OECD Reviews of Regulatory Reform: Australia 2010
Towards a Seamless National Economy

Executive Summary

Key messages

- Australia has been one of the most successful OECD countries in weathering the Global Financial Crisis. Mature regulatory settings and a strong fiscal position have worked in Australia's favour; it was among the few OECD countries which did not enter a recession. However Australia still has a challenge to lift productivity to return to a higher long-run growth path and continued future prosperity.
- The government has laid out an ambitious regulatory reform agenda to build a seamless national economy and unleash productivity. Regulatory reform is given a high profile in government, with the creation of a portfolio position of Minister for Finance and Deregulation, together with a Minister assisting the Finance Minister on Deregulation. The government is putting a new focus on the potential for well-designed and targeted regulation to reduce costs and complexity for business and the not-for-profit sector, and enhance Australia's productivity and international competitiveness. A culture of continuous improvement supported by evidence-based decision making needs to be embedded more strongly in government practices, with Ministers and their departments more clearly accountable for the quality of regulation in their portfolio.
- A significant effort has been made towards regulatory improvement at Commonwealth level and through renewed Commonwealth-State partnerships. A national reform agenda has been set in partnership with the Australian States and Territories (the States) to harmonise key regulations imposed on business operating across jurisdictions. Innovative institutional structures have been established to facilitate national reforms supported by federal fiscal arrangements. The current reform program hopefully should embed an ethos whereby Commonwealth agencies and the States co-ordinate the regulation of national markets where appropriate, because all players recognise that there are net benefits in doing so – not only because of financial incentives.
- Australian competition law has been effective in establishing robust and competitive markets. There has been significant reform in the last decade, but there is also a need to give greater prominence to long standing commitments to further reform of particularly challenging aspects of the transport, energy, water and infrastructure sectors.
- Globalisation also presents particular challenges for the Australian federation. Business has regularly identified costs associated with inconsistent or duplicative regulatory regimes between jurisdictions as a significant issue for competitiveness. Further streamlining of regulatory frameworks as part of the multi-level strategy will enhance market openness, as well as the ability to compete globally in knowledge intensive industries. Major reform of bio-security management, including border security, will also contribute to improving market openness.

Australia has a well managed economy, which has successfully weathered the crisis

Australia has been one of the best performing economies in the OECD over the past two decades. From 1992 to 2008 Australia enjoyed 17 consecutive years of economic growth. Over the 1990s, improvements in the regulatory environment, coupled with the emergence of information and communication technology (ICT), led to vigorous growth in productivity. In the current decade, strong employment and particularly investment growth have driven GDP increases, despite a lower productivity performance. Incomes have also been boosted over recent years by a sharp rise in the terms-of-trade, which have increased by over 65% between 2003 and mid-2008. This increase was primarily driven by the commodities boom associated with the rise of China and India. As the global economy moved towards recession in 2008, Australia's terms-of-trade fell, offsetting some, but by no means all, of the previous gains.

The impact of the global recession on Australia has been less severe than in most other OECD countries. The economy has benefitted from a healthy macroeconomic situation, coupled with a strong fiscal position when the crisis started, even if the current account persists averaging 4.5% of GDP, with a net investment income deficit. Australia's well regulated and resilient financial sector has limited the direct negative impact of the financial crisis on the economy. Monetary and fiscal policies shielded businesses and citizens from the more damaging impacts of the global recession and Australia has benefited from the rapid rebound of some Asian economies, in particular China. As inflation risks are still present, Australia was the first G20 country to increase interest rates in the second half of 2009.

Regulatory reform has contributed significantly to economic success

Increased exposure to international trade during the 1980s and the product market liberalisation conducted in the 1990s under the National Competition Policy (NCP) framework reduced barriers to entry, and increased competition in the Australian economy. This contributed to an impressive surge in productivity in the 1990s, which according to a 2005 Productivity Commission report, added at least 2.5%, or $20 billion, to Australia's GDP.

From 1993-94 to 1998-99, labour productivity increased at an annual rate of 3.3% per year. This is the fastest on record, and helped to close the productivity gap between Australia and the US. Employment also increased over the period, suggesting that gains in productivity were not acquired at the expense of increasing under-employment, with increased labour market flexibility. This was facilitated by the decentralisation of wage bargaining mechanisms in 1991 under the Hawke-Keating Labor government, followed by the *Workplace Relations Act* in 1996. Further reforms were introduced under the 2006 *WorkChoices* legislation. However, these measures did not receive broad support in the context of the 2007 Australian Federal election.

