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# Domestic transparency in Australia's economic and trade reforms: the role of 'the Commission'

**Gary Banks and Bill Carmichael \***

## **Introduction**

A successful conclusion to the Doha Round remains elusive despite six years of intensive negotiations. The sense of déjà vu is palpable. As in previous rounds, the key sticking point — divisions between the EU, US and developing countries on the adequacy of current 'concessions' — reflects perceptions within those countries that their liberalisation only benefits them if it is reciprocated by their trading partners. That in turn is a reflection of a poorly informed policy discussion within WTO member countries, and the lack of domestic processes to promote it.

This, of course, is not a new diagnosis. Two decades ago, two international study groups reporting on ways to overcome the then impasse in progressing multilateral trade negotiations advocated establishing 'domestic transparency' mechanisms within member countries to generate better information about the costs and benefits of domestic liberalisation, and thus a more 'positive' approach to international trade negotiations (Leutwiler 1985, Long 1989). The proposal was also revived in the early stages of the Uruguay Round in the negotiating group on the Functioning of the GATT System (Rattigan, Carmichael and Banks 1989) but consideration was deferred pending establishment of an *external* monitoring process within the WTO, the Trade Policy Review Mechanism. That deferral became permanent.

The consequences of this deficiency in national preparations for trade negotiations have become more profound given the expansion of 'trade' negotiations beyond tariffs and quotas on manufactures to more difficult areas of domestic policy, and

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by the expansion in membership of the WTO. These days, negotiations encompass agriculture, services and ‘behind-the-border’ issues such as foreign investment, competition law, product standards, intellectual property, governance and other matters which are widely seen as belonging to domestic policy. The complexities of this broadened trade agenda, the fact that it has more to do with domestic than international policy matters, and the lack of mechanisms to examine the consequences of policy change, have compounded the difficulties of achieving liberalisation in international settings.

The broadened international agenda has heightened the need for more transparent domestic policy-making processes. Australia’s experience in this area, reflecting in part our traditional lack of negotiating scope in the GATT as an agricultural exporter, has attracted renewed international attention. The latest WTO Trade Policy Review of Australia makes the following observation:

The high degree of transparency in the formulation and evaluation of Australia’s economic policies in relation to their rationale, nature, and economic effects, enhances government accountability and public debate over the merits of these policies. Hence, transparency has contributed greatly to the continued process of reform, which began in the 1980s, and in which trade liberalization, much of it unilateral, has played an integral part. (WTO 2007, p. vii)

The TPRM report emphasised that the transparency function had become institutionalised in Australia, notably through the role of the Productivity Commission (and its predecessor organisations) as an independent review and advisory body on microeconomic policy and regulation.<sup>1</sup>

While other countries have organisations within the public or private sectors which do research or provide advice on trade and related policies, Australia appears to be unique in having fashioned an independent institution within government to pursue this on an ongoing basis, using public processes and an explicit national interest perspective. Even within the Australian tradition of extensive use by governments of public inquiries to investigate all manner of public policy issues (Prasser 2006), the Commission’s standing transparency function is distinctive.

Although formed in 1998, the Productivity Commission’s institutional roots go much deeper. It is the direct descendent of the Industry Commission (1990-1998) and, before that, the Industries Assistance Commission (1974-1990). In turn, that body was created from the Tariff Board, which was founded in 1921.

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<sup>1</sup> Growing interest in the Commission is also evident as part of a wider push within a number of countries to enhance their own capacity for policy formulation and economic decision making. A recent focus for this has been ‘institution building’ within Asian members of APEC, but interest extends as far afield as Chile, Botswana, Kazakhstan and even France.

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The purpose in this paper is to distil those aspects of the Australian experience likely to be of interest to an international audience. To this end, the paper focuses primarily on four issues:

- why ‘the Commission’ was established in 1974 to replace the Tariff Board;
- continuity and change in how this institution has operated through its three forms;
- the nature of its contribution to policy decision-making and debate over the years; and
- insights that are likely to remain of relevance to Australia in future, as well as to those exploring the scope for institutional innovation and greater transparency in policy formulation within their own countries.

### **The Tariff Board: forging a beginning**

Paradoxically, the institution most identified in Australia with the extensive trade liberalisation and other microeconomic reforms of the past few decades had its origins in the Tariff Board, which served in an essentially protectionist role until near the end of its life. The relevance of this background is twofold:

- the features of the Board that made transparent the costs of protection were carried forward in subsequent institutional transformations and proved important to their survival and success; and
- it has relevance to other countries in demonstrating that transparency institutions could be fashioned from existing bodies.

Protection from imports was a heated policy issue before and after the federation of Australian colonies in 1901. The Australian Parliament established a Tariff Board in 1921 as an experiment in deflecting intense lobbying from protectionist manufacturing groups and counter-pressures from free traders (Rattigan 1986, pp. 2–3). Initially established for only two years, the Board’s (protectionist) advice in that period proved sufficiently acceptable to the Government that, in 1924, it was made a permanent inquiry and advisory body on tariff making. Those amendments also included a requirement for the Board to hold public hearings. The Board’s existence was further entrenched as a result of the 1932 trade treaty between Australia and the United Kingdom where, in exchange for preferential entry to the UK market, proposed changes in duties on imports had to be referred to the Board for advice before the Australian Government could take any action.

Tariffs were not the major instrument of Australian manufacturing protection between the 1930s and the early 1960s, but they became so once wartime controls

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and the quantitative import restrictions of the 1950s were removed and import competition intensified.

The main features of the policy environment in which the Tariff Board operated were:

- various areas within the bureaucracy providing segmented advice on industry policy consistent with their being responsible for particular parts of the economy, and in circumstances where they were often driven by the information provided by and/or the interests of their ‘clients’;
- a work program determined by government, but dominated by requests from local manufacturers for increased protection on specific products;
- the absence of integrated official data systems necessary for economy-wide policy analysis;
- the absence of a coherent set of national policy goals to guide advice on protection and industry development, and uncertainty as to how the existing statutory guidance to the Board to promote ‘economic and efficient’ industry should be interpreted; and
- from 1960, the existence of a separate advisory body (the Special Advisory Authority) for granting ‘temporary’ assistance that was used continually by some sections of industry to circumvent any long-term cuts in their tariffs.<sup>2</sup>

An institutional design scorecard for the Tariff Board would contain a number of positives — chiefly in terms of process — but also some significant negatives, including a lack of information about the wider economic consequences of following its advice (Box 1).

