hand, the application of principles of competitive neutrality to government business activities will be of particular significance for Victorian local authorities given the already extensive pro-competitive reform of council operations through the introduction of compulsory competitive tendering.

Councils will also be affected by the adoption of pro-competitive legislative principles, including the requirement to review and, where appropriate, reform restrictions on competition contained in local laws.

The principle of competitive neutrality states that government owned businesses should not enjoy any net competitive advantage relative to their private sector counterparts simply by virtue of their public sector ownership. Competitive neutrality principles need to be considered wherever government is engaged in significant commercial activities and wherever competition is being introduced into the performance of functions which were former government monopolies, including the supply of non-commercial government services subject to competitive tender.

As required under the *Competition Principles Agreement,* the Victorian Government has published a policy statement on how it intends to apply principles of competitive neutrality within the State's jurisdiction, including an implementation timetable and a complaints mechanism. That policy is to apply to all significant government businesses, including local government businesses, and to non-commercial activities of State and local government agencies wherever these are subject to competitive tendering. Application of the policy is to be subject in each case to the assessment that the wider efficiency benefits would outweigh the costs of implementation.

In accordance with the policy, councils will be responsible for ensuring that their significant business enterprises comply with principles of competitive neutrality. Where there are expected to be benefits in terms of improved resource allocation which would outweigh implementation costs, and subject to the approval of the Minister for Local Government and the Treasurer, councils will need to consider adopting a corporatised structure for their significant commercial operations and the application of policies - such as Commonwealth and State tax equivalent payments - to remove any net competitive advantages enjoyed by those businesses as a result of government ownership. For significant business activities not considered to warrant separate incorporation or the application of tax equivalent payment regimes, councils will need to consider the application of competitively neutral pricing principles. In applying competitive neutrality policies to significant local government business activities which are primarily for profit or commercial purposes, councils will be subject to the State's competitive neutrality complaints mechanism to be established within the Department of Treasury and Finance.

In applying competitive neutrality principles in the context of competitive tendering, councils will need to adopt competitively neutral pricing principles and appropriate structural arrangements for in-house units competing for council contracts. In preparation for competitive tendering, councils have already instituted significant reforms in respect of their business activities and ways of operating in order to fulfil the requirements of competitive tendering. By July 1997, competitive tendering requirements will mean that councils will have already subjected the structure and pricing of their business activities to close scrutiny. Victorian councils should therefore be well placed to comply with Victorian Government policy on competitive neutrality from an early date. General compliance with these policies will be monitored by the Office of Local Government, which will also be responsible for considering any complaints against councils by third parties alleging non-compliance with competitive neutrality in the context of competitive tendering.

Compliance with the National Competition Policy agreements will also require the review and, where appropriate, reform of local laws which restrict competition.

In September 1995, the Minister for Local Government requested the Local Government Board to review the local laws provisions in Part 5 of the *Local Government Act* 1989. In particular, the Minister requested that the Board assess any adverse impacts on economic activity caused by local laws and how these could be addressed. The Board was also to have regard to the goals of National Competition Policy.

In May 1996 the Local Government Board released a discussion paper canvassing views on four possible options for the future of local laws. Whichever of these options is ultimately adopted, the revocation or review and reform of local laws that restrict competition will be completed by no later than June 1999. In addition, by July 1997, approval processes for making or amending local laws will be in place. This will ensure that new or amended local laws do not restrict competition unless it is demonstrated that the benefits of the restriction to the community as a whole outweigh the costs and that the objectives of the legislation can only be achieved by restricting competition.

Relationship to national competition institutions

With respect to compliance with the Competition Code or Part IV of the *Trade Practices Act* councils will be subject to the oversight of the ACCC, as will all State government agencies. As well as enforcement of national competition laws, the ACCC has an educative role in helping agencies to understand their obligations under the law and in providing advice on effective compliance strategies.

The National Competition Council will monitor the State's compliance with other aspects of the National Competition Policy agreements, including the compliance of local government authorities within the State's jurisdiction.

The Minister for Local Government will be responsible for ensuring that councils comply with NCP, including annual reporting requirements, with respect both to progress with the review and reform of legislative restrictions on competition and with the implementation of competitive neutrality principles in accordance with Victoria's published policy and implementation timetable. The Premier will be responsible for any direct reporting to the NCC regarding the compliance of both State and local government agencies with NCP requirements.

While the NCC may also conduct, or provide assistance with, reviews under the *Competition Principles Agreement,* the reviews it undertakes will be in accordance with a work program determined by the participating Commonwealth, State and Territory Governments. The NCC is not empowered to accept referrals of work from any other source, including local government.

Implementation timetable

Commencing from July 1996, local government in Victoria will progressively become subject to certain requirements under both the Competition Code and the *Competition Principles Agreement.* The implementation of Compulsory Competitive Tendering will be completed during the same time frame.

The key requirements for local government are shown on the following page:

Policy element	Timetable	Action required
Competition Code	Councils subject to Code from 21 July 1996	• All Victorian councils advised to undertake trade practice audit and develop compliance strategies by July 1996.
Compulsory Competitive Tendering	1995–96	• Councils to tender 30% of total expenses as set out in the Council's operating statement for 1995–96.
	1996–97 and subsequent years	• Councils to tender 50% of total expenses as set out in the Council's operating statements for 1996–97 and each subsequent year.
Competitive Neutrality	by June 1997	• Councils to have reviewed the corporate structure of their business activities and determined which of Model 1 or Model 2 competitive neutrality policies will apply.
	from July 1997	• Councils to apply competitively neutral pricing principles to all in house bids and to Model 2 business activities. Allegations of non-compliance to be investigated by OLG.
	from Sept 1997	• Councils to report annually on implementation of competitive neutrality principles, including substantiated allegations of non-compliance.
	by July 1998	• Councils apply Model 1 policies to any significant business activities approved for corporatisation. Corporatised entities to be subject to Statewide complaints mechanism.
Review of Local Laws	from July 1997	• Ensure all new local laws comply with Competition Principles.
	from Sept 1997	• Councils to report annually on the implementation of the *Competition Principles Agreement* legislative principle.
	by June 1999	• Review and where appropriate reform local law restrictions on competition.

"Councils are now in a position to provide better roads, better libraries, better childcare - a better standard of living for all Victorians. They are also in a better position to deepen and broaden the State's economic base through local and regional development."

The Hon. Roger Hallam, MLC
Minister for Local Government (Vic)
Local Government in 1995

Recent reform of the structure and operation of local government in Victoria means that councils in this State are particularly well placed to respond to and build on the requirements of National Competition Policy.

The reshaping of local government in Victoria - which has included significant boundary reform, divestiture of utility functions, deregulation of some former local government monopolies and the introduction of competitive tendering for the delivery of core services - has strengthened local government, instilled in it a culture of competitiveness and refocussed councils on their core responsibilities. In addition to the reforms initiated by the Victorian Government, individual councils have been pro-active in adopting new and more responsive management structures and approaches.

Restructure of Local Government

Between April 1993, when the Greater Geelong City Council was established, and January 1995, when new councils were established in north-west and north-central Victoria, the number of councils in Victoria was reduced from 210 to 78.

This restructure process was not simply a re-drawing of municipal boundaries to create a smaller number of larger councils than existed previously.

Its aim was to establish councils with a significantly stronger voice and greater resources to meet their responsibilities in key areas such as planning, tourism, economic development and environmental management.

Importantly, restructure has also resulted in significant economies of scale, reduced duplication and increased efficiency in local government. This has enabled all restructured municipalities to reduce their overall expenditure in 1995-96 (as revealed in their annual reports for that year) and deliver significant rate reductions to their communities.

- In 1995-96, Victorian ratepayers paid $263 million less in council rates compared to 1993-94 as a direct result of recent reform. This equates to a reduction of 17.7 per cent. Further reductions in aggregate rate levels will occur over the next two financial years.
- Rate cuts have been provided to 88 per cent of Victorian ratepayers.
- In addition to these rate reductions, efficiency gains made by councils made a further $59 million available in 1995-96 for improved services and new capital works initiatives.
- Total council debt was reduced by at least $78 million in 1995-96. This is a conservative estimate and is likely to be exceeded as councils use the proceeds of the sale of electricity distribution assets to retire debt.

Competitive tendering

A major element of the reform of Victorian local government has been the introduction of compulsory competitive tendering (CCT). By exposing local government services to competition, competitive tendering affords councils the opportunity to examine and improve the specification of service levels and standards. Through this, councils can improve their capacity to respond to community needs and preferences.

The underlying rationale for compulsory competitive tendering is that a council will be able to ensure, through market testing, that it is delivering quality services to the community in an efficient and effective manner.

The introduction of CCT in Victoria began in 1992 with the Government's local government pre-election policy statement. Its implementation was examined by the Local Government Board which established an Advisory Committee and consulted widely on the best method for implementing competitive tendering.

The Board's final report in December 1993 recommended a performance based model, suggested by local government itself, which required councils to achieve CCT expenditure targets. This model allowed local government to determine which services to put to tender, rather than follow the more prescriptive British or New Zealand models where specific services are nominated for exposure to tendering.

The CCT legislation passed by the Victorian Parliament in May 1994 required councils to market test 20 per cent of total operating expenses in the 1994-95 financial year, 30 per cent in 1995-96, and 50 per cent in 1996-97 and subsequent years.

A *Victorian Local Government Code of Tendering* was released in August 1995 to provide a guide to good practice in local government tendering. Developed with local government and private sector input, the Code's intent is to ensure that local government tendering is fair, transparent and accountable to the tenderers and the community. The Code sets out the principles which underlie good tendering practice and provides guidance on the way each stage of the tendering process should be conducted.

During 1995, the Victorian Office of Local Government undertook a series of spot audits at a number of councils to ensure fairness and probity during the tendering process. While the audit report concluded that there was room for improvement in some councils' CCT processes, it did not identify any pattern of advantage to either "in-house" or external tenderers in the awarding of tenders.

The 1994-95 target of market testing 20 per cent of total expenses was achieved by almost all Victorian councils. Overall, councils tendered 24.7 per cent of their expenditure in 1994-95.

While still in its infancy, competitive tendering has already demonstrated its considerable potential to improve the efficiency and effectiveness of local government operations through the introduction of competition. This potential was recognised in a recent report by the former Industry (now Productivity) Commission, *Competitive Tendering and Contracting by Public Sector Agencies* (October 1995), which concluded that, managed correctly, competitive tendering can produce real benefits to the public sector in terms of both cost and quality of service.

This and other reports relating to the implementation of competitive tendering in Victoria are listed in Appendix A.

Local Government utility responsibilities

A third element in the reshaping of local government has been the divestment of utility functions.

Since 1992, the Victorian Government has undertaken a sweeping program of public sector reform. A central feature of this program has been the reform of the Victorian Government's business enterprises in the electricity, gas, water and ports sectors. These reforms have resulted in the separation and divestment of local government's water and sewerage services and electricity distribution functions, enabling councils to focus more clearly on their core service and governance responsibilities.