ICT and innovation has also increased productivity and internationally, diffusion of technology was a key driver of productivity growth. Australia has become a leading adopter and beneficiary of ICT investment, the diffusion of which has been facilitated by reforms to product market regulation. The August 2008 report, *Venturous Australia – building strength in innovation*, by Terry Cutler, found that 98% of new technologies are sourced from outside the country.

But challenges to productivity remain

However, further productivity improvements are required if Australia is to return to a higher long-run growth path. The Australian economy experienced a slowdown in productivity over the past recent decade. While subject to some debate, this may be reflective of the combined effect of short term economic shocks from a severe drought on agriculture, water and the electricity sector, increased investment in mining resulting in the increasing use of mining resources with lower yields as well as more systemic factors.

Meeting the challenges of globalisation calls for resolving infrastructure bottlenecks and improving core energy and communication activities. Ensuring that infrastructure investment delivers the strongest possible contribution to growth requires evaluation of potential projects and a strong policy framework. The Australian Government established the Building Australia Fund to augment funds available for infrastructure investment in the 2008-09 Budget. Infrastructure investment proposals are identified by an advisory board, Infrastructure Australia, which provides a national approach. This role could be further improved by the public disclosure of the supporting cost-benefit assessment for nominated projects. To ensure that the full value of increased investment is realised, remaining regulatory reform in relation to infrastructure, access, transport, energy and water should be completed.

Like many OECD countries, Australia faces long term fiscal challenges from an ageing population. While public finances are currently well-placed compared to other OECD countries, the second Intergenerational Report published in 2007 indicates that Australia's net debt position could swell to over 30% of GDP by 2046-47. Long term fiscal pressures related to health care spending are also expected to be a major source of future government outlays.

A sophisticated governance system with a renewed impetus towards deregulation

Australia is one of the front-running countries in the OECD in terms of its regulatory reform practices. Australia benefits from a mature system for regulatory management, with early and comprehensive adoption of OECD good practices as well as introduction of novel approaches. The government elected in 2007 has provided a renewed reform impetus, establishing a solid institutional framework and announcing a commitment to "continuous improvement" in regulatory quality. The government has endorsed the principles of good regulatory processes recommended by the Banks Taskforce on Reducing the Regulatory Burdens on Businesses and adopted by the previous government, and has reaffirmed the commitment to best practice regulation requirements.

Recent reforms have strengthened Australia's system for Regulatory Impact Assessment (RIA) to protect business from new, unnecessary regulation, making it among the most rigorous and comprehensive in the OECD. A new policy function has been created in the Department of Finance and Deregulation to promote better regulation across the administration, complementing the Office of Best Practice Regulation (OBPR), which was previously located within the Productivity Commission. RIA has been progressively extended to all policy instruments with a regulatory character. Formal Cabinet processes support the requirement for the preparation of Regulation Impact Statements (RIS) for proposals with a significant impact on business. The OBPR performs a gate-keeping function and also provides training and direct assistance in the application of cost-benefit analysis. The OBPR publishes information on the compliance of agencies with the agreed criteria for RIS.

New program initiatives include the initiation of partnerships with other Ministerial portfolios to identify and progress reforms. The government has also commenced a review of all pre-2008 Commonwealth subordinate legislation to document regulations which impose a net cost on business and identify scope to improve regulatory efficiency. The Commonwealth government has eschewed the use of targets to drive reductions in administrative burdens. However, Australia has been innovative in the use of other methods, in particular benchmarking by the PC to report comparisons of regulatory practices across the States and the Commonwealth, and to examine the burden in particular sectors of Commonwealth regulation. Australia is also implementing a range of e-government strategies to streamline reporting requirements for business, including the use of standard business reporting to pre-fill government forms and a one stop shop portal for business and citizens.

The use of *ex post* assessment is also well integrated in the regulatory process, with 10-year sunset periods for subordinate legislation, and scheduled reviews of legislation. The quality of legal drafting is carefully maintained through professional drafting offices, the complete legislative database is available online, and subordinate legislation is not enforceable unless it is on an official register.