In the mid-1960s, under the combined influence of a new Chairman (Alf Rattigan), a separate high profile public inquiry into Australia’s economic policies (the Vernon Committee) and developments in protection analysis fostered by Australian academics (notably Prof. Max Corden), the Board began to question the effects on the wider economy of its longstanding, needs-based approach to tariff advice. In the face of considerable resistance from the then Government, the Board increased its analytical capacity, began estimating and making transparent its measures of the relative protection levels accorded different industries (using the relatively new concept of the ‘effective rate’ of assistance) and published a tariff review program focusing on broad groups of manufacturing industries (rather than narrow product lines) commencing with those most highly assisted.

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<sup>2</sup> These characteristics of the policy environment and their consequences are discussed by Carmichael (2005, pp. 20–4).

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Box 1      **The Tariff Board: a policy transparency scorecard**

***Positives***

- a standing (rather than ad hoc) advisory body on manufacturing tariffs
- independent from executive government, the bureaucracy and industry
- public inquiries and reporting
- mandatory referral before government could change tariffs

***Negatives***

- vague statutory guidance on policy objectives
- no capacity to consider the wider economic consequences of its recommendations
- narrowness of references, reactive to industry pleading
- circumvention via a ‘temporary’ assistance mechanism
- lack of control over its resources (for most of its life)

These were times of considerable tension between sections of the Government and the Board, as it pushed the existing boundaries of its remit. The Board’s activities threatened the Government’s ability to appease opposing pressure groups in its key industrial and agricultural constituencies. It did this by revealing their true (relative) levels of assistance and by exposing the fallacy of governments being able to deliver the protection ‘all round’ that had been promised for import-competing and export industries alike.

As a result of the Board’s use of transparent criteria against which to assess claims for assistance, and concern for the wider economic impacts of its recommendations, its advice gained greater respect and authority.

### **Creation of the IAC: a new blueprint**

The election of a new government in December 1972 brought decisive changes to the Tariff Board and to Australian tariff policy. The newly elected Prime Minister, Gough Whitlam, had the (then) radical notion that the fiscal requirements of the new Government’s ambitious social programs depended on an efficient and productive economy. Whitlam sought advice from Sir John Crawford, an eminent former senior public servant, on the establishment of an institution with a wider remit than the Tariff Board and a clearer focus on national economic performance.

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In his report, Crawford identified three main reasons for establishing such a body:

- it could assist the Government to develop coordinated policies for improving resource allocation;
- given its independence, it could provide disinterested advice in contentious areas of public policy; and
- it could facilitate public scrutiny of those policies by means of transparent inquiry processes and public reports to Parliament. (Crawford 1973)

Crawford's proposals (Box 2) were accepted by the Whitlam Government. They formed the basis for a new statute followed by the commencement of Industries Assistance Commission operations in January 1974.

**Box 2      Crawford's proposal for 'a commission to advise on assistance to industries'**

***Guidelines for the Commission***

- a broad framework consistent with the Government's long-term national economic and social policy goals

***Functions***

- advisory only, with no executive or administrative responsibilities
- advice on all forms of assistance to all industries, including mining and services
- power to initiate its own inquiries
- report periodically, in its annual reports, on assistance afforded to all industries, industries' performance and the general effects of industry assistance policies on the economy
- mandatory referral to the commission before government action to grant temporary assistance or to grant or change duties, subsidies, bounties etc. where assistance exceeded 12 months

***Membership***

- Commissioners appointed on the basis of competence, not on their capacity to represent particular interest groups

***Procedures***

- all communications of importance between the Commission and the Government should be made public
- Commission not be restricted to using information and comment gathered through its public inquiry process
- wherever possible, reliance on official statistical collections when collecting and analysing information for inquiries

Source: Crawford (1973)

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It is clear from Crawford's report that the new Commission was seen as providing a counterweight to the sectional and other political pressures resisting trade and industry liberalisation. He put it this way:

Measures which assist particular industries obviously constitute forms of economic discrimination which, at least in the short term, are to the advantage of the assisted industries and to the disadvantage of those who pay for assistance ... But the parties to such conflicts of interest will not always be equally represented in the argument and discussion which precede decisions by Government and Parliament: those likely to gain directly from a particular measure, such as tariff or subsidy, will tend to be more concentrated, organised, and articulate, than those likely to lose from the measure. If Parliament is to have regard for the equity of its decisions on assistance to particular industries, and for the longer term implications of these decisions for the community as a whole, it must, I believe, have a source of advice such as the Commission, that can inform it on those matters which particular interests will tend to neglect. (Crawford 1973, pp. 3–4)

### **Three core design features**

The legislation creating the IAC provided it with a charter and independence required to ensure that its advice to governments would be disinterested, open to public scrutiny and formulated with regard for the best interests of the community as a whole, not just those of particular groups.

Three features of the IAC's structure and operations underpinned the effectiveness of its contribution to public debate and policy formulation.

- *Independence.* The Commission operated under the protection and guidelines of its own legislation. It had an arm's length relationship with government, which could tell it what to do but not what to say. Its role was purely advisory, having no judicial, executive or administrative functions. Members of the Commission were appointed for fixed (renewable) terms and could not be removed by the government of the day.
- *Transparency.* Its inquiry tasks were specified in publicly available terms of reference. The Commission's statute required it to hold public hearings and release draft reports before finalising its recommendations to government. The Commission was also required to prepare an annual report covering its operations and analysing the structure of assistance to industry and its effects. And the Government was obliged to release publicly all Commission reports within a specified period.
- *Economy-wide mandate.* Guidelines in the legislation stated that the Commission should be concerned with improving the efficiency with which the economy uses

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its resources and to take account of the wider interests of consumers and users of products affected by its proposals.