Until comparatively recently, many non-metropolitan Victorian councils were responsible for the provision of water and wastewater services to their communities, in addition to their direct local government responsibilities.

In October 1993, the Government's policy *Reforming Victoria's Water Industry - A Competitive Future* was released. The policy identified substantial scope for improvement in the Victorian water industry by introducing competition to drive efficiencies and by empowering customers to make choices about the services they require. In 1994, building on this statement, the Government began restructuring the 83 non-metropolitan urban water authorities into 18 new regional water authorities.

The process of separating water functions from local government and incorporating these into the new regional water authorities was completed in 1995. This has given new focus to the management of water and wastewater services as separate, commercially-oriented businesses across the State.

Victoria's utility reforms have also involved a major restructure of the State's electricity sector. This has resulted in the division of the former State Electricity Commission of Victoria (SECV) into separate generation, transmission and distribution businesses and the progressive corporatisation and privatisation of the generation and distribution businesses.

Until 1994, 11 metropolitan municipalities operated electricity distribution services. These were responsible for distributing approximately 15 per cent of the State's electricity.

With the reform of the Victorian electricity industry, the 11 municipal electricity undertakings were absorbed into the five new distribution companies established by the Government to introduce competition into the retailing of electricity in Victoria.

The privatisation of each of the five new businesses was announced during 1995. Under an agreement with the Government, the successors to the former councils which owned municipal electricity undertakings received a share of the proceeds of the sale of the distribution businesses.

In April 1995, the Commonwealth and all States and Territories agreed to implement a National Competition Policy. The policy is to be given effect through the implementation of three intergovernmental agreements signed by the Council of Australian Governments:

- *the Conduct Code Agreement;*
- *the Competition Principles Agreement; and*
- *the Agreement to Implement National Competition Policy and Related Reforms.*

Conduct Code Agreement

Under the Conduct Code Agreement, State and Territory Governments agreed to extend the application of Part IV of the *Trade Practices Act* 1974 to all persons within their jurisdiction. This will ensure that universal and uniformly applied competitive conduct rules apply to all market participants, regardless of their ownership or legal form.

To give effect to this, each State and Territory agreed to enact its own legislation applying Part IV, known as the Competition Code.

Oversight of the Competition Code is the responsibility of the Australian Competition and Consumer Commission (ACCC), which was established on 6 November 1995 through a merger of the former Trade Practices Commission and the Prices Surveillance Authority.

Competition Principles Agreement

While the Conduct Code Agreement deals mainly with restrictions on competition arising from anti-competitive conduct, the *Competition Principles Agreement* establishes principles to address other forms of restriction on competition identified by the National Competition Policy Review Committee (Hilmer Report) as impediments to greater competition in the Australian economy.

The Agreement commits the parties to the following actions:

- consider the establishment of independent sources of prices oversight advice with respect to government business enterprises where these do not already exist;
- remove any net competitive advantage enjoyed by significant government enterprises by virtue of their public sector ownership, subject to the benefits outweighing the costs;
- when introducing competition to a sector traditionally supplied by a public monopoly, remove from the public monopoly any responsibility for industry regulation, and undertake a review of the appropriate structure and regulatory framework to be applied to the industry;
- review and, where appropriate, reform all existing legislation that restricts competition by the year 2000 and thereafter every ten years in line with the guiding principle that legislation should not restrict competition unless it can be demonstrated that:
  - the benefits of the restriction to the community as a whole outweigh the costs; and
  - the objectives of the legislation can only be achieved by restricting competition; and
- conform to a set of agreed guiding principles to facilitate third party access to services provided by significant infrastructure facilities to which access is necessary to permit effective competition in an upstream or downstream market.

A copy of the relevant sections of the *Competition Principles Agreement* is provided at Appendix B.

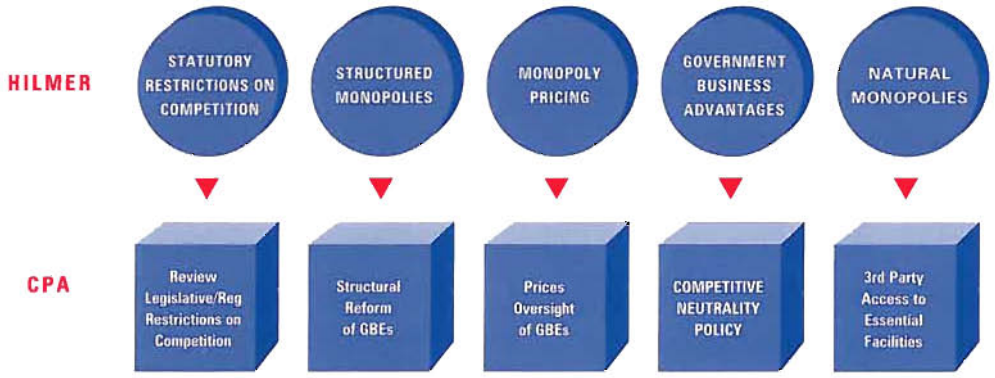


FIGURE 1

Agreement to Implement the National Competition Policy and Related Reforms

This Agreement sets out the overall timetable for the implementation of the National Competition Policy reforms and related COAG agreements governing reforms in specific industries - electricity, gas, road transport and water.

Provided that the States and Territories meet this agreed timetable, the Agreement provides that the Commonwealth will make to each State and Territory a series of "competition payments". By the year 2001-02, the total pool of competition payments will amount to $600 million per year in 1994-95 terms.

Under the Agreement, the Commonwealth will also extend its guarantee to maintain Financial Assistance Grants in real per capita terms on a rolling three year basis from 1997-98.

National competition institutions

Governments also agreed to the establishment of two new national competition bodies:

- the Australian Competition and Consumer Commission (ACCC); and
- the National Competition Council (NCC).

Australian Competition and Consumer Commission (ACCC)

The ACCC was established in November 1995 through a merger of the former Trade Practices Commission and Prices Surveillance Authority. It is responsible for enforcement of the competition and consumer provisions of the *Trade Practices Act* and the provisions of the Competition Code. All enforcement action will be brought in the Federal Court.

The ACCC will also make determinations under the national third party access regime established through the insertion of a new Part IIIA into the *Trade Practices Act*.

In addition, the ACCC is responsible for prices surveillance, inquiries and monitoring under the *Prices Surveillance Act*. This may include price oversight of a State or Territory Government business where the State or Territory concerned has agreed, or where the

National Competition Council has recommended declaration of the authority and the business is not already subject to an effective prices oversight mechanism established by the relevant State or Territory.

National Competition Council (NCC)

The NCC is a new national advisory body established by the *Competition Policy Reform Act* (Cth) 1995. The NCC will make recommendations on whether a facility should be declared an essential service for purposes of the national third party access regime. It will also monitor compliance with the National Competition Policy Agreements and advise on whether States and Territories have satisfied the conditions for receipt of Competition Payments.

The NCC may also conduct or provide assistance with reviews under the *Competition Principles Agreement* in accordance with a work program determined by participating Commonwealth, State and Territory governments. The NCC is not empowered to initiate such reviews or to carry out work referred to it by any other body, including local government.

"Every modern market economy has a set of rules designed to ensure that the competitive process is not undermined by the anti-competitive behaviour of firms, whether acting collusively or individually... in Australia these rules are contained in Part IV of the Commonwealth Trade Practices Act 1974."

"The Committee reviewed the provisions of the Act in some detail and for the most part found them to be operating satisfactorily... the most pressing issue is to ensure that unjustified gaps in their application are filled in a way that promotes a nationally consistent legal framework for business activity".

National Competition Policy
Report of Independent Committee of Inquiry, 1993 pp.xxi-xxii

Extension of Part IV of the Trade Practices Act

Part IV of the Commonwealth *Trade Practices Act* 1974 (as amended by the *Competition Policy Reform Act* 1995) sets out the competitive conduct rules which govern incorporated enterprises. This Act draws on the Commonwealth's constitutional power to regulate corporations, but also applies to unincorporated businesses engaged in interstate trade. The reach of the Commonwealth's corporations power does not extend to other unincorporated enterprises, nor does it cover State owned entities or business activities covered by the "shield of the Crown".

Under the intergovernmental Conduct Code Agreement, the Commonwealth and the States and Territories agreed to extend the application of Part IV to all persons within their jurisdiction. This has the effect of extending the reach of competition law to unincorporated businesses and to State and Territory Governments, their authorities and local government bodies.

The extension of Part IV of the *Trade Practices Act* (TPA) requires each State and Territory to enact legislation to apply the Competition Code as a law of its jurisdiction.

Victoria's *Competition Policy Reform Act* 1995 applying the Competition Code (Part IV of the TPA) within the State received Royal Assent on 14 November 1995.

The Competition Code will take effect from 21 July 1996.

There will be a 12 month moratorium on pecuniary penalties, which will apply from 21 July 1997. However, other remedies (such as damages and injunctions) will be applicable from 21 July 1996.

Provisions of Part IV

Part IV of the TPA prohibits certain forms of anti-competitive conduct.

A number of restrictive practices are regarded as being so inherently anti-competitive that they are prohibited absolutely.

Other practices are only prohibited if they have the purpose, or are likely to have the effect, of substantially lessening competition.

The following forms of conduct are **prohibited absolutely:**

Prohibited conduct	Description
Primary Boycotts	• where two or more competitors collaborate for purposes of preventing or limiting supply of goods or services to, or acquisition of goods or services from, particular persons or classes of persons. Risk areas include trade association meetings/opportunities for collusion among competitors.
Price fixing between competitors	• any arrangement which has the purpose or effect of fixing, controlling or maintaining prices for, or any discount allowance, rebate or credit in relation to, goods or services to be supplied or acquired by any of the parties to the arrangement. Encompasses any restraint on price flexibility.
Third line forcing	• where a supplier supplies goods or services on condition that the buyer buys goods or services from another person.
Resale price maintenance	• any direct or indirect attempt at enforcing resale price maintenance. The practice of *recommending* prices for goods and services is not prohibited provided that certain conditions are complied with.

Part IV also prohibits the following forms of conduct if they have the **purpose** or are likely to have the **effect** of **substantially lessening competition** in a market.

Prohibited conduct	Description
Anti-competitive agreements	• contracts, arrangements or understandings which have the purpose or are likely to have the effect of substantially lessening competition in a market. Risk areas include market sharing agreements and agreements which restrict the supply or quality of goods.
Misuse of market power	• an entity which has a substantial degree of power in a market is prohibited from using that power for the purpose of: – eliminating or substantially damaging a competitor; – preventing the entry of a person into any market; or – deterring or preventing a person from engaging in competitive conduct in any market; examples could include refusals to deal, termination of existing supply or trading arrangements, predatory pricing and price discrimination.
Exclusive dealing	• the interference by a supplier with the freedom of its buyers to buy from other suppliers and with the freedom of its suppliers to supply to other buyers. Risk areas include: – exclusive distribution – the purchase of goods or services on condition that the supplier will not supply goods or services to another distributor in a territory; – exclusive purchase – the supply of goods or services on condition that the buyer will not acquire similar goods or services from another supplier; and – restrictions on the resupply of goods or services to particular persons or in particular areas.
Mergers	• a merger is prohibited if it would have the effect, or be likely to have the effect, of substantially lessening competition.
Other boycotts	• where two parties together engage in conduct which restricts a third party from supplying to, or acquiring from, a fourth party.