A new and innovative model for state federal relationships to deliver a seamless national economy

The new agenda for Commonwealth-State relationships includes efforts to build a national seamless economy, harmonising key regulations across jurisdictions. These efforts are conducted in the context of the Council of Australian Governments (COAG). COAG is chaired by the Prime Minister and comprises the first ministers of State and territory governments. In November 2008 COAG committed to new co-operative working arrangements between the Commonwealth and the States with a new Inter-governmental Agreement on federal fiscal relations. This reduced the number of Specific Purpose Payments to the States from over 90 to five, while increasing the overall quantum of funding. Funding arrangements have been refocused on outputs and outcomes, and the Commonwealth has agreed to provide incentive payments, in the form of National Partnership Payments to reward State efforts for implementing jointly approved regulatory reforms.

In November 2008, 27 priority areas of regulatory reform, and a further eight competition reforms, were reflected in the preparation of a National Partnership (NP) agreement to Deliver a Seamless National Economy, ratified in February 2009. Delivery on the deregulation priorities is supported by a AUD 100 million facilitation payment, and a further AUD 450 million in reward payments are scheduled for the period 2008-09 to 2012-13, contingent on the performance of the States. The agenda also involves reforms in the areas of energy, transport, infrastructure, planning and the environment. The agenda is managed by the Business Regulation and Competition Working Group (BRCWG), which includes high level representation from the States and is co-chaired by the Minister for Finance and Deregulation and the Minister Assisting the Finance Minister on Deregulation. The BRCWG builds on the strength of central government departments both at Commonwealth and state level. Its strong capability is a potential resource to identify areas for further reform and to maintain a focus on deregulation outcomes in the future. The independent COAG Reform Council monitors the performance of all jurisdictions and ensures transparency in performance reporting.

The delivery of the COAG reform agenda requires significant co-ordination at State level, and has been facilitated by an alignment of the broad reform priorities of the individual States and the COAG agenda, even if the elements of emphasis differ. Early indications are that the Seamless National Economy NP is progressing according to schedule, but high expectations have been invested in the reform program and it is being carefully followed by business groups. It is too early to be definitive about final outcomes. The COAG agenda is extensive and complex and maintaining momentum over the remainder of the reform program will be a challenge. It can be anticipated however, that the schedule of reward payments and the oversight role of the COAG Reform Council will help significantly.

The COAG national reform agenda has also given impetus to improvements to regulatory management practices at the level of the States. In general the Australian States demonstrate regulatory management practices that are among OECD best practice. A commitment to develop regulation that is efficient, effective and in the national interest, appears to be a shared national objective.

Effective enforcement of competition law leading to a competitive market environment

Australia has an integrated approach to the promotion of market competition, with market-based approaches the preferred policy approach. The Australian Competition and Consumer Commission (ACCC) has the primary responsibility for enforcing the *Trade Practices Act 1974* (TPA), which is Australia's competition, fair trading and consumer protection legislation. The TPA enhances consumer welfare by prohibiting certain anticompetitive conduct, such as restrictive agreements and practices, abuse of dominance and misuse of market power, and mergers and acquisitions that substantially lessen competition. The combination of consumer protection and sector regulation establishes a cohesive and integrated policy approach. The broad complementary enforcement and regulatory powers of the ACCC assist compliance and promote public support for pro-competitive reforms.

Since the NCP, Australia maintains consistent and complementary competition laws and policies that apply to all businesses regardless of ownership. This is supported through requirements for competitive neutrality (that government businesses should not enjoy net competitive advantage as a result of their public sector ownership); agreement that price oversight of state or territory government business enterprises is primarily the responsibility of the relevant State; and agreement regarding structural reform of public monopolies through the introduction of competition. Removing "exemptions" was closely related to rationalising infrastructure regulation in the context of the NCP, because infrastructure services and regulation provided by the States were not subject to Commonwealth competition law. Impediments to competition have been progressively removed and a common, coherent scheme for assessing and regulating sectoral access to essential facilities has been established. The scope of exceptions to competition law has been reduced.