The rationale behind these core design features for the Commission was explained in the following terms by the Prime Minister when introducing legislation in Parliament for the IAC:

The first and most important reason for establishing the Commission is to allow public scrutiny of the process whereby governments decide how much assistance to give different industries ... Such a process must be independent and impartial, and seen to be independent and impartial.

... 'public inquiries and reports' denote a deliberate, orderly and widely accessible system of communication between the Government, industry and the wider public.

... the Commission will be a single institution, with responsibility for advising on the assistance which should be given to industries in all sectors of the economy. It will therefore be very conscious of the need to develop a rational and consistent approach to all industries. (Whitlam 1973, pp. 1632–3)

These features have remained fundamental to the role and operations of the two organisations that succeeded the IAC, namely the Industry Commission and today's Productivity Commission<sup>3</sup>. In combination, these institutional arrangements preserve the autonomy of governments over policy, while ensuring transparency and an economy-wide perspective in the advice going forward to them on key issues.

The main differences between the organisations have been in their coverage, which has been progressively extended beyond industry assistance matters to include structural reform issues across all sectors of the economy, and in social and environmental as well as economic spheres. Around 80 per cent of the IAC's inquiry reports concerned assistance for manufacturing industries. These days, around 80 per cent of Productivity Commission inquiries relate to cross-sectoral, infrastructure, social and environmental policy issues. Box 3 illustrates the breadth of matters the Productivity Commission has addressed in recent years.

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<sup>3</sup> The procedures and structure of the IAC in providing advice on protection were described in some detail by Rattigan and Carmichael (1996, pp. 74–96). See also Productivity Commission (1998).



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**Box 3: A selection of Productivity Commission reports**

*Trade liberalisation/industry assistance*

- Australia's general tariff arrangements
- Review of automotive assistance
- Review of textile, clothing and footwear assistance
- Pig and pigmeat industries: safeguard action against imports
- Review of the pharmaceuticals industry investment program
- Multilateral liberalisation of services trade
- Trade and investment effects of preferential trading arrangements
- Removing tariffs on goods originating from Least Developed Countries
- International air services
- Public support for science & innovation

*Productivity studies*

- Productivity in Australia's wholesale and retail trade
- ICT use and productivity
- Microeconomic reforms and Australian productivity: exploring the links
- Can Australia match US productivity performance?

*Infrastructure reform issues*

- Review of the gas access regime
- Price regulation of airport services
- Telecommunications competition regulation
- Progress in rail reform
- Road and rail freight infrastructure pricing

*Labour market issues*

- Australia's health workforce
- Independent review of the Job Network
- National workers' compensation and OHS arrangements
- Non-traditional work in the Australian labour market
- Container stevedoring work arrangements
- Men not at work: an analysis of men outside the labour force

*Environmental issues*

- Rural water use and the environment
- Energy efficiency
- Waste management
- Conservation of historic heritage
- Pricing of irrigation water
- Impact of a foot and mouth disease outbreak in Australia
- Water quality in the Great Barrier Reef
- The environmental performance of commercial buildings

*Social issues*

- Australia's gambling industries
- Indicators of indigenous disadvantage
- Social capital
- Review of the Disability Discrimination Act
- Nursing home subsidies
- Inquiry on first home ownership

*Regulatory reviews*

- Broadcasting
- Impact of native vegetation and biodiversity regulations
- Reform of building regulation
- Radiocommunications
- Liner cargo shipping
- Regulation of the taxi industry
- Review of the Prices Surveillance Act
- Review of mutual recognition
- Review of legislation regulating the architectural profession
- Performance benchmarking of Australian business regulation

*Other studies*

- Report on Government Services
- Potential benefits of the National Reform Agenda
- Impacts of medical technology in Australia
- GTE financial performance
- Cost recovery by Commonwealth agencies
- Resourcing universities

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Nevertheless, the core rationale for the Commission has remained constant, expressed by the current government in the following terms:

Sound policy development must be based on a full appreciation of the facts. A primary role of the Productivity Commission will be to identify impediments to improve productivity in particular sectors. It will also have due regard to the important relationships between improved use of resources in one sector and the rest of the economy. It is only with this sort of information and economy-wide focus that governments can make sensible and considered choices as to future policy — choices that will ensure better and more sustained growth prospects for all Australians

... the Productivity Commission's economy-wide perspective, its broad charter, public inquiry process and research functions will play a key role in promoting policies at both the government and business levels to improve the competitiveness and dynamism of Australian industry. [Its legislation] provides for an effective and broad-ranging institution to serve the needs of parliament, the people and government. (Miles 1996)

