

Productivity Commission Inquiry

Impact of Competition Policy Reforms
on Rural and Regional Australia

Submission by:

Murray Regional Development Board

&

Riverina Regional Development Board

Background:

The Murray and Riverina Regional Development Boards are Government appointed bodies charged with leading community economic and regional development across over 20 local government areas in the Southern Region of New South Wales. With both Boards representative of this broad geographic area, they are well qualified to comment on the effects of National Competition Policy (NCP) in rural and regional Australia.

This submission concentrates on the areas of NCP that the Board feels most qualified to comment on, namely reforms to electricity, water, Telstra and Local Government. *It is not an all encompassing response to the impacts of NCP.*

Competition & Regional Development

While the the inquiry process will be focused on actual and perceived negative impacts of NCP, the Boards are very supportive of the broad thrust and objectives of making Australian industries more competitive. Much of the regions' output is exported where it competes with the best of other countries, hence the imperatives for reform across all sectors - production, transport and processing.

Reforms to transporting, especially wharf and road (fuel taxes) will greatly improve overall competitiveness - so essential for industries whose production relies on competitive transport systems over long distances to reach points for export.

Locational preferences by new and exporting businesses include access to reliable and cost competitive telecommunications as a high priority. Regional development requires a competitive table tilted in it's favour by targeted intervention by Governments in the operation of the market. This submission identifies areas where intervention is essential, with comments on a number of changes to present Commonwealth Government policies and their selective implementation by State Governments.

The Rural Outlook:

The effect of NCP:

Impacts of National Competition Policy have been felt right across the nation, through urban, regional, rural and remote areas. While in many cases these changes have improved the viability of certain services and improved levels of service, there have also been instances when communities, particularly those in regional and remote areas, have experienced a significant decline in the level of service.

The loss of services:

The loss of many basic services to rural and remote Australia has meant more than just the loss of access to government agencies and other services. In many cases, the loss of these services threatens the viability and sustainability of entire communities.

A declining population base:

Access to services remains a fundamental requirement for communities in regional and remote areas. Consequently, removal of services from these communities impacts severely on the sustainability of current population base, promoting a shift in population toward metropolitan and provincial cities at the expense of the many towns and villages in country Australia.

Under utilised infrastructure

With this decline in services and subsequently population, regional centres are being left with infrastructure which is surplus to their needs, ultimately capable of supporting much larger populations. Narrandera, in the Riverina region, is one such centre, with office space in various government buildings under utilised, a water/sewerage system capable of supporting 1-2,000 people over and above the current use, and recreational infrastructure capable of servicing a far greater population.

An ageing population:

This population shift towards urban areas away from the regions has had a profound impact on the viability of other business in these areas and ultimately the capacity of these areas to create sufficient employment opportunities for communities. This reduction in employment opportunities sees the movement of youth away from these areas, a significant contributing factor to ageing populations in regional and remote areas.

Inter-generational transition

The impact of other elements of NCP such as water reform have also placed pressure on primary producers to pursue increased efficiencies within their operations, ultimately leading to an increase in the size and scale of their farming enterprises. These increases in the size of farm operations are proving to be significant, hindering the entry of new better educated players with limited capital, ensuring that those already in farming find it more difficult to get out of the industry.

Competition Policies & Sustainability of Natural Resources:

The reform agendas for water and vegetation clearance have major implications as to the way these natural resources are utilised. Whilst support is generally strong across the Regions for the principles behind these reforms, tensions are increasing between the simultaneous attainment of environmental and economic objectives.

Of particular importance is the cumulative effects of these and other reforms on the adjustment capacity of the rural sector - a subject that requires much more understanding and attention by policy developers. Further, the capacity to adjust is not uniform as there is great variability of performance between similar farm enterprises and businesses.

Suggested improvements: There are opportunities for much more broadly based consultation lead by agencies with a sound understanding of the rural scene. Farmers and those who service them (public and private providers) are seeking extensive educational programs, supportive assistance from agencies and targeted financial incentives over a number of years.

Rural adjustment

The Commonwealth and the NSW Government Rural Partnership Programs - *West 2000* for the pastoralists in the Western Division and *Kickstart Sunraysia* for horticulturists in the far west of the Region have been well received in their second year of operation. During the year the Commonwealth released its new policy on rural adjustment - Agriculture - Advancing Australia. These regional approaches to adjustment appear to be more effective than the previous generic national approach. Flexibility is the key to the delivery of regional adjustment policies and it is pleasing to report that this appears to be now accepted by the Commonwealth.

Water Reforms

The NSW Government in their discussion paper on "Water Sharing in New South Wales - access and use" issues are raised that challenge and change the historical role of governments in promoting development and in providing certainty with respect to all their actions which for irrigators revolves around having defined property rights for their water licence.