Penalties

Various penalties may be applied or remedies sought for a breach of the restrictive trade practices provisions of Part IV or the Competition Code. These include:

- monetary penalties of up to $10 million for companies or State authorities and $500,000 for individuals;
- injunctions;
- damages;
- divestiture of shares or assets in the case of prohibited mergers; and
- ancillary orders of various kinds to remedy the loss or damage suffered.

The State Government will not be liable for pecuniary penalties (fines), but this protection does not extend to State authorities that are bodies corporate or companies, nor does it extend to individuals who are knowingly concerned in any contraventions.

Exemptions

There are three possible avenues whereby conduct may be exempted from Part IV of the TPA or the Competition Code:

- exceptions enacted under an Act or regulations made under a State Act;
- authorisation by the Australian Competition and Consumer Commission (ACCC); or
- in the case of exclusive dealing, notifying the conduct to the ACCC.

Legislative exemptions

The Victorian Government has adopted a policy of ensuring that exemptions from Competition Laws are only allowed when absolutely necessary. As a general rule, the Government does not support exemptions from Part IV of the TPA (or the Competition Code). In other words, offending conduct should, wherever possible, be modified so that it ceases to offend Part IV (or the Competition Code).

The Government will only enact exemptions where it has been demonstrated that:

- the benefits to the community as a whole of the restriction on competition (caused by the conduct to be exempted) would outweigh the costs to the community as a whole of the restriction on competition (caused by the conduct to be exempted); and
- the objective of the proposed exemption can *only* be achieved by restricting competition.

In all cases, the approval of the Premier must be obtained before excepting legislation or regulations can be made.

ACCC authorisations/notifications

Any conduct covered by the Competition Code may be authorised except for misuse of market power. Conduct which would otherwise offend Part IV is permitted while an authorisation is in force.

An application for authorisation is made to the ACCC and will attract a fee of $7,500 (or $15,000 in the case of a merger). The ACCC will not grant an authorisation unless it is satisfied that the proposed conduct would result, or be likely to result, in a benefit to the public which would outweigh the detriment to the public constituted by any lessening of competition that would result, or be likely to result, if the proposed conduct were engaged in.

Conduct which would otherwise offend the *exclusive dealing* provisions of the Competition Code is permitted where notice of the conduct has been given to the ACCC, for so long as the ACCC has not withdrawn this protection. The ACCC can withdraw this protection by giving 30 days written notice if it is satisfied that the likely benefit to the public from the conduct will not outweigh the likely detriment to the public from the conduct.

Application to Local Government

The provisions of Part IV of the *Trade Practices Act* (as incorporated in the Competition Code) will apply to local government from 21 July 1996.

There are two exceptions. Section 2D of the TPA provides that the Competition Code *does not apply* to:

- *the refusal to grant, or the granting, suspension or variation of, licences (whether or not they are subject to conditions) by a local government body (a "licence" is defined to mean a licence that allows the licensee to supply goods or services); and*
- *a transaction involving only persons who are acting for the same local government body.*

In addition to the Competition Code, the TPA will directly apply (as it already does) to any local councils which are trading corporations as defined under the Commonwealth Constitution and/or to any local councils to the extent they are engaged in trade or commerce across two or more States. The exemptions mentioned above also apply in these circumstances.

It is stressed that the Competition Code is not a voluntary code, it is a law of Victoria with which councils must comply. All Victorian councils will be subject to the Code from 21 July 1996. While full pecuniary penalties will not apply until 21 July 1997, other remedies (eg damages and injunctions) will be available from 21 July 1996.

On 5 September 1995, the Director of the Office of Local Government wrote to the Chief Executive Officers of all Victorian councils, outlining the contents of the Competition Code and recommending that councils obtain appropriate legal advice as to whether or not their activities will be in breach of the Code.

The Director noted that, to the extent that any of a council's activities do breach the Competition Code, changes will need to be made or, if absolutely necessary, an exemption or authorisation obtained.

What is expected of Local Government?

From July 1996, the Competition Code is a law of Victoria. Penalties for breach of the Code can be severe and ignorance of the law will not count in defence of any breach. All councils that have not already done so are strongly advised to conduct an audit of their activities to identify any conduct which may contravene the Competition Code.

While it is not possible to provide an exhaustive listing of all forms of conduct that may contravene the Code, the following forms of conduct in particular should be avoided:

- discussing prices with competitors;
- agreements with competitors to share or split up a market;
- agreements to refuse to deal with a particular person;
- discussing customers or other competitors with persons who may be a competitor;
- imposing re-sale prices on customers to which goods or services are supplied;
- withholding or threatening to withhold goods or services for the purpose, or with the effect, of damaging a competitor.

These will not apply in circumstances where a joint tender is being prepared with a party, such as another council, which in other circumstances would be a competitor.

In auditing their activities, councils should review the terms of all existing contracts and arrangements to ensure that they do not contain any provisions which could breach the Competition Code. Contracts signed *before 19 August 1994* will be "grandfathered" (allowed to continue even if they breach the Code). However, this protection will not extend to any changes or extensions made to such contracts after that date. Any contracts entered into since 19 August 1994 and intended to last beyond 21 July 1996 will need to be reviewed and modified if necessary in order to comply with the Code.

As a matter of good risk management practice, councils should also develop and implement ongoing compliance programs to ensure that they continue to act in accordance with the provisions of the Code. Not only are there hefty fines for breach of the Code, the costs involved in litigation can be considerable. An effective compliance program should start with identification of the markets in which councils are participants - who are the suppliers, customers and competitors. The next step is to identify who within the organisation may be at risk of contravening the law and to make sure that appropriate action is taken to educate those persons so that they know where the risks are and who to turn to if they are in any doubt. For ongoing reference, councils should consider developing a compliance manual tailored to their business environment.

To assist organisations to comply with the Trade Practices Act, the ACCC publishes a manual on trade practices compliance entitled 'Best and Fairest'. This guide can be obtained from the Melbourne office of the ACCC which is located at:

Level 35, The Tower
360 Elizabeth Street, Melbourne
Tel: (03) 9290 1800
Fax: (03) 9663 3699

Areas where councils could be at risk of engaging in conduct which could breach the Competition Code include:

- arrangements with other councils to charge agreed fees for a particular service or use of a facility;
- misuse of regulatory powers to damage a competitor in a market for which the council is in competition with other suppliers; and
- use of profits from monopoly activities to subsidise competitive activities with the purpose or intent of damaging a competitor (predatory pricing).

Councils should place particular emphasis on ensuring that the provisions of the Competition Code are complied with in competitive tendering processes.

In addition, the *Victorian Local Government Code of Tendering* requires a council to "ensure that the tender process used is fair to all parties, and use its best endeavours to demonstrate that fairness to tenderers and potential tenderers." Specifically, the Code of Tendering obliges a council to:

- package work put to tender in a manner which encourages competition and the best outcome for residents and ratepayers;
- not participate in, and actively discourage other parties from, improper tendering practices such as collusion, misrepresentation, and disclosure of confidential information; and
- require any conflict of interest to be disclosed immediately.

'If a less efficient Government business is able to rely on net competitive advantages to take business from a more efficient firm, society's resources are not being put to their best use'

National Competition Policy
Report of Independent Committee of Inquiry, 1993 p 297

Background

The principle of competitive neutrality is that business activities of government owned bodies should not enjoy any net competitive advantage simply as a result of public sector ownership.

The Hilmer Report identified a number of advantages accruing to government owned business, including:

- immunity from various taxes and charges;
- immunity from various regulatory regimes;
- explicit or implicit government guarantees on debt;
- concessional interest rates on loans;
- not being required to account for depreciation expenses;
- not being required to achieve a commercial rate of return on assets; and
- effective immunity from bankruptcy.

The application of competitive neutrality policies to remove or offset any net competitive advantage resulting from the above is particularly important where there is direct competition, or potential competition, between public and private entities. In these circumstances, and all other things being equal, cost advantages enjoyed by the government owned entity would enable it to price its product below a more efficient private sector producer. By taking business away from a more efficient producer, resources may be wasted which could have been allocated to better uses and society as a whole would be the worse off.

COMPETITIVE NEUTRALITY

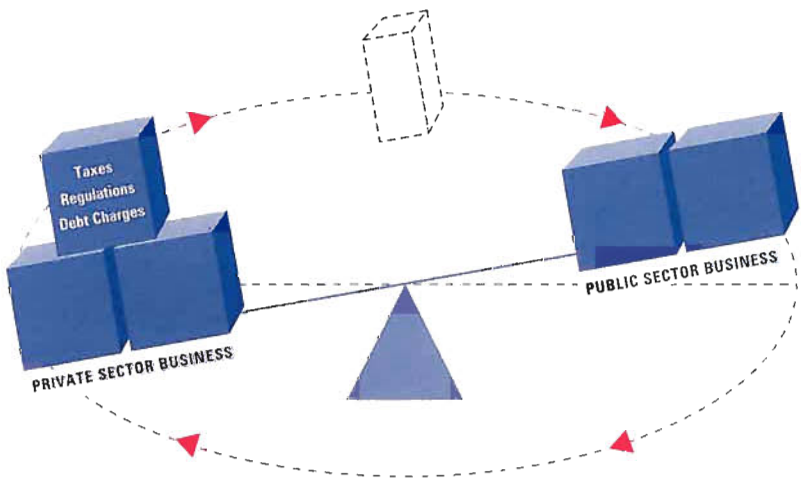


FIGURE 2

However, the presence of a competitive market is not essential. Even where direct exposure to competition is not possible, incentives for increased efficiency and improved service delivery can be provided by ensuring that government businesses are organised along similar lines and face similar costs and regulatory requirements to private corporations. It is with the objective of harnessing these incentives that the Victorian Government has adopted a corporatised structure for its major Government Business Enterprises and subjected them to equivalent taxation and commercial rate of return dividend requirements to a private corporation.

Coverage of competitive neutrality principles

Under the *Competition Principles Agreement*, except in cases where the implementation costs would outweigh the expected benefits in terms of increased efficiency and improved resource allocation, all governments agreed to apply policies of competitive neutrality to all significant Government Business Enterprises which are classified as Public Trading Enterprises (PTEs) or Public Financial Enterprises (PFEs).

Governments also agreed to implement competitive neutrality principles where appropriate to other "significant business activities" undertaken by government agencies as part of a broader range of functions.