## **The public inquiry process**

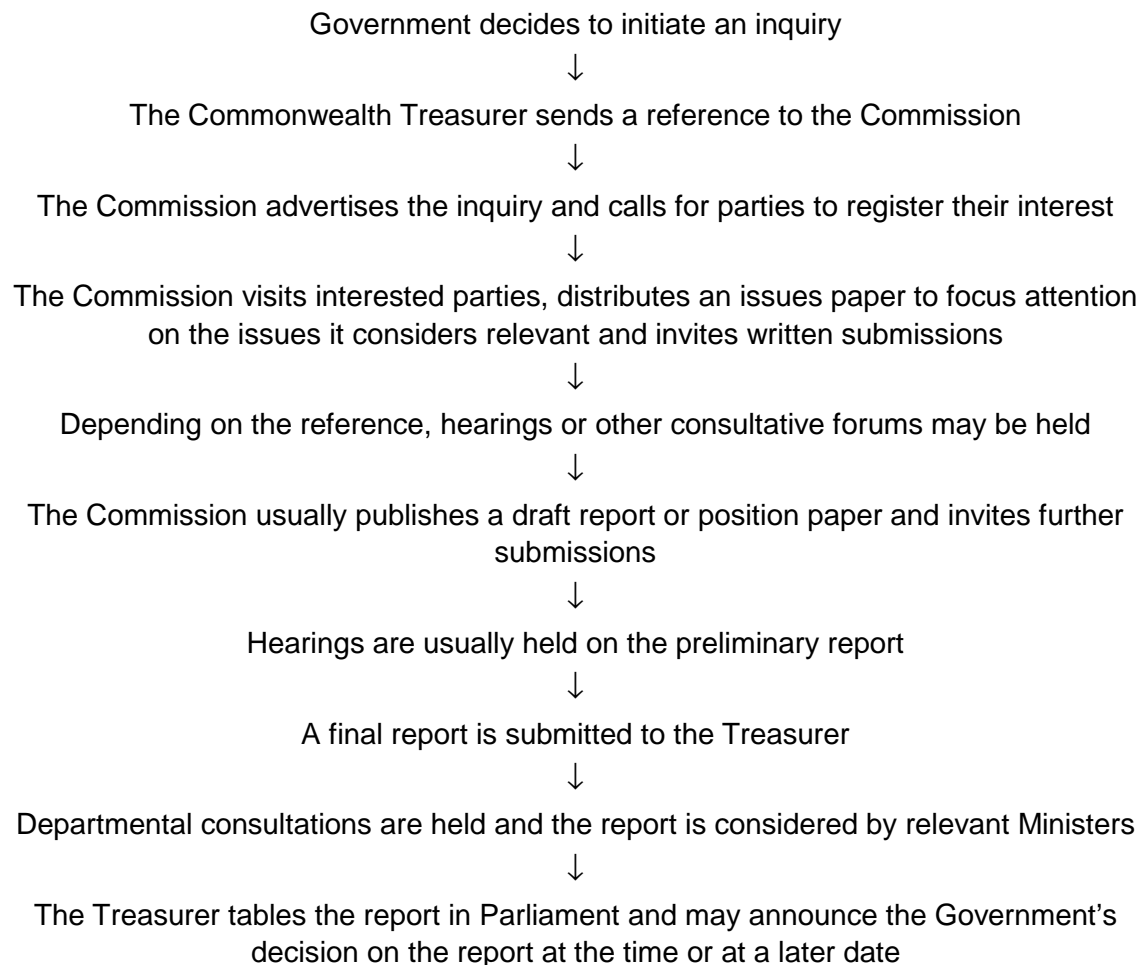
The Commission's public inquiries tend to be resource intensive and have a high public profile compared to other research studies and are therefore not designed for trivial or straightforward matters. Rather, they typically concern policy issues that have a significant impact on different groups within society, or are otherwise contentious or complex to assess, but where the potential of a long-term payoff for the nation from better informed policy making is high. These features put a premium on good process and effective engagement with potentially affected sections of the community. Box 4 outlines the main stages in the inquiry process.

Once the Australian Government agrees on the focus and scope of an inquiry (often in consultation with other governments and community groups), the Treasurer sends a 'reference' to the Commission. The terms of reference outline in writing what the inquiry covers and how long the Commission has to report. Most inquiries specify a duration of 9 to 12 months, sometimes less for urgent matters. Such timeframes need to ensure adequate opportunity for public participation and for feedback on the Commission's preliminary findings before its report is finalised and sent to the Government.

Public inquiries are widely advertised and provide an opportunity for different points of view to be heard and considered. The Commission is active in identifying those potentially interested in the inquiry and all individuals and organisations with an interest can participate. They may do so through the Commission's visit program, through written submissions and attendance at hearings, or at workshops and other forums. Submissions and transcripts of public hearings are posted on the Commission's website and are also available in hard copy.

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**Box 4      Stages in the Inquiry process**



These transparent processes ensure that the arguments of interest groups are subject to close scrutiny, as is the Commission's own analysis.

Final inquiry reports must be tabled in Parliament within 25 sitting days of the Treasurer receiving the report. But it is up to governments to make the final decisions in response to the Commission's findings and recommendations.

### **The value of a supporting research function**

Crucial to the Commission's contribution has been its capacity to undertake research on its own initiative. Without rigour and coherence in the frameworks it uses to analyse policy issues and solutions, the Commission's advice would risk becoming inconsistent and therefore less useful to policy makers.

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According to Rattigan (1986, p. 21) many of the early difficulties of the Tariff Board could be traced to its incapacity to stand back from day-to-day inquiry work, assess the shortcomings in its overall approach and to develop ways to overcome them. Hitherto, the Board had ignored the requirement to report annually on ‘the operation of the Tariff and the development of industries’: that is, on the economy-wide consequences of the structure of protection.

In its earlier forms, the Commission set about developing the policy information systems, analytical tools and research methods needed to discharge its reporting functions, including through its annual reports. These reported on the assistance provided to industries, the factors affecting the economic performance of those industries and effect on the Australian economy of the provision of that assistance.

For a long time, the annual report was the main vehicle through which the Commission could publish research findings on the structure of protection, sources of structural change in the economy and related matters, and to explain the rationale for the Commission’s general approach to its inquiry work. By comparison, the Productivity Commission has an explicit statutory duty to initiate research that complements its other functions and to promote public understanding of the tradeoffs involved in different policy approaches. In addition, it must report annually on the impact of assistance and regulation on the productivity and performance of the Australian economy as a whole.

This widening remit for research that is separate from studies commissioned by government, is reflected in the broadening of supporting research outputs over the years, but some key areas of focus have remained.

For example, the IAC continued the work on effective rates of protection for manufacturing industry initiated by the Tariff Board. Building on the pioneering work of Max Corden, the Commission assessed tariffs, quotas and subsidies on inputs and outputs to estimate the net effect on an industry’s level of assistance. The dollar values of industry assistance, net subsidy equivalents per protected job and the consumer tax equivalents of tariffs attracted intense media and public attention. Over the years, the measurement framework has been extended to encompass agricultural and mining industries and budgetary assistance to services. As the WTO’s *World Trade Report 2006* noted, the Commission’s annual *Trade & Assistance Review* is one of only three such detailed, comprehensive and publicly accessible reports produced world wide (WTO 2006, p. 111).