Suggested improvements. It is crucial that the processes for development of any changes arising from this Discussion Paper and others of a similar nature be undertaken in a manner where there is on-going and extensive consultation within a flexible timetable. Secondly, irrigators are seeking certainty with respect to their water licences and very much resent the present lack of use by governments of water trading markets to acquire water for the environment. The present salami slicing approach is reducing irrigators security to entitlements. Socio-economic impact studies, as outlined in the COAG principles, are not being undertaken by governments either preceding or during reformist processes with a 'one size fits all' philosophy where no account is taken of a particular areas ability to adjust to change

Infrastructure Reforms Under NCP:

Electricity:

Aims of Reform:

- Reduce prices
- Increase consumer choice
- Increase customer service levels

Regional Situation:

The NSW Electricity market is moving towards being fully deregulated by the 1st January, 2000. At present, those businesses using more than 160MW/h per annum at a single site, have the option of choosing their electricity retailer. In rural and regional areas, such sites are a rarity rather than the norm. In support of this, when the Murray Region Organisation of Councils surveyed member councils for such sites, it found less than five across 7 local government areas.

While granted that prices have been reduced under a deregulated market structure (for eligible parties), the question must be asked; at what cost to service? In an arena where services have traditionally been delivered in a manner conducive to economic development in the regions, capital investment and maintenance to the networks in densely populated regions appear now to be given priority over rural and remote areas.

Case 1: Balranald Substation

Put simply, it is the opinion of many from the Balranald region, that current electricity supply is inadequate. As such a new substation needs to be constructed in the very near future. The deliberations over construction of such a substation at Balranald have continued for a period of over 3 years, proving to be a serious impediment to industry development in that particular area.

Over this time, the opportunity costs of inadequate infrastructure have continued to mount. Industry have at times had to endure delays and production losses due to power outages. In extreme cases, entire operations have been lost to the region, along with the employment opportunities they create.

Furthermore, during this period, commitment has been made to construct a new substation at Balranald, and then been rescinded after reforms have taken place. Correspondence has been received from Murray River Electricity confirming action plans to construct the proposed substation with a completion date of 30 November 1997. Since this time, Australian Inland Energy, the current responsible body, have concluded current supply as 'adequate for current needs'.

It is the view of the Murray Regional Development Board that this about face must be attributed to the reform agenda and the 'profit at all costs' ethos that has come with it.

As the Balranald Substation case suggests, free market forces alone will not permit adequate maintenance and capital investment in rural and remote regions as sales revenue received from those regions for the most part, is proportionally small in comparison to the bottom line costs required.

Under a system of county councils, funds for these maintenance programs were contributed to by State Electricity Charge revenue. Under a corporatised market system, this revenue is now returned to the State Government as a dividend, and as a consequence, maintenance funding is reduced.

In addition to this, cost shiftings are evident in smaller Local Government Areas, where historically works were provided on a cooperative basis, and are now subject to greater cost recovery provisions.

Finally, it is the opinion of the Board that Government intervention into the provision of utility services is essential in maintaining the integrity of service delivered in regional and remote areas. A system where State Electricity Charge revenue is better returned to the region is needed urgently, ensuring that rural and regional networks do not deteriorate any further, and have the capacity to meet industry development requirements.

Water

Aims of Reform:

- Promote economic and environmentally sound use of water resources
- Rural water charges reflect actual cost of delivering water to users

Regional Situation:

Water is the lifeblood of the Murray Region, with the vast majority of farming methods and enterprises reliant on regulated supply. Major industries in the region that are totally reliant on water include viticulture, horticulture, dairy and rice processing. In total these industries account for over \$650 million of NSW GVP.

Since reforms of the water industry took place, water prices on a permanent trading market have increased from around \$100 per megalitre(ML) to between \$400 - \$450ML. As such, operating costs in these industries have risen dramatically, in many cases affecting the viability of whole farming enterprises.

If then, as suggested in the issues paper for this inquiry, that trading of water should be expected to ease the financial burdens of farmers and graziers, it has obviously failed in that most primary producers reliant on water will be facing a greater financial burden.

Impacts of water reform have not only been felt by existing industry. It is also serving to be an impediment to investment and effectively regional development, in that any expansion in industries reliant on irrigation now requires capital investment of a greater magnitude.

Competitive Neutrality and Local Government

Aims of Reform:

The basis concept is that a "level playing field" should exist between persons competing in a market place, particularly between private and public sector competitors. Local Government Businesses should operate without net competitive advantage over other businesses as a result of their public ownership.

Efficiency in business operations is assumed. The real basis, for Council compliance with competitive neutrality principles is to ensure that all business costs are recognised, and if there is subsidisation of a Council Business activity it is explicit and the Council will be politically accountable for that support.