The Victorian Government has determined that principles of competitive neutrality will also apply where competition is being introduced into the delivery of non-commercial services purchased by State and local government agencies on behalf of tax or ratepayers and where in-house bids are permitted in direct competition with private tenderers for the contract to supply those services. However, the principles will not extend to general governance functions.

It must be emphasised that the principle of competitive neutrality is concerned exclusively with economic efficiency objectives. Competitive neutrality policies aim to promote greater economic efficiency by removing or offsetting resource allocation distortions which result from competitive advantages conferred by government ownership. However, the pursuit of economic efficiency is but one among many public policy goals and is not intended to override any other economic, social or environmental policy objectives. It is to meet such public policy objectives that government seeks to ensure the provision of certain goods and services free or at less than full cost which the market would not otherwise provide in sufficient quantities or at a price affordable to all. In selecting the most appropriate supplier of such goods and services, the primary consideration for governments will be the capacity of alternative suppliers to deliver the specified service to the standards required. Only once these criteria are satisfied should considerations of relative efficiency be taken into account. It is at this point that the application of policies of competitive neutrality can help to ensure that competing bids are compared on an equivalent basis.

Policies to achieve competitive neutrality

The *Competition Principles Agreement* outlines two alternative approaches to the achievement of competitive neutrality, depending on the nature and significance of the business involved.

For significant Government Business Enterprises which are classified as "Public Trading Enterprises" (PTEs) and "Public Financial Enterprises" (PFEs), Clause 3(4) of the Agreement provides that a corporatisation model will be adopted where appropriate and the following will be imposed:

- full Commonwealth, State and Territory taxes or tax equivalent systems;
- debt guarantee fees directed towards offsetting the competitive advantages provided by government guarantees; and
- those regulations to which private sector businesses are normally subject, such as those relating to the protection of the environment, and planning and approval processes, on an equivalent basis to private sector competitors.

For "other significant business activities" undertaken as part of a broader range of functions, Clause 3(5) of the Agreement provides that either:

- the principles outlined in 3(4) will be implemented; or
- the Parties will ensure that the prices charged for goods and services will take account, where appropriate, of the above items, and reflect full cost attribution for these activities.

In either case, implementation of the principles is to be subject to the assessment that the benefits to be realised from implementation outweigh the costs.

The alternative approaches outlined in the *Competition Principles Agreement* represent just two options within a spectrum of possible structural, administrative and ownership options which can be employed to reduce or offset competitive advantages conferred by government ownership. These are depicted in summary form in Figure 3. Each shift to the right in Figure 3 represents a further step towards exposing a government business activity to the full commercial discipline of the market place.

At a minimum, offsetting net competitive advantages conferred by government ownership requires the adoption of *competitively neutral costing and pricing principles* for government business activities. This enables the consumer or purchaser of a service to select the most efficient among alternative suppliers of a given standard of service.

By itself, competitively neutral pricing is simply an accounting device. The business does not incur these costs directly and so will not face the same incentives to increase its internal efficiency. The efficacy of the pricing principles approach may therefore be enhanced by complementary structural and administrative reforms which seek to impose greater commercial discipline on the agency. Options range from the establishment of separate administrative units with their own operating accounts, through commercialisation (with full recovery of all expenses incurred in production and separate balance sheet and rate of return requirements) to full legal separation, exposure to corporations law and the imposition of the entire range of costs which would apply were the business in private ownership.

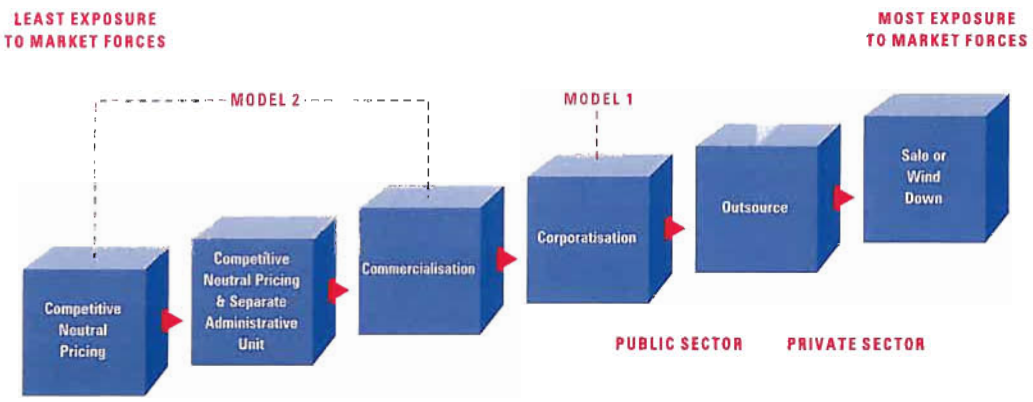


FIGURE 3

Victorian Government Policy on Competitive Neutrality

As required under the Competition Principles Agreement, in June 1996 the Victorian Government published a statement of its policy on competitive neutrality, including an implementation timetable and a complaints mechanism. The policy is to apply to both the State and local government sectors. The policy, entitled Competitive Neutrality: A Statement of Victorian Government Policy, is available from the Department of Premier and Cabinet.

Victorian Government policy on the application of competitive neutrality policies to significant government businesses and selected other activities is as follows:

For all significant State and local government business activities in Victoria undertaken primarily for profit or commercial purposes:

i) review of ongoing ownership arrangements, with consideration given to sale or wind-down; and

ii) application of either Model 1 or Model 2 competitive neutrality policies (see below) to all commercial activities remaining in government ownership, provided the expected benefits outweigh the costs.

In addition, for predominantly tax-funded or rate-funded areas of government activity:

iii) from July 1997, wherever competition is introduced into the supply of general government (predominantly tax-funded) activities for which the State Government or a local council is the sole purchaser ***and*** *in-house tenders are allowed, Model 2 competitive neutrality policies (see below) will apply to those activities.*

Competitive Neutrality Policies	Application
Model 1 • **corporatisation, including commercial accounting and rate of return requirements;** • **application of Commonwealth tax equivalent payments;** • **application of State tax or tax equivalent payments and of State utility charges;** • **application of local rate or rate equivalent payments;** • **application of debt guarantee fees;** • **application of relevant regulations to which the private sector is normally subject.**	Provided the benefits to be realised from implementation outweigh the costs, Model 1 policies will apply to: 1. *significant Government Business Enterprises* (GBEs) which are *Public Trading Enterprises* (PTEs) or *Public Financial Enterprises* (PFEs); and 2. *other significant government business activities* that are not PTEs or PFEs where: a) the activity is or has the potential to be in competition with the private sector; *and/or* b) there are expected to be improved resource allocation outcomes from removing net competitive advantages resulting from government ownership.
Model 2 • **examination of the most appropriate ongoing structural arrangements for the delivery of the business or service delivery activity, including commercialisation or the adoption of a Service Agency model; and** • **adoption of pricing principles which take account of and reflect full cost attribution for the net competitive advantages conferred on the activity by public sector ownership.**	Provided the benefits to be realised from implementation outweigh the costs, Model 2 policies will apply to: 1. *other commercial activities* of government entities (a substantial proportion of whose costs are met from user charges) where: a) the activity is or has the potential to be in competition with the private sector; and/or b) there are expected to be improved resource allocation outcomes from removing net competitive advantages resulting from government ownership; but c) the costs of implementing Model 1 policies would outweigh the benefits; and 2. non-commercial *general government (predominantly tax-funded) activities* where a) competition is being introduced to the supply of services to government; and b) in-house tenders are allowed.

Cost/benefit assessment

The *costs* of implementing competitive neutrality are primarily the transaction costs associated with implementation. Depending on which of Model 1 or Model 2 is applicable, these may include the costs of:

- separate incorporation;
- legislative and regulatory amendment;
- changes to management systems and processes;
- obtaining information and undertaking analysis to assess appropriate levels for tax equivalents, debt guarantee fees or pricing principles;
- administration of tax equivalent and debt guarantee frameworks; and
- compliance and the monitoring of compliance.

Costs may also include wider costs to the community as a whole if applying the policy would impede achievement of other public policy objectives.

The *benefits* of implementing competitive neutrality policies are the benefits to the community which accrue both from increased efficiency within the government owned business (technical efficiency) and from improved resource allocation when resources are freed up for more productive uses (allocative efficiency).

Complaints mechanism

As required under the *Competition Principles Agreement,* the Victorian Government Policy on Competitive Neutrality includes the establishment of a complaints mechanism to receive and investigate allegations of non-compliance with the policy. The complaints mechanism will be located in the Department of Treasury and Finance. It will have recommendatory powers only. Its coverage will extend to significant commercial activities of local councils, but will not cover activities subjected to competitive tender which will continue to be handled through the Office of Local Government.

Annual reporting requirements

Each Government has agreed to publish an annual report on the implementation of competitive neutrality principles within its jurisdiction, including allegations of non-compliance.

Competitive Neutrality in the Local Government context

A major focus of competitive neutrality is on enhancing the efficiency of the large public utilities which dominate the provision of energy, water and transportation services in Australia. With recent divestment of their public utility functions, Victorian local authorities are no longer engaged in significant business activities in these markets, although they may be engaged in other significant commercial undertakings where competitive neutrality principles will be relevant.

On the other hand, as a result of compulsory competitive tendering, Victorian councils are significantly further advanced than in other jurisdictions with introducing competition into the delivery of non-commercial activities of government. Accordingly, competitive

neutrality principles will be of greater relevance to these aspects of local government activity in Victoria than elsewhere.

The reform of local government in Victoria and, in particular, the ongoing implementation of competitive tendering, means that councils should be well placed to meet most competitive neutrality requirements by July 1997.

Competitive tendering has instilled in local government a competitive culture and is requiring councils to assess tenders for the provision of goods and services on a commercial basis.

The requirement that councils clearly separate their role as a "purchaser" of services from that as a "provider", to ensure the fairness of the tender process, has led to significant internal restructuring within councils and the formation of separate business units to bid for council contracts.

Competitive neutrality principles will complement and reinforce the *Victorian Local Government Code of Tendering* which obliges councils to assess in-house bids and external tenders on the same terms. Under the Code, councils are to treat an in-house tender on the same terms as an external tenderer. There is to be a clear separation between in-house tenders and those evaluating the tenders.

The Code obliges councils to prepare in-house tenders on the basis that all direct costs and indirect or overhead costs attributable to the tender are included. The requirements of competitive tendering have resulted in a number of councils giving consideration to the corporatisation of certain business activities, to allow these to operate as a separate legal entity on a commercial basis.

Application to Local Government

Consistent with Victorian Government policy, councils will be required to apply competitive neutrality principles to:

- significant local government businesses engaged in primarily for profit or commercial purposes,
- in-house bids for the supply of non-commercial activities subject to competitive tendering.

Councils should apply either Model 1 or Model 2 policies to these activities, subject in each case to the assessment that the benefits in terms of improved efficiency and better resource allocation would outweigh the costs of implementation.