Policy modelling has also played an important role from the earliest days of the Commission. Reform is usually disruptive and costly to some, so assurance that the beneficial impacts justify such costs is critical in developing and selling proposals for policy change. The Commission was an early supporter of the development of

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official input-output tables and a prime mover in harnessing the power of general equilibrium modelling to assess economy-wide effects. The IAC sponsored the establishment of the IMPACT Project with its large-scale multi-sectoral model of the Australian economy. The model, and subsequent versions of it, permitted quantitative analysis of the effects of tariff and other policy changes (Powell and Snape 1993, Dee 2005).

Modelling highlighted the importance of interdependencies within the economy and the need for policy makers to take more than just the ‘first-round’ or direct effects into account. Typically the ‘big numbers’ that such modelling has generated, have proved powerful in bringing home to policy makers and the community what is at stake in policy reform, with the media playing a key role in this.

The Productivity Commission’s supporting research program is integral to its work and comprises a significant proportion of its output. As noted, the program is more broadly based than that of its predecessors and fulfils a wider range of functions. Nowadays, supporting research:

- continues its traditional role of providing specialist input to inquiries through modelling frameworks and quantification — such as input to the Commission’s 2005 inquiry reviewing national competition policy showing that productivity and price changes in major infrastructure industries had boosted Australia’s GDP by 2.5 per cent;
- can help pave the way for subsequent references from the Government by raising public consciousness of the issues — supporting research outputs on the role of property rights and other market instruments in achieving environmental goals and modelling of water trade in the Murray–Darling Basin preceded references on native vegetation regulation and the role of market mechanisms in rural water use;
- can help fill gaps in policy discussion where a formal inquiry is unlikely — for example, the Commission convened a workshop of leading analysts on ‘managed competition’ in health care and disseminated the proceedings to promote wider discussion and further research; and
- promotes more informed community debate on a wide range of policy issues — the Commission’s analyses of the factors influencing Australia’s productivity performance and of the role of non-traditional employment in today’s labour market are two examples.

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## Impact on policy debates and decisions

In seeking to gain an understanding of the Commission's role, international visitors often ask for evidence that it has made 'a difference' to policy making in Australia. It is hard to be conclusive. After all, the Commission is only an advisor, not a decision maker; there are many other sources of advice to government, and there can be lags between when the Commission reports and the ultimate policy decision, such that attribution is difficult. And of course, views by different parties on the performance of the Commission can be conditioned by how those interests have been affected by its advice and analysis.

One simple indicator of the Commission's influence is government acceptance of its findings and recommendations. In the case of its inquiries into industry protection or assistance, notwithstanding some high profile rejections (generally in politically charged circumstances), the great bulk of the Commission's recommendations have been implemented either fully or in part.

Furthermore, an initial unwillingness by government to accept or act on key recommendations does not mean that the Commission has no influence in the longer term. For example, asked by the Government in the early 1980s to report on options for general reductions in protection, the IAC's report was 'shelved' as the economy moved into recession (IAC 1982). However, it subsequently became a key reference in the lead-up to the 1988 program of phased tariff reductions across most industries. A further such tariff reduction program was announced in 1991, despite the onset of recession.

The more contentious reports have concerned Australia's most highly assisted manufacturing industries: passenger motor vehicles, and textiles, clothing and footwear. A measure of the Commission's ultimate success in helping to shape long-term assistance policy was government endorsement in the early 2000s of the Productivity Commission's advice on post-2005 tariff reductions and transitional assistance for these industries. However, earlier reports were not always so well received. Indeed, the previous reports (by the Industry Commission) in 1997 had been largely rejected. (Public Service insiders have even suggested that the response to the TCF report was decided before its shrink-wrap cover was removed!) By the same token, it can also be argued that, in the absence of the Commission's inquiries, there could well have been a *rise* in auto tariffs in January 2000, given the pressure being placed on the Government at the time (Banks 1998).

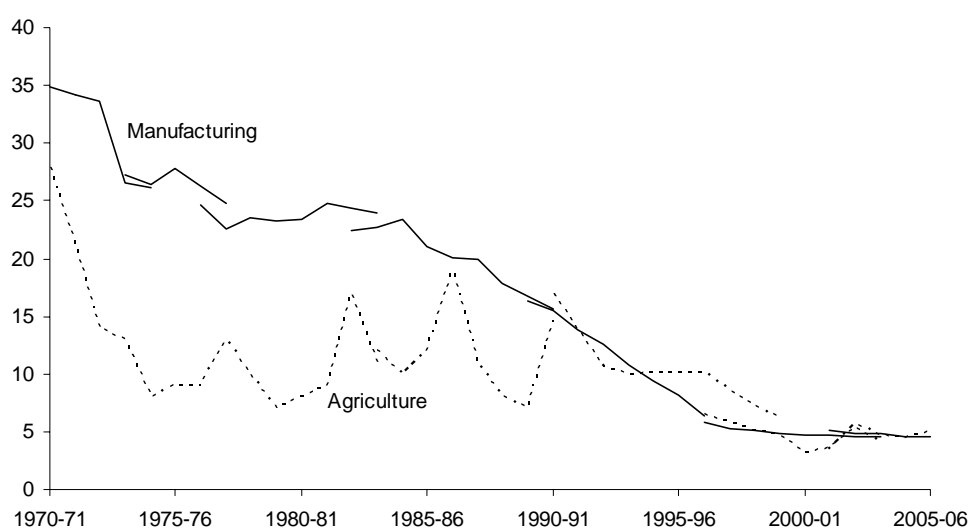
It has taken more than four decades of policy effort and debate to lower Australia's trade barriers and industry assistance levels, but the protectionist regime has been almost dismantled (Figure 1). Nevertheless, tariff reform remains incomplete. In 2000 the Australian Government deferred implementing the Commission's

recommendation to reduce the remaining general tariffs of 5 per cent to zero, preferring to delay removal until a time ‘consistent with trade and fiscal objectives’. Moreover, the legislated reduction in automotive tariffs has the caveat of a further review to be conducted by the Commission in 2008 ‘to determine whether changes are warranted to the legislated tariff reductions in view of conditions in the international trade environment’.