Australia's competition law was the subject of the 2003 Dawson Review, and the amendments recommended in the Review and a subsequent Senate Committee have been largely implemented. While these represent general improvements, notably in terms of increased sanctions for cartels, the scope and effectiveness of the prohibition against misuse of market power may be less clear now than it was before the amendments. This may reflect the influence of small business "politics" in Australian competition law, as the TPA now includes a prohibition aimed at predatory pricing that could curb discounting by large corporations. The new prohibition risks creating uncertainty, is inconsistent with international precedents, and at a minimum the market share aspect of the "Birdsville amendment" should be removed.

Some aspects of the NCP remain unfinished. The access regime has been subject to criticism, particularly in terms of access to railway lines, with litigation used as a means to frustrate the operation of the system. In October 2009, the government introduced legislation into the Australian Parliament to enact binding time limits on decision-makers for regulatory decisions, in place of previous target time limits. Outstanding reforms remain to be completed in the energy sector. The government has announced changes to improve the operation of the access regime which applies to telecommunications.

Enjoying the benefits from globalisation through strong market openness

Australia has maintained a policy of market openness with full integration of its markets to international competition. This has delivered significant benefits, as two-thirds of Australia's trade is with APEC economies, with rapidly growing Asian markets in China and South Korea, as well as with India. Australia's trade policy supports international trade negotiations, endorsing the conclusion of the Doha Round taking place under the WTO. It also pursues bilateral free trade agreements with important trading partners.

Various domestic processes provide for transparency and information dissemination, including through the use of RIA. Stakeholders are routinely consulted on regulatory changes likely to affect trade. Value-for-money and transparency also apply to public procurement; and a central website lists all the contracts and annual procurement plans awarded through the AusTender website. Australian Customs and Border Security have also streamlined customs procedures to facilitate the transit of goods.

While Australia market openness generally reflects a strong commitment to free trade, quarantine inspections have been subject to criticism by Australia's trading partners. This is due to the comprehensive mandated inspection targets for air and sea vessels as well as air passengers. A major review of the quarantine system, the *Quarantine and Biosecurity Review*, conducted by an independent panel chaired by Mr. Roger Beale AO and released in 2008, recommended a move away from mandated inspection targets in favour of a risk-based approach to reduce the burden of border controls. A system has been trialled by the Australian Quarantine and Inspection Service, and the government announced in September 2009 a series of measures aimed at commencing implementation of these reforms.

Foreign equity restrictions remain in certain sectors and foreign purchases of Australian businesses or real estate are subject to screening procedures. To address concerns, the government issued a set of transparency principles in February 2008 and also announced some liberalisation measures in September 2009, with the threshold for investment screening for non-US investments raised to AUD 219 million, and exempting Greenfield investment. This is expected to exempt a fifth of the applications from screening.

Moving reforms forward and boosting economic growth

Australia has endorsed a new growth-oriented reform agenda focused on strengthening regulatory frameworks to boost productivity growth. Many of the challenges facing the Australian economy have inter-jurisdictional dimensions. Success depends crucially on co-ordinated actions by a number of agencies at state level, as well as State Parliaments passing and amending state laws. Productive Commonwealth-State relationships are crucial for the reform agenda in Australia, as firms wanting to operate in more than one State face additional State-specific compliance costs, even if they meet regulatory requirements in their home State. In the future, the challenge will be to co-ordinate regulation of national markets so that new barriers are not created and that all jurisdictions regulate with regard to the national interest without the need for further financial incentives.

Australia represents in many ways a "role model" for OECD countries in its proactive approach to regulatory reform. Success will require maintaining momentum for reform, including through the more difficult task of implementation. The goal is to embed a commitment to good regulatory management in the development of regulatory policy. Australia demonstrates strong institutional capacities to serve the process. Regular communication with business and the community on the benefits of reforms will also be necessary to maintain support and ensure that the issues likely to deliver greatest benefit are included. Previous efforts at benchmarking the performance of all jurisdictions should be continued to provide good examples and maintain the focus on national objectives. COAG has well designed frameworks for the *ex ante* assessment of national regulatory responses, but compliance with these frameworks by Ministerial Councils needs to be strengthened.

Ultimately, the goal is for Commonwealth and State governments to work co-operatively in regulating national markets, with a shared understanding of the benefits of doing so. Current institutional frameworks are effective, but they will have to stand the test of time. The current effort reflects a unique opportunity, which needs to be seized, with gains demonstrated as early as possible to justify the energy and resources that have been invested, as well as providing positive incentives for the future.