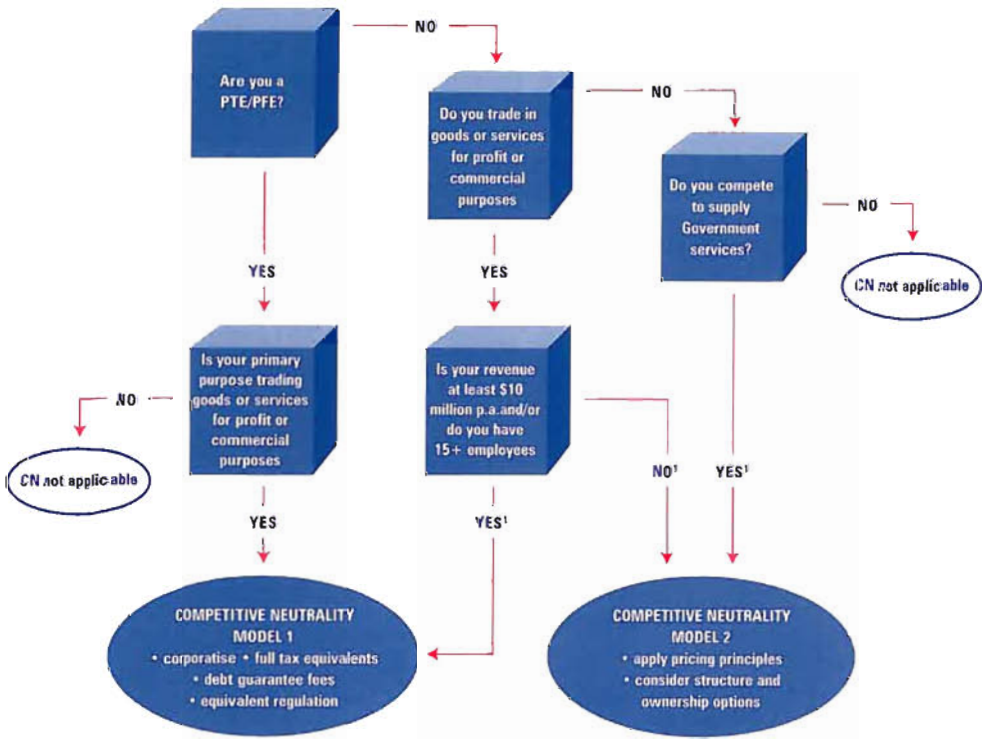
The decision tree set out in Figure 4 illustrates the key steps involved in determining where competitive neutrality policies should apply and which approach (Model 1 or Model 2) to employ in each case.

The first step is to determine whether the business meets the ABS definition of a public trading enterprise (PTE) or a public financial enterprise (PFE). To satisfy this definition, the predominant activity of the business would need to be trade in goods and/or services *and* the business would need to meet a substantial part of its operating costs or earn a substantial part of its operating revenue from user charges.

If the answer to these questions is yes, the next step is to verify that the business has a predominantly commercial or profit making focus. If not, competitive neutrality is unlikely to be relevant. If yes, Model 1 policies should be applied, subject to the assessment that the benefits would outweigh the costs.

If the business activity does *not* satisfy the ABS definition of a PTE or a PFE, the next step is to determine whether the business is nevertheless engaged in trade in goods or services for profit or commercial purposes. If yes, competitive neutrality policies are applicable, but which of Model 1 or Model 2 should apply depends on the scale of the operation and its significance in the relevant market. As a guide, a business would need annual revenues of at least $10 million or a workforce of at least 15 to warrant the adoption of Model 1 policies, and careful weighing up of the costs and benefits of corporatisation should occur for organisations with revenue bases between $10 million and $20 million. Otherwise, Model 2 should be applied.

Finally, if a business is *not* engaged in trade primarily for profit or commercial purposes, it needs to be established whether the business is in actual or potential competition with the private sector for the supply of goods or services to government. This will be the case for all non-commercial activities subject to competitive tender, and Model 2 policies will generally be applicable in all such cases. (The exception would be if a council team were to bid for government work *outside* its own municipality, when Model 1 policies would apply.)



Note 1: subject to an assessment of the costs and benefits of applying the policy

FIGURE 4

Model 1 - corporatisation approach

Where councils are engaged in significant commercial activities traded in the open market, they will need to consider possible corporatisation of those activities and the adoption of the full suite of competitive neutrality policies contained in Model 1 - viz: the application of tax equivalents and debt guarantee fees where appropriate and equivalent regulations to those applying to private corporations.

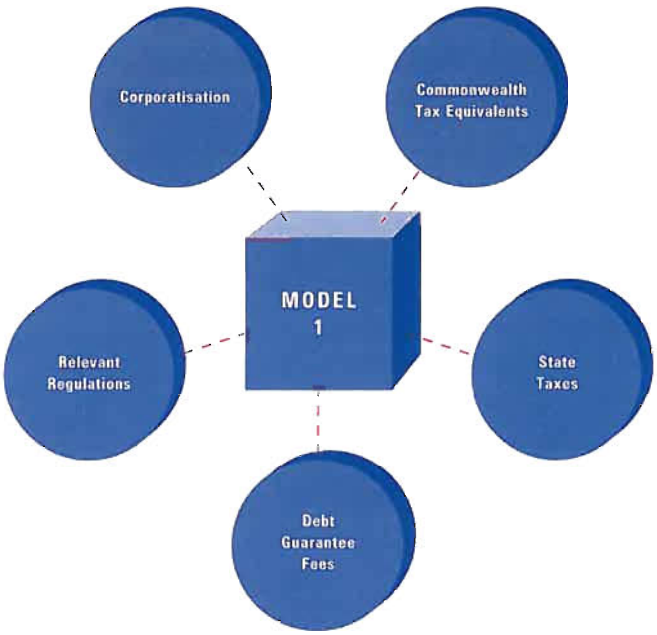


FIGURE 5

It is not the intent of National Competition Policy that State or Local Government authorities shift their focus toward selling services in the private market. On the contrary, competition policy in general, and the principle of competitive neutrality in particular, may have the effect of discouraging government agencies from entering into or remaining in areas of business activity which can be provided more efficiently by the private sector. Nor should councils actively seek or encourage product or market diversification, other than where the State has endorsed such action (for example in tourism or waste management). Nevertheless, circumstances may arise where a council seeks involvement in business activities outside council operations or beyond its municipal boundaries. Any such changes away from traditional rate revenue sources into different product and market areas or to other municipalities in competition with the private sector must be assessed from a total risk management perspective. There will be strict standards for the sorts of business form adopted to ensure commercial viability.

Separate incorporation requires statutory approval under Section 193 of the *Local Government Act* 1989. As part of the approval process, the Treasurer and the Minister for Local Government will require issues of competitive neutrality to be addressed. Thus far, one wholly owned company has been approved - City Wide Service Solutions Pty Ltd, which is owned by the Melbourne City Council. Discussions are currently underway on three further applications, for companies to manage the Queen Victoria Market, the Melbourne Wholesale Fish Market and the Prahran Market.

So that the effects of the reforms to the structure and operations of local government in Victoria are not compromised, proposals for incorporation will be considered by the Department of Treasury and Finance and the Office of Local Government against the guidelines set out below. It should be noted, however, that Ministerial approval under Section 193 does not represent a guarantee or acceptance of liability by the State Government in relation to liabilities incurred, or into any aspects of the future funding of any particular project. This remains the responsibility of the proponent council.

- it will be to councils' advantage to discuss and seek in-principle approval for any incorporation well before there is significant commitment of resources, including management time;
- proposals should be fully costed. This should include cost attribution for competitive neutrality factors a such as tax equivalents and debt guarantee fess, where applicable;
- factors such as the optimum utilisation of plant and equipment should be considered only after a council takes account of minimum requirements, including its obligations for emergency management;
- specific council incorporation proposals will be assessed, in the first instance, on commercial criteria using appropriate hurdle rates of return. Proposals should show these criteria, including an analysis of the risk/return trade-off. Councils should indicate clearly the proposed method of financing and its impact on the council's financial structure. When proposing an entrepreneurial venture, a council will need to demonstrate not only the financial viability of the project, but also that the council itself has the capacity, given its overall financial status, to cope with any unforseen event that could jeopardise the viability of the project. In addition, a council will need to consider the Loan Council implications of any proposed borrowing it intends to undertake in facilitating the project;
- the council's proposal should demonstrate, in diversification into activities outside council, that private sector entities do not already adequately provide the activity or service; and
- incorporation proposals should clearly show the accountability links that council will establish for the entity. At a minimum, this will cover the formal organisational links, the shareholding (if any), the process for Board appointments, and the monitoring, financial and audit arrangements.

The Government, through the Office of Local Government and the Department of Treasury and Finance, will provide assistance to councils on request in determining the appropriate corporate structure for their significant business activities.

Model 2 - Competitively neutral pricing principles

For local government commercial activities which do not satisfy cost-benefit criteria for separate incorporation and the application of full tax equivalent regimes required under Model 1, councils will need to consider the application of Model 2 policies.

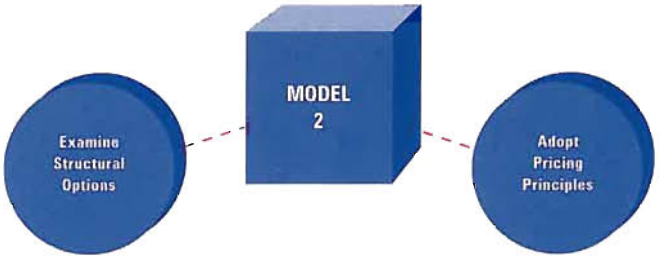


FIGURE 6

Model 2 policies will for the most part also apply to non-commercial local government activities subjected to competitive tendering.

Application of Model 2 competitive neutrality policies calls for an examination of the ongoing structural and administrative arrangements for the business activity, and the adoption of competitively neutral pricing principles to the goods or services produced by the activity.

Review of ongoing structures

The application of competitive neutrality principles using Model 2 will require councils to examine the most appropriate ongoing structure for the delivery of the activity. Some possible structural and administrative options for ongoing business activities were depicted in Figure 3. Consideration should be given to at least the following options:

- outsourcing;
- commercialisation; or
- administrative reorganisation.

As more contracts are put to tender as part of the implementation of CCT, in-house teams will inevitably lose some contracts and win others, including some for external work. By the time councils are market testing 50 per cent of their total expenditure, which is required by the 1996-97 financial year, it will be clear what business activities they will continue to maintain. Councils will then be in a position to consider appropriate administrative structures for those activities.

Consistent with the competitive neutrality provisions of the *Competition Principles Agreement,* it is expected that, by July 1997, all councils will have reviewed the organisational structure of their business activities which compete with the private sector.

The application of competitive neutrality policies to significant business enterprises in which councils are engaged primarily for profit or commercial purposes will be subject to the State's competitive neutrality complaints mechanism to be established within the Department of Treasury and Finance.

Competitively neutral pricing principles

In adopting competitively neutral pricing, councils should be guided by the principles set out in the Box below.