### *Achieving transparency ‘behind the border’*

With Australia’s tariff walls falling and competitive pressures on the traded goods sector rising, policy impediments ‘behind the border’ began to attract attention.<sup>4</sup> Initially, the Commission’s reporting helped to widen the microeconomic reform program in the 1990s to improving the performance of economic infrastructure services dominated by government-owned monopoly suppliers in energy generation and distribution, water, rail, ports and postal services.

**Figure 1 Declining industry assistance in Australia**



Data source: Productivity Commission estimates.

More recently, governments have embraced one of the principal policy messages arising from a series of Productivity Commission reports on the regulation of economic infrastructure — the need to rebalance the emphasis in the regulatory frameworks away from achieving immediate gains for users and consumers to also facilitate new efficient investment in telecommunications, gas pipelines, airport services and other essential infrastructure.

<sup>4</sup> The Tasman Transparency Group (2007) has pointed out that domestic transparency procedures are needed to bring opaque ‘behind-the-border’ barriers into account in trade negotiations. These barriers are pervasive in the markets for services.

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The Commission's inquiry work has contributed to reforms in other 'behind the border' areas involving anti-competitive regulatory regimes — such as in broadcasting, radio-communications, gambling and the occupational regulation of architects — as well as regulation affecting traded services such as international cargo liner services, harbour towage and international air services. The Commission's exposure of the extent of problem gambling, the adverse impacts of controls on native vegetation and biodiversity, measures to improve efficiency in the use of energy and water, and the scope to improve labour market outcomes through the redesign of programs for delivering unemployment assistance and regulating occupational health and safety, indicate the wider applicability of the Commission's transparency function.

### *Renewal of the Commission's mandate*

Perhaps the strongest vindication of the Commission's role is that successive governments from both the major political parties have renewed and expanded the institution's mandate over the last three decades. Government ministers have accorded the Commission a significant role in contributing to policy development (Box 5). Even some industry groups, which did not always like the Commission's findings, have valued the transparency and consultative nature of its processes. While there have been times when governments or oppositions were tempted 'to shoot the messenger', they have re-endorsed the value of having advice that is independent, transparent and economy-wide in perspective.

Further support for the Commission's transparency function is found in the preparedness of the different levels of government in Australia, through the Council of Australian Governments, to request that the Commission be sent references on cross-jurisdictional policy issues such as Australia's health workforce, road and rail freight infrastructure pricing and, most recently, the benchmarking of regulatory regimes.



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**Box 5 Government assessments of the Commission's contribution**

When introducing legislation into Parliament in 1989 to establish the Industry Commission, the then Government stated:

... the Industry Commission will further the important role that the Industries Assistance Commission has played in the structural adjustment process in Australia. It will build on the Industries Assistance Commission's earlier work which was instrumental in awakening the community to the costs of many industry assistance policies. As an institution, the Industries Assistance Commission has been an important force in economic policy in Australia, building community awareness of the need for Australian industry to be outward looking and internationally competitive. ... By providing independent and expert advice to the Government and through its public inquiry processes, the Industry Commission will facilitate the ongoing structural change that is needed in the economy. (Morris 1989, p. 2424)

The current Prime Minister has commented on the Commission's long-term contribution to trade and industry assistance policy formulation in the following terms:

The dynamic supporting trade liberalisation in democracies will only succeed if communities in each country believe it's in their interests to liberalise. In the Australian context, the work of the Productivity Commission and its predecessors ... has been fundamental to building and maintaining Australian public understanding of the benefits of greater openness to international competition ... Because of the Government's belief in the robustness and transparency of the Australian institutional framework, we have regularly advocated the Productivity Commission as a model for other countries to adopt. If other countries could adopt similar transparent institutional responses, public opinion would be better informed on the cost of trade barriers, and support would be built for good policies in broader areas of industry protection. (Howard 2003)

In a more general context, the current Treasurer has stated:

... the Productivity Commission has provided a vital, independent source of public information and advice to government on policy reforms needed to underpin Australia's long-term prosperity. (Costello 2003)

## Some implications

Australia's experience demonstrates that institutionalised transparency can help governments undertake beneficial reform and make better policies, but is also suggestive of some general cautions. Expectations need to be tempered: transparency is unlikely to transform the policy environment overnight. Building a pro-reform constituency in government and the wider community is a gradual process. It took Australia four decades to get tariffs down and more than a decade tackling sources of underperformance in economic infrastructure services. And neither reform program is yet complete.

That said, reforms once made in Australia have tended to stick, having stronger foundations of support or acceptance within the community precisely because the

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basis for reform *was* transparent. The programs of tariff liberalisation and regulatory reform initiated under one government have generally been maintained by new governments of different political complexions.

The Australian experience with early tariff reform is also instructive of the adverse consequences of avoiding transparency. The 25 per cent tariff cut of 1973 followed a report prepared secretly within government and was implemented without warning. In hindsight, there can be little doubt that it set back public acceptance of protection reform and created uncertainty about how reform would be conducted in future. Reflecting that uncertainty, and in response to pressure from those who stood to lose most from the tariff cuts, the Government subsequently acted to effectively quarantine Australia's most highly protected industries from the general reduction. While the 25 per cent cut lowered the average level of protection, the Government's subsequent selective imposition of quantitative restrictions increased the disparities in protection across industries. This greatly reduced the potential benefits. It is significant that, more than three decades later, the two manufacturing groups quarantined from the across-the-board reduction in tariffs are still the exceptions in Australia's otherwise low protection regime.

A second implication is that reform is a *process*, not an event. One set of reforms exposes the need for others. As Australia opened its borders to foreign goods, services and capital, 'upstream' inefficiencies in government utilities and inflexibilities in labour market regulation became more apparent and unacceptable to those facing new competitive pressures. This effectively enlarged the 'constituency for reform' within Australia. As noted, the Commission's work program went increasingly 'behind the border', to cover an array of industry assistance issues and anti-competitive regulation across the economy and, nowadays, the human capital related drivers of productivity growth and living standards.

A point to emphasise, given the context for this international conference, is that the Commission's contribution to Australia's trade policy has generally not been made as part of the trade negotiation process itself. Rather, the Commission's reports have focused on the case for domestic liberalisation. However, this unilateralist focus progressively affected Australia's approach to multilateral trade negotiations. In effect, the negotiations largely served to 'lock in' our protection reductions, through binding international agreements, rather than driving the reforms themselves (Banks 2003).

The nature of the Commission's contribution, which relies not only on solid research but also on providing adequate scope for public input and scrutiny, is not a good fit with the secrecy and rapidity that characterises decision-making in trade negotiations. However there is scope for the Commission to play a more direct role,

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by providing an assessment of the potential for gains and losses for Australia when prospective trade agreements are contemplated and, subsequently, before agreements are signed, assessing whether the final outcome from negotiations is likely to deliver net benefits for Australia. It could also provide guidance on more general or systemic issues, such as the product coverage of negotiations, the design of rules of origin (see PC 2004) or identifying the greatest distortions from a domestic welfare perspective.

A caveat is that there needs to be sufficient lead-time for the Commission to consult and test its analysis with other experts and those potentially affected. This applies equally to modelling work, which has previously been performed by consultants under tight timeframes. While the Commission no longer has a monopoly on modelling technology or expertise (to the contrary) it does provide a 'neutral' incentives environment for modelling directed at the national interest. In hindsight, the 'battle of the models' that occurred during the AUSFTA negotiations, arguably did more to confuse than enlighten the community about the likely outcomes for Australia from that agreement.

Finally, the longevity of 'the Commission' should not obscure the difficult times it weathered along the way. The institution found itself under threat of closure or emasculation on several occasions. It is the insights gained from the Commission's survival that are most likely to be of interest to those contemplating how transparency might best be introduced into the policy apparatus in their own countries.

### *Independence*

The Commission's independence has been invaluable in ensuring that its advice is not compromised or swayed by particular sectional or bureaucratic interests. Independence, together with quality analysis directed at community-wide ends, underpin the credibility of the Commission's advice in contentious areas of public policy.

However, this independence is not unfettered. Governments determine the policy questions on which the Commission provides advice and governments control whether and what changes in policy will be implemented subsequently. Thus, the Government can ensure that the Commission's formal advice does not stray into certain aspects of a policy issue that it believes should not be addressed. For example, the Commission's reference on telecommunications competition regulation explicitly excluded consideration of the structural separation of the dominant service provider. And an inquiry into the private health insurance industry and its regulation excluded consideration of reforms to the wider health system.

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Rather, the Commission's independence stems from its ability under its statute to provide the advice it considers will advance the overall interests of the community. There can, of course, be times of 'creative tension' between adviser and government — typically when the reasons governments use to explain policy decisions don't square with the criteria its independent adviser has used. Political commitment to the transparency function therefore requires a degree of forbearance by government in the face of advice that may sometimes be contrary to its wishes.

The independence of the transparency function can also be safeguarded by how appointments are made. The Commission has a small group of members appointed by the Government for fixed but renewable terms of up to five years. This permanency enables those members to provide continuity of experience across the range of the Commission's work and protects them against dismissal for providing 'unpopular' advice.

Consistent with the original Crawford conception, governments have in the main abided by the convention of appointing members on the basis of their general competence or expertise, rather than as representatives of particular industries or groups. Crawford saw the 'representational' model as flawed. With an economy-wide mandate, the range of interest groups laying (legitimate) claim for inclusion would make the size of membership unworkable. For excluded stakeholders, the agency would be tainted by perceptions that its advice was not truly independent of the views of those interests which secured representation.

In any case, specialist knowledge can be gained through consultations, use of consultants and staff recruitment. One innovation at the commencement of the Commission was the provision for appointing part-time Associate Commissioners for the duration of particular inquiries. This allows the Commission to draw on 'outside' experience and expertise in enhancing its analytical capability and understanding of the policy issues, as well as improving communication with stakeholders. However, again, the scope for such appointments to enhance the credibility of an inquiry depends on those individuals not having strong links to a stakeholder group that would deflect them from giving primacy to the interests of the whole community.

### *Portfolio affiliation*

For a transparency body to be effective, responsibility for it should rest with a minister having economy-wide responsibilities. The Australian experience is that the Commission prospered least when it reported to a minister with responsibility for a particular sector of the economy. In its first year of operation, the IAC reported to Parliament through the Prime Minister. Thereafter, responsibility for the

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Commission was transferred to a succession of industry-neutral portfolios before, in 1983, going to a minister whose prime responsibility was manufacturing industry.

The contrasting experience in the latter move shows that portfolio affiliation matters. A properly functioning domestic transparency agency acts as a counterweight to sectional interest groups, whereas industry ministers have industry constituencies to which they naturally feel the need to be responsive. The Commission's experience in the 1980s, like that of the Tariff Board, was that sectorally oriented government ministers and departments sought to limit the nature and flow of inquiries. Coordination arrangements within government for considering the Commission's reports also fell by the wayside and industry ministers did not concede any role for the Commission in their 'patch'.