The issue of taxation neutrality is central to the promotion of a level playing field between in-house and private sector tenders. A number of private sector tenderers have expressed concerns that in-house teams appear to have taxation advantages when bidding for council work.

In 1995, the Office of Local Government engaged consultants to investigate the effect of taxation issues on the comparative costing of bids for council tenders. The resulting *Report on Taxation Issues in Compulsory Competitive Tendering in Local Government* concluded that, while the most significant taxes in this context are sales tax and payroll tax, the impact of these taxes varies with the nature and structure of the work tendered by a council.

The incidence of sales and payroll taxes does not always benefit an in-house bid. For example, payroll tax is only payable by bidders whose total payroll costs exceed a certain threshold amount. (In 1995-96 the threshold payroll was $515,000, representing a workforce of around 17-20 employees.) Moreover, since local government is exempt from sales tax with respect to the purchase of goods required for the ordinary services of government, most council contracts can and should be structured so that any provider can obtain sales tax exemption.

While other Commonwealth taxes (mainly company tax where applicable), and State taxes (including taxes on land, financial transactions and transfer of assets) may marginally affect the comparability of in-house and external bids, these taxes will generally represent only a small proportion of total business costs and will not be a deciding factor in the selection of a supplier. However, if accounting for these costs would materially affect the cost to council of a service which, were it provided in-house, would be exempt from such taxes, this component of competitive neutrality pricing principles should not apply on the grounds that costs would outweigh benefits.

Reciprocal taxing and charging between State and Local Government

To facilitate the future application of competitively neutral pricing principles to State and local government business activities and to situations of competitive tendering for the supply of general government services, the Victorian Government is prepared to give consideration to the principle of reciprocal taxing and charging between the State and local government sectors. However, it is recognised that this could have unintended distributional consequences for local government finances. Moreover, taxing between levels of government cannot be considered in isolation. It should only be considered in the context of a comprehensive review of national taxation policy and implemented as part of a broader package of tax reform.

Model 2: Competitive Neutrality Pricing Principles

The following pricing principles are to apply to all activities subject to Model 2 competitive neutrality policies:

1. **Pricing should reflect full attribution of all costs incurred in the production of the good or service.** All expenses used in the provision of a unit of the good or service, including cash and non-cash items, should be accounted for. Costs may include direct labour costs, labour on-costs, materials and other operating expenses, accommodation and corporate overheads.
2. **Pricing should include the net effect of any competitive advantages/disadvantages due solely to Government ownership.** To the base of all costs actually incurred should be added costs which would be faced by a private sector provider of similar goods or services but from which government providers are exempt or face lower costs due to government ownership, less the costs of any significant competitive disadvantages resulting from public sector ownership.
3. **The decision process should be transparent and defensible.** The manner in which competitively neutral pricing principles have been applied should be fully documented and reasons given for the inclusion or exclusion of any relevant cost. For example, where a judgement is made that a particular cost is not relevant, or that a competitive advantage is fully offset by a competitive disadvantage, the reasoning behind such judgements should be documented.

The application of these pricing principles is not a cost recovery exercise. Where government decides on public policy grounds to supply certain goods or services free or at well below cost, competitively neutral pricing principles are not intended to disturb these objectives in any way. However, they will affect the manner in which those activities are 'priced' or 'costed' by in-house bidders for contracts to supply those services. Similarly, where government decides for public policy reasons to apply a subsidy to some or all consumers of commercially provided goods or services, that subsidy should be explicitly recognised in the costing of those services. Where government subjects the delivery of such services to competitive tender, the government subsidy to support the CSO component should be equally available to in-house and external tenders.

What is expected of Local Government?

The application of competitive neutrality principles to Victorian local government business activities will impose relatively few additional requirements on councils. Competitive neutrality principles should be applied wherever councils are engaged in commercial activities or have introduced competition into the delivery of services. They are not intended to apply to regulatory or general governance functions.

- The date by which councils will be required to review the structure of their business activities and/or apply (Model 2) competitively neutral pricing principles has been set at July 1997. This is in recognition that the timetable for the implementation of CCT require, by that time, all Victorian councils to be competitively tendering at least 50 per cent of their total expenses. This means that, by July 1997, all councils should have already subjected the structure and pricing of their activities to close scrutiny.
- Where a council considers that Model 1 policies should be applied to a significant, ongoing business activity, involving corporatisation and the imposition of tax equivalent payments, this will need to be formally approved by the Minister and the Treasurer, and longer lead times will be involved in implementation. Accordingly, it is proposed that July 1998 be the target date for the application of Model 1 policies to any significant existing local government business activities approved for corporatisation.
- In accordance with sub-clause 3(10) of the *Competition Principles Agreement*, councils will be required to report annually on the implementation of competitive neutrality principles. This requirement will apply from September 1997, commencing with annual report for the 1996-97 financial year.
- Corporatised council business activities and other significant commercial activities of local government will be subject to the complaints mechanism to be established within the Department of Treasury and Finance to investigate allegations of non-compliance with the government's policy on competitive neutrality.
- The application of competitive neutrality policies to non-commercial activities which are competitively tendered under CCT will *not* be subject to the general competitive neutrality complaints mechanism. Rather, these activities will be subject to the complaints process established by the Office of Local Government in relation to CCT.
- In their annual reports on the implementation of competitive neutrality principles, councils will be required to include a report on action taken or proposed to deal with substantiated allegations of non-compliance with the policy.

6. LEGISLATION REVIEW

"If Australia is to take competition and competition policy seriously, a new mechanism is required to ensure that regulatory restrictions on competition do not exceed what is justified in the public interest."

National Competition Policy
Report of Independent Committee
of Inquiry, 1993 p.185

Background

The Hilmer Report found that legislative and regulatory restrictions were among the most pervasive forms of restriction on competition in the Australian economy.

All Australian Governments have agreed that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:

a) the benefits of the restriction to the community as a whole outweigh the costs, and

b) the objectives of the legislation can only be achieved by restricting competition.

Consistent with this principle, all Governments have to review legislation that restricts competition by December 2000. Thereafter, legislation is to be reviewed every ten years. Governments have also agreed to ensure that any proposed new legislation complies with the above principles.

LEGISLATIVE REVIEW PRINCIPLES

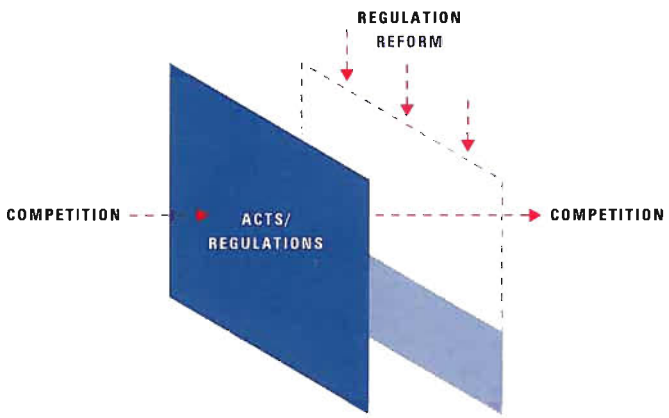


FIGURE 7

Application to Local Government

Local government is subject to three forms of Victorian law:

- State enabling legislation – laws establishing and governing the operation of local government (*Local Government Act* 1989 (Vic));
- other State legislation, including planning schemes, conferring specific powers and responsibilities on local government; and
- local laws made under powers conferred by the enabling legislation.

In accordance with the *Competition Principles Agreement,* the Victorian Government has prepared a timetable for the review and, where appropriate, reform of State Government legislation which restricts competition, including restrictions contained in legislation conferring specific powers and responsibilities on local government.

Review of local laws

Local laws which restrict competition must also be reviewed and, where appropriate, reformed over the period to the year 2000.

There are at present some 1700 local laws in place in Victoria. Those which were made by former councils prior to amalgamation are sunsetted one year after the abolition of those councils.

While the local laws currently in place cover a wide variety of matters, the overwhelming majority are unlikely to have any impact on competition. However, there are some areas in which local laws could be construed as restricting competition. These include:

- traffic regulation and parking;
- shop trading hours;
- trading on footpaths and signage;
- itinerant traders; and
- local laws made subsequent to State Government deregulation of a sector that are contrary to that deregulatory intention.

On 7 September 1995, the Victorian Minister for Local Government made a referral to the Local Government Board to conduct a review of local laws provisions contained in Part 5 of the *Local Government Act* 1989, in particular to assess how any adverse impacts on economic activity can be addressed.

In undertaking the review, the Minister requested that the Board should have regard to the Government's reform goals and to the goals of National Competition Policy.

In May 1996 the Local Government Board released a discussion paper canvassing views on four possible options for the future of local laws, as follows:

1. existing power of councils to make local laws on a wide range of topics would be maintained but backed by a *voluntary* code on the preparation of local laws consistent with agreed principles, including more extensive procedures for community consultation and legal scrutiny;
2. existing power of council to make local laws retained but new *statutory* requirements applied to formalise compliance with agreed principles, including more extensive procedures for community consultation and legal scrutiny;

3. adoption of *model local laws* on an agreed range of topics prepared jointly by State and local government, with local variations on these subject to more formal consultation processes, and with councils retaining the right to introduce local laws not covered by the model provided they comply with agreed principles as above; and

4. *statutory limits* on the range of matters on which local laws can be made, possibly in combination with the model laws model outlined in option 3.

Whichever of these options is ultimately adopted, the revocation or review of local laws that restrict competition will be completed by no later than June 1999.

In addition, by July 1997, approval processes for making or amending local laws will be in place to ensure that such laws do not restrict competition unless it is demonstrated that the benefits of the restriction to the community as a whole outweigh the costs and that the objectives of the legislation can only be achieved by restricting competition.

Annual reporting requirements

The Competition Principles Agreement includes a commitment by each jurisdiction to publish annual reports on progress with the review and reform of legislative restrictions on competition. This reporting requirement commences with the year ending 30 June 1997.

The Minister for Planning and Local Government will be responsible for providing reports to the Premier on progress in implementing the review and reform of local laws which restrict competition. Individual councils will be responsible for reporting annually on any new local laws which restrict competition. The Premier will compile a report for Victoria that will be published in line with the requirements of the *Competition Principles Agreement*.

"The removal of regulatory restrictions on competition may not necessarily... be sufficient to foster effective competition in sectors currently dominated by public monopolies... structural reform of existing public monopolies may be required, as governments have recognised with reforms in place or underway in a number of sectors."

National Competition Policy
Report of Independent Committee
of Inquiry, 1993 p.185

Background

While each State and Territory Government remains free to determine its own agenda for the reform of public monopolies, the *Competition Principles Agreement* contains provisions that apply where competition is to be introduced to a sector traditionally supplied by a public monopoly.

All Governments have agreed that:

- before competition is introduced to a sector traditionally supplied by a public monopoly, responsibilities for industry regulation will be removed from the public monopoly; and
- before competition is introduced to a market traditionally supplied by a public monopoly, or before a public monopoly is privatised, a government will review such matters as the entity's appropriate commercial objectives, separation of natural monopoly from potentially competitive elements, separation of regulatory from commercial functions and implementation of competitive neutrality.

Application to Local Government

Section 2 referred to the divestment that has taken place in recent years in Victoria of councils' water and sewerage services and electricity distribution businesses.

These reforms, which have resulted in the progressive privatisation or corporatisation of a number of these businesses, have also allowed local government to focus on its core service and governance responsibilities.

The Victorian situation now contrasts strongly with that in Queensland, and to a slightly lesser extent, New South Wales and Tasmania, where local government continues to play a significant role in the provision of utility services.

With the divestment of councils' utility responsibilities, the structural reform provisions of the *Competition Principles Agreement* are not considered to be relevant to local government in Victoria.

In the context of competitive tendering, however, similar principles will be applicable to the separation of a council's regulatory functions from activities exposed to competitive tender, as will implementation of competitive neutrality principles.

"Where a firm is not subject to effective competitive pressure... it may be able to restrict output and charge higher prices than would be possible in a contestable market. This behaviour is known as 'monopoly pricing' and can result in higher prices to consumers and a misallocation of resources."

National Competition Policy Report of Independent Committee of Inquiry, 1993 p.270

Background

The *Prices Surveillance Authority Act* 1983 provides for prices oversight of private enterprises and Commonwealth Government Business Enterprises that are monopoly or near monopoly suppliers of goods or services.

Under the *Competition Principles Agreement,* prices oversight of State and Territory business enterprises remains primarily the responsibility of the State or Territory that owns the enterprise. However, State and Territory Governments have agreed to consider establishing independent sources of price oversight of their GBEs, where such oversight does not exist.

The *Prices Surveillance Authority Act* has also been amended to permit price oversight of State and Territory Government businesses in certain circumstances.

Application to Local Government

The prices oversight provisions of the *Competition Principles Agreement* are not considered to be applicable to local government in Victoria as councils have few, if any, enterprises that are monopoly or near monopoly suppliers of goods or services.

It is expected that the pricing of general council services in Victoria will become increasingly competitive over time through the continuing implementation of compulsory competitive tendering.

9. ACCESS TO ESSENTIAL FACILITIES

"Introducing competition in some markets requires competitors to be assured of access to certain facilities - referred to as 'essential facilities' - that cannot be duplicated economically."

National Competition Policy Report of Independent Committee of Inquiry, 1993 p.186

Background

Access to strategic essential facilities may be necessary if a party is to compete in certain markets. These essential facilities will be natural monopolies where access is necessary to enable effective competition in a market.

Under the *Competition Principles Agreement,* all Governments have agreed on a framework for third party access to services provided by significant infrastructure facilities.

The *Commonwealth Competition Policy Reform Act* 1995 establishes a national regime for third party access to services provided by means of nationally significant infrastructure facilities. The *Competition Principles Agreement* provides for the establishment of State or Territory based access regimes in accordance with a set of agreed principles.

Application to Local Government

The essential services access provisions of the *Competition Principles Agreement* are not considered to be applicable to local government in Victoria. The access provisions concern the establishment of mechanisms to grant third parties legal 'rights' to negotiate access on reasonable terms to essential services provided by certain infrastructure facilities. It is understood that these provisions relate only to access to services provided through "significant infrastructure assets" which have natural monopoly characteristics.

With the recent divestment of local government's water and sewerage service and electricity distribution responsibilities, it is highly unlikely that Victorian local government would be considered responsible for "significant infrastructure assets".

However, the *concept* of providing access to council facilities in the context of compulsory competitive tendering is one which local councils might consider as a strategy for stimulating greater competition. When calling for tenders for the supply of services to its ratepayers, for example, the City of Melbourne offers private tenderers access to council facilities and equipment on the same terms as these are available to its in-house team, City-Wide Services Solutions Pty Ltd.

In implementing competitive neutrality policies, all Governments have agreed to impose full Commonwealth, State and Territory taxes or tax equivalents on those of their significant Government business enterprises which are classified as Public Trading Enterprises or Public Financial Enterprises.

The Statement of Victorian Government Policy on Competitive Neutrality indicates that State Government Business Enterprises subject to Model 1 competitive neutrality policies will generally be liable for all State taxes and charges that would apply were the business in private ownership and will also be liable for Commonwealth tax equivalents and for local government rates or rate equivalents.

Conversely, significant local government business enterprises with a primary commercial or profit-making focus should be liable for all relevant Commonwealth and State taxes or tax equivalents.

Current tax/rate status of State and Local Government business enterprises

The current situation with regard to liability of local government for State taxes is that:

- local government activities are generally liable for State taxes where the activity is undertaken primarily for profit or commercial purposes; and
- local government activities undertaken for public or municipal purposes are generally exempt from State taxes.

Conversely, property used by State government entities primarily for public (as opposed to commercial) purposes is generally exempt from local government rates, but State government businesses will generally be liable for local government rates. However, there is a general exemption for property vested in the Crown.

Where a State government business is privatised or partially privatised, it is likely to be rateable. Under a 1993 Victorian Government policy, privatised entities are liable to pay rates to local government.

In addition, in the case of certain large scale assets such as electricity generation plants, entities are required to make payments in lieu of rates.

As the Victorian Government progressively reviews the future structure and ownership of particular business enterprises, decisions on the rateability of assets are being made. As a result of reforms made to date:

- the five privatised electricity distribution companies are now liable for local government rates;
- electricity generation companies are now required to make payments to councils in lieu of rates, by agreement with the council, both prior to and following privatisation;
- the three metropolitan water distribution companies (which are State owned companies) - City West Water, Yarra Valley Water and South East Water - are not specifically exempt from rates but most of the land which they occupy, being Crown land, is not rateable; and
- with respect to ports, the Ports of Portland and Geelong have been sold and subsequent owners will be rateable. The Melbourne Ports Corporation, which will carry out the functions of a commercial landlord, will remain in State ownership but will be liable for rates.

To facilitate the future application of competitive neutrality principles to the State and local government sectors, the Victorian Government is prepared to give consideration to reciprocal charging between the State and local government sectors through removal of all current tax and rate exemptions. However, taxing between levels of government should only be considered in the context of a comprehensive review of national taxation policy and implemented as part of a broader package of tax reform.

APPENDIX A: LIST OF PUBLICATIONS
COMPULSORY COMPETITIVE TENDERING

Audit of CCT Procedures in Councils 1995,
Office of Local Government, November 1995.

Better Service, Best Value: Competitive Tendering - Minister's Report on the First Year of CCT,
Office Of Local Government, November 1995.

Compulsory Competitive Tendering - Draft Report,
Local Government Board, November 1993.

Compulsory Competitive Tendering - Final Report,
Local Government Board, December 1993.

Compulsory Competitive Tendering - Models For Organisational Structure,
Office of Local Government (Nicole Morgan), December 1994.

Compulsory Competitive Tendering - Procedures Manual,
Local Government Industry Working Party, August 1994.

Minister's Review - Local Government in 1993,
Office of Local Government, December 1993.

Minister's Review: It's Coming Together - Local Government in 1994,
Office of Local Government, December 1994.

Minister's Review: First Fruits of Reform - Local Government in 1995,
Office of Local Government, January 1996.

Report on Taxation Issues in Compulsory Competitive Tendering in Local Government,
Arthur Andersen, August 1995

Value For Money - Case Studies in Competitive Tendering and Contracting in Local Government,
Office of Local Government, June 1994.

Victorian Local Government Code Of Tendering,
Office of Local Government, August 1995.

Competition Principles Agreement between

The Commonwealth of Australia

The State of New South Wales

The State of Victoria

The State of Queensland

The State of Western Australia

The State of South Australia

The State of Tasmania

The Australian Capital Territory, and

The Northern Territory of Australia

WHEREAS the Council of Australian Governments at its meeting in Hobart on 25 February 1994 agreed to the principles of competition policy articulated in the report of the National Competition Policy Review;

AND WHEREAS the Parties intend to achieve and maintain consistent and complementary competition laws and policies which will apply to all businesses in Australia regardless of ownership;

The Commonwealth of Australia

The State of New South Wales

The State of Victoria

The State of Queensland

The State of Western Australia

The State of South Australia

The State of Tasmania

The Australian Capital Territory, and

The Northern Territory Of Australia

agree as follows:

Interpretation

1. (1) In this Agreement, unless the context indicates otherwise:

"Commission" means the Australian Competition and Consumer Commission established by the Trade Practices Act;

"Commonwealth Minister" means the Commonwealth Minister responsible for competition policy;

"constitutional trade or commerce" means:

(a) trade or commerce among the States;

(b) trade or commerce between a State and a Territory or between two Territories; or

(c) trade or commerce between Australia and a place outside Australia;

"Council" means the National Competition Council established by the Trade Practices Act;

"jurisdiction" means the Commonwealth, a State, the Australian Capital Territory or the Northern Territory of Australia;

"Party" means a jurisdiction that has executed, and has not withdrawn from, this Agreement;

"Trade Practices Act" means the *Trade Practices Act* 1974.

(2) Where this Agreement refers to a provision in legislation which has not been enacted at the date of commencement of this Agreement, or to an entity which has not been established at the date of commencement of this Agreement, this Agreement will apply in respect of the provision or entity from the date when the provision or entity commences operation.

(3) 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.

(4) It is not intended that the matters set out in subclause (3) should affect the interpretation of "public benefit" for purposes of authorisations or notifications under the Trade Practices Act.

(5) This Agreement is neutral with respect to the nature and form of ownership of business enterprises. It is not intended to promote public or private ownership.

Prices Oversight of Government Business Enterprises

2. (1) Prices oversight of State and Territory Government business enterprises is primarily the responsibility of the State or Territory that owns the enterprise.

(2) The Parties will work cooperatively to examine issues associated with prices oversight of Government business enterprises and may seek assistance in this regard from the Council. The Council may provide such assistance in accordance with the Council's work program.

(3) In accordance with these principles, State and Territory Parties will consider establishing independent sources of price oversight advice where these do not exist.

(4) An independent source of price oversight advice should have the following characteristics:

(a) it should be independent from the Government business enterprise whose prices are being assessed;

(b) its prime objective should be one of efficient resource allocation but with regard to any explicitly identified and defined community service obligations imposed on a business enterprise by the Government or legislature of the jurisdiction that owns the enterprise;

(c) it should apply to all significant Government business enterprises that are monopoly, or near monopoly, suppliers of goods or services (or both);

(d) it should permit submissions by interested persons; and

(e) its pricing recommendations, and the reasons for them, should be published.

(5) A Party may generally or on a case-by-case basis:

(a) with the agreement of the Commonwealth, subject its Government business enterprises to a prices oversight mechanism administered by the Commission; or

(b) with the agreement of another jurisdiction, subject its Government business enterprises to the pricing oversight process of that jurisdiction.