The industry minister responsible for the Commission shed this light on his difficulty in obtaining worthwhile work for the IAC in the mid-1980s:

From time to time [the Chairman of the IAC] complained that the Commission didn't have enough to do. He suggested it might widen its scope and conduct an inquiry into the transport industry or the mining industry. In Cabinet the transport Minister Peter Morris rejected an inquiry into 'his' industry. He liked a quiet life, and was not keen on restructuring. I pointed out that manufacturers made numerous complaints about waterfront inefficiencies. Morris appointed an inquiry of his own. Nothing seemed to happen. The complaints were to go on. Gareth Evans as Minister for Resources said the mining industry didn't want to be inquired into. So nothing happened there either. (Button 1998, p. 264)

The IAC's transparency function had already been curtailed by legislative amendments in 1984. Among other things, these removed its ability to initiate its own inquiries into areas of industry assistance not reviewed for long periods of time. Though never used, that power had added force to the IAC's requests to government that its work program extend to reviewing impediments holding back the performance of the Australian economy. Without that power and with a ministerial stalemate on new work, the Commission's inquiry program was diminishing rapidly.

Responsibility for the IAC was transferred to the Treasurer in 1987, where the Commission has remained since. The move to the Treasury portfolio saw the announcement of a substantial forward work program covering, for example, impediments arising from government control and regulation of public utilities and domestic barriers to international trade in services. The diversity and significance of the Commission's work program since then — including reviews of transport and mining that had previously been stymied — demonstrates the importance of an economy-wide portfolio 'home' for such an institution.

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## *Resourcing*

In practical terms, adequate funding and control over its use determine how well the domestic transparency function can be performed. These were early ‘battle grounds’ as the Tariff Board began to reinterpret its role and saw a need for greater research, and bureaucratic opponents sought to hinder this. Subject to general governmental controls affecting public sector agencies, the Commission has control over how it uses its budget allocation to meet the needs of its inquiry, supporting research and other functions.

Control over its budget allows the Commission to decide on staffing levels and how best to supplement in-house skills. The Commission has also been able to make use of academics and consultants in developing appropriate conceptual frameworks for policy analysis and to tap the specialist skills needed for economic modelling and quantitative analysis.

The expansion of modelling capabilities within private interest groups or for hire by them, means that modelling can be used by those wishing to oppose economic reforms of benefit to the whole community. Governments themselves can use models to make decisions appear respectable that, if objectively assessed, may turn out to be indefensible. In either case, members of the public, without the technical know-how needed to make informed judgements, are left to make up their own minds what to believe and public discourse descends to an unproductive ‘battle of the models’. Thus an important consideration in resourcing an independent transparency body is to endow it with the resources necessary to help public understanding of what is at stake in policy initiatives and for the community to distinguish between spin and substance in the analysis of economic and trade reforms.

In particular, a domestic transparency institution must have the expertise to monitor and evaluate modelling even if it contracts out such work. The Commission’s current practice also brings external scrutiny to bear on its own quantitative analysis. It typically presents sensitivity analysis by altering key assumptions within feasible ranges, uses refereeing processes and holds workshops to have its modelling scrutinised by outside experts, and engages with other modelling analysts to understand why different models produce varying results.

## *Open inquiry processes*

Effective policy formulation in contentious areas of public policy requires effective consultation as well as good analysis. The hallmarks of the Commission’s inquiry procedures are: public notification of new inquiries and their terms of reference;

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face-to-face visits or roundtable discussions with major interest groups; insistence that all key aspects of submissions and the information and views provided at hearings be made publicly accessible; and exposure of the Commission's preliminary analysis and conclusions to public scrutiny before its advice to government is finalised.

Terms of reference play an important role in the transparency of policy advice. They are a public signal of the specific issues on which the government is seeking community input and the Commission's advice. Were it to occur, responsibility for unnecessarily constraining the scope of an inquiry or for 'loaded' terms of reference — effectively pre-determining the outcome — can be sheeted home to government. From time to time, attempts were made to 'condition' Tariff Board advice in these ways, and covert overtures to interpret terms of reference in particular ways needed to be rebuffed (Rattigan 1986). Statutory independence and open inquiry processes provide safeguards in such circumstances. The Productivity Commission has been given an additional protection: statutory licence to make recommendations on any matters it considers relevant in addressing the terms of reference received from government.

Open public inquiry processes underpin the domestic transparency function in a number of ways.

- Transparent inquiry processes ensure that the institution's research and policy advice are tested publicly and are therefore more robust than many other sources of advice to government, much of it self-serving or too narrowly focused. The Commission's findings and recommendations to government are shaped in the light of extensive public feedback on its draft report. This can reveal flaws or omissions which can be addressed in the final report. Indeed, some Commission final reports have contained significant differences to the drafts circulated for public scrutiny.
- The public inquiry process enables the views of all stakeholders to be heard, not just those of special interest groups. Public processes ensure that the arguments being advanced by interest groups are also subject to rigorous scrutiny, weakening their influence where they are poorly based.
- Open inquiry and reporting processes also perform an educative role — effectively enfranchising those community groups that would otherwise be unaware of policy impacts on them. In particular, media coverage of Commission reporting has ensured wider public dissemination of the analysis of policy changes that are in the longer term interest of the community. The better understood is the basis for policy change, the more likely it is that reforms will be accepted and supported in the broader community.

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- The Commission's processes and reports also provide governments with an opportunity to gauge, at arm's length, the likely reactions of those affected by different policy approaches. Indeed, for particularly sensitive issues, governments have sometimes preferred that the Commission assess a range of policy options or present (policy relevant) findings rather than settle on formal recommendations. Some reform proposals — such as those with concentrated adjustment costs — can require significant trade-offs among the different policy objectives of governments. In such circumstances, a prime role of the transparency function is to inform policy makers of the implications of different policy choices. Such processes help to reduce the prospects of governments being caught out by unanticipated responses from adversely affected groups.

### *An example for others?*

As a result of the system of open inquiries and public reports that form the basis for Australia's transparency arrangements, decision-making has been better informed about the future consequences of policy initiatives under consideration. This system has helped make it possible for Australian governments to move forward on economic and trade reform, a journey that is not yet over.

A final word to international readers. We recognise that Australia's transparency arrangements may not suit other countries. There can be no 'one size fits all' approach. Arrangements in other countries must necessarily reflect their cultural and political systems, and ensure domestic ownership of national trade policy. However, finding ways of achieving the broad principles of domestic transparency in other countries' institutional settings is an objective to which Australia's experience lends considerable support.



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