(6) In the absence of the consent of the Party that owns the enterprise, a State or Territory Government business enterprise will only be subject to a prices oversight mechanism administered by the Commission if:

(a) the enterprise is not already subject to a source of price oversight advice which is independent in terms of the principles set out in subclause (4);

(b) a jurisdiction which considers that it is adversely affected by the lack of price oversight (an "affected jurisdiction") has consulted the Party that owns the enterprise, and the matter is not resolved to the satisfaction of the affected jurisdiction;

(c) the affected jurisdiction has then brought the matter to the attention of the Council and the Council has decided:

(i) that the condition in paragraph (a) exists; and

(ii) that the pricing of the enterprise has a significant direct or indirect impact on constitutional trade or commerce;

(d) the Council has recommended that the Commonwealth Minister declare the enterprise for price surveillance by the Commission; and

(e) the Commonwealth Minister has consulted the Party that owns the enterprise.

Competitive Neutrality Policy and Principles

3. (1) The objective of competitive neutrality policy is the elimination of resource allocation distortions arising out of the public ownership of entities engaged in significant business activities: Government businesses should not enjoy any net competitive advantage simply as a result of their public sector ownership. These principles only apply to the business activities of publicly owned entities, not to the non-business, non-profit activities of these entities.

(2) Each Party is free to determine its own agenda for the implementation of competitive neutrality principles.

(3) A Party may seek assistance with the implementation of competitive neutrality principles from the Council. The Council may provide such assistance in accordance with the Council's work program.

(4) Subject to subclause (6), for significant Government business enterprises which are classified as "Public Trading Enterprises" and "Public Financial Enterprises" under the Government Financial Statistics Classification:

(a) the Parties will, where appropriate, adopt a corporatisation model for these Government business enterprises (noting that a possible approach to corporatisation is the model developed by the inter-governmental committee responsible for GTE National Performance Monitoring); and

(b) the Parties will impose on the Government business enterprise:

(i) full Commonwealth, State and Territory taxes or tax equivalent systems;

(ii) debt guarantee fees directed towards offsetting the competitive advantages provided by government guarantees; and

(iii) those regulations to which private sector businesses are normally subject, such as those relating to the protection of the environment, and planning and approval processes, on an equivalent basis to private sector competitors.

(5) Subject to subclause (6), where an agency (other than an agency covered by subclause (4)) undertakes significant business activities as part of a broader range of functions, the Parties will, in respect of the business activities:

(a) where appropriate, implement the principles outlined in subclause (4); or

(b) ensure that the prices charged for goods and services will take account, where appropriate, of the items listed in paragraph 4(b), and reflect full cost attribution for these activities.

(6) Subclauses (4) and (5) only require the Parties to implement the principles specified in those subclauses to the extent that the benefits to be realised from implementation outweigh the costs.

(7) Subparagraph (4)(b)(iii) shall not be interpreted to require the removal of regulation which applies to a Government business enterprise or agency (but which does not apply to the private sector) where the Party responsible for the regulation considers the regulation to be appropriate.

(8) Each Party will publish a policy statement on competitive neutrality by June 1996. The policy statement will include an implementation timetable and a complaints mechanism.

(9) Where a State or Territory becomes a Party at a date later than December 1995, that Party will publish its policy statement within six months of becoming a Party.

(10) Each Party will publish an annual report on the implementation of the principles set out in subclauses (1), (4) and (5), including allegations of non-compliance.

Structural Reform of Public Monopolies

4. (1) Each Party is free to determine its own agenda for the reform of public monopolies.

(2) Before a Party introduces competition to a sector traditionally supplied by a public monopoly, it will remove from the public monopoly any responsibilities for industry regulation. The Party will re-locate industry regulation functions so as to prevent the former monopolist enjoying a regulatory advantage over its (existing and potential) rivals.

(3) Before a Party introduces competition to a market traditionally supplied by a public monopoly, and before a Party privatises a public monopoly, it will undertake a review into:

(a) the appropriate commercial objectives for the public monopoly;

(b) the merits of separating any natural monopoly elements from potentially competitive elements of the public monopoly;

(c) the merits of separating potentially competitive elements of the public monopoly;

(d) the most effective means of separating regulatory functions from commercial functions of the public monopoly;

(e) the most effective means of implementing the competitive neutrality principles set out in this Agreement;

(f) the merits of any community service obligations undertaken by the public monopoly and the best means of funding and delivering any mandated community service obligations;

(g) the price and service regulations to be applied to the industry; and

(h) the appropriate financial relationships between the owner of the public monopoly and the public monopoly, including the rate of return targets, dividends and capital structure.

(4) A Party may seek assistance with such a review from the Council. The Council may provide such assistance in accordance with the Council's work program.

Legislation Review

5. (1) The guiding principle is that legislation (including Acts, enactments, Ordinances or regulations) should not restrict competition unless it can be demonstrated that:

(a) the benefits of the restriction to the community as a whole outweigh the costs; and

(b) the objectives of the legislation can only be achieved by restricting competition.

(2) Subject to subclause (3), each Party is free to determine its own agenda for the reform of legislation that restricts competition.

(3) Subject to subclause (4) each Party will develop a timetable by June 1996 for the review, and where appropriate, reform of all existing legislation that restricts competition by the year 2000.

(4) Where a State or Territory becomes a Party at a date later than December 1995, that Party will develop its timetable within six months of becoming a Party.

(5) Each Party will require proposals for new legislation that restricts competition to be accompanied by evidence that the legislation is consistent with the principle set out in subclause (1).

(6) Once a Party has reviewed legislation that restricts competition under the principles set out in subclauses (3) and (5), the Party will systematically review the legislation at least once every ten years.

(7) Where a review issue has a national dimension or effect on competition (or both), the Party responsible for the review will consider whether the review should be a national review. If the Party determines a national review is appropriate, before determining the terms of reference for, and the appropriate body to conduct the national review, it will consult Parties that may have an interest in those matters.

(8) Where a Party determines a review should be a national review, the Party may request the Council to undertake the review. The Council may undertake the review in accordance with the Council's work program.

(9) Without limiting the terms of reference of a review, a review should:

(a) clarify the objectives of the legislation;

(b) identify the nature of the restriction on competition;

(c) analyse the likely effect of the restriction on competition and on the economy generally;

(d) assess and balance the costs and benefits of the restriction; and

(e) consider alternative means for achieving the same result including non-legislative approaches.

(10) Each Party will publish an annual report on its progress towards achieving the objective set out in subclause (3). The Council will publish an annual report consolidating the reports of each Party.

Access to Services Provided by Means of Significant Infrastructure Facilities

6. (1) Subject to subclause (2), the Commonwealth will put forward legislation to establish a regime for third party access to services provided by means of significant infrastructure facilities where:

(a) it would not be economically feasible to duplicate the facility;

(b) access to the service is necessary in order to permit effective competition in a downstream or upstream market;

(c) the facility is of national significance having regard to the size of the facility, its importance to constitutional trade or commerce or its importance to the national economy; and

(d) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist.

(2) The regime to be established by Commonwealth legislation is not intended to cover a service provided by means of a facility where the State or Territory Party in whose jurisdiction the facility is situated has in place an access regime which covers the facility and conforms to the principles set out in this clause unless:

(a) the Council determines that the regime is ineffective having regard to the influence of the facility beyond the jurisdictional boundary of the State or Territory; or

(b) substantial difficulties arise from the facility being situated in more than one jurisdiction.

(3) For a State or Territory access regime to conform to the principles set out in this clause, it should:

(a) apply to services provided by means of significant infrastructure facilities where:

(i) it would not be economically feasible to duplicate the facility;

(ii) access to the service is necessary in order to permit effective competition in a downstream or upstream market; and

(iii) the safe use of the facility by the person seeking access can be ensured at an economically feasible cost and, if there is a safety requirement, appropriate regulatory arrangements exist; and

(b) incorporate the principles referred to in subclause (4).

(4) A State or Territory access regime should incorporate the following principles:

(a) Wherever possible third party access to a service provided by means of a facility should be on the basis of terms and conditions agreed between the owner of the facility and the person seeking access.

(b) Where such agreement cannot be reached, Governments should establish a right for persons to negotiate access to a service provided by means of a facility.

(c) Any right to negotiate access should provide for an enforcement process.

(d) Any right to negotiate access should include a date after which the right would lapse unless reviewed and subsequently extended; however, existing contractual rights and obligations should not be automatically revoked.

(e) The owner of a facility that is used to provide a service should use all reasonable endeavours to accommodate the requirements of persons seeking access.

(f) Access to a service for persons seeking access need not be on exactly the same terms and conditions.

(g) Where the owner and a person seeking access cannot agree on terms and conditions for access to the service, they should be required to appoint and fund an independent body to resolve the dispute, if they have not already done so.

(h) The decisions of the dispute resolution body should bind the parties; however, rights of appeal under existing legislative provisions should be preserved.

(i) In deciding on the terms and conditions for access, the dispute resolution body should take into account:

(i) the owner's legitimate business interests and investment in the facility;

(ii) the costs to the owner of providing access, including any costs of extending the facility but not costs associated with losses arising from increased competition in upstream or downstream markets;

(iii) the economic value to the owner of any additional investment that the person seeking access or the owner has agreed to undertake;

(iv) the interests of all persons holding contracts for use of the facility;

(v) firm and binding contractual obligations of the owner or other persons (or both) already using the facility;

(vi) the operational and technical requirements necessary for the safe and reliable operation of the facility;

(vii) the economically efficient operation of the facility; and

(viii) the benefit to the public from having competitive markets.

(j) The owner may be required to extend, or to permit extension of, the facility that is used to provide a service if necessary but this would be subject to:

(i) such extension being technically and economically feasible and consistent with the safe and reliable operation of the facility;

(ii) the owner's legitimate business interests in the facility being protected; and

(iii) the terms of access for the third party taking into account the costs borne by the parties for the extension and the economic benefits to the parties resulting from the extension.

(k) If there has been a material change in circumstances, the parties should be able to apply for a revocation or modification of the access arrangement which was made at the conclusion of the dispute resolution process.

(l) The dispute resolution body should only impede the existing right of a person to use a facility where the dispute resolution body has considered whether there is a case for compensation of that person and, if appropriate, determined such compensation.

(m) The owner or user of a service shall not engage in conduct for the purpose of hindering access to that service by another person.

(n) Separate accounting arrangements should be required for the elements of a business which are covered by the access regime.

(o) The dispute resolution body, or relevant authority where provided for under specific legislation, should have access to financial statements and other accounting information pertaining to a service.

(p) Where more than one State or Territory access regime applies to a service, those regimes should be consistent and, by means of vested jurisdiction or other cooperative legislative scheme, provide for a single process for persons to seek access to the service, a single body to resolve disputes about any aspect of access and a single forum for enforcement of access arrangements.

Application of the Principles to Local Government

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

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

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

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

(3) Where a State or Territory becomes a Party at a date later than December 1995, that Party will publish its statement within six months of becoming a Party.