Regional Situation:

The application of competitive neutrality principles to NSW Councils will only affect operations that can be classified as business activities. Councils must assess their operations and designate activities that are businesses. Category One businesses are where turnover exceeds \$2M. Other businesses are Category Two and turnover must be greater than \$50K. Separate internal reports must be prepared and full cost attribution to the business must occur. The same rules and regulations as apply to the private competitor must apply to the business and a complaints handling process must be established.

In the case of Albury City Council, the following have been classified as businesses:

- Water Supply
- Sewer Services
- Airport
- P.S. Cumberoona (tourist boat)
- Engineering Design Services
- Sports Stadium, Athletics complex, Swimming Pools.
- Banjora Child Care Centre
- Cemetery/Crematorium

Victorian Local Government has taken a different approach whereby 50% of Council's turnover must be subject to "market testing" and Council operations have been restructured by having one section responsible for buying services (*client*) under a compulsory competitive tendering (CCT) process. Another section of the Council (*provider*) can tender for the Council works, and also compete in the market place against private and other Council businesses.

NSW Local Government has not gone down the CCT path but has opted for a competitive provision of service (CPS) approach. Business activities that are in direct competition with other providers are identified and required to compete on a "level playing field". The compliance processes have already been

outlined. Traditional Council services are delivered by the means that the individual Council considers appropriate and efficient.

The NCP requirements that NSW Local Government must observe are not considered to be onerous, but will require some changes in management and operational structure, and financial operations and reporting. Concern is raised about the possibility of Victorian type changes.

In Victoria, operational changes were also accompanied by structural change to Local Government and have produced some improvements in efficiency and short term cost savings. Nevertheless, there have also been examples of private contractors undertaking traditional Local Government activities and failing to perform to the council's satisfaction resulting in protracted conflict and litigation and subsequent decrease in service levels.

Some small communities have been devastated by the lost of Council activities i.e. Tungamah in Victoria. "Contract specified" levels of service have caused conflict with some Councils when omissions are noticed or changes are required, as these prove to be very expensive to rectify.

These Victorian experiences are of concern to rural NSW, and on an industry basis are not favoured, although some Sydney Councils are reorganising along the Client/Provider lines. When plenty of options for competition is available CCT is very beneficial to a Council, however when options are limited, as is the case in some parts of rural Victoria the results could be detrimental in the long term.

Reform of Government Monopolies:

Telstra

Aims of Reform:

- Reduce costs
- Increase level of service
- Increase consumer choice

Regional Situation:

Deregulation of the telecommunications industry and the partial privatisation of Telstra has provided impetus for significant changes. By design, this has led to an increased level of competition in service provision in major populated areas such as the capital and provincial cities, but has led to little or no change in rural and remote areas.

Furthermore, this has also seen a vast reduction in the number of service personnel located in these regions, impacting adversely upon timely fault rectification and connection of services. Pecuniary penalties are not an effective mechanism in ensuring prompt service as they fall well short of the forgone income and undermine existing client business relationships. While the Boards agree that some of this can be attributed to re-structuring and the preclusion of inefficiencies, much of it must be attributed to the profit driven operation of a company seeking to deliver to its shareholders.

With telecommunications traditionally being provided as an essential utility service, many areas have been serviced with infrastructure that is uneconomic and which provides poor return on investment. As such, the maintenance and investment in such services is now either ignored or delivered at the most 'cost effective' means, which is not always the most 'service effective'.

This provides problems for existing telecommunications infrastructure in rural and remote areas, and not surprisingly, abets a reluctance to invest in technological changes such as data capable lines and mobile telecommunications. The projected revenue from such services is, in most cases, a fraction of the total investment costs required.

This is not to say that increased competition has not provided any benefits to rural and remote areas. In larger population centres, competition has indeed increased along with the service, but it is only in the major centres where this has occurred. The attractions then, of outlying regions adjacent to these centres are not great, nor are the regions near the high yield end of the market, rendering them less likely to be subject to capital investment by telecommunications carriers.

The application of the Universal Service Obligation has been touted as the method to secure investment in the regions, although in reality it may undermine their case for investment. In the event that the USO is applied to Telstra with stipulations such as the standard telephone service and potentially ISDN capable lines, this will present circumstances where the cross subsidy

funded by metropolitan revenues will become inflated, along with the costs to Telstra.

Those telecommunications providers not effected by the USO then, will have a distinct advantage over Telstra, undermining the fundamental notion behind NCP; '*a level playing field*'. To combat this, it is essential that the USO is applied to the telecommunications industry as a whole, with funding for it's application being derived from licensing fees and industry levies, ensuring that the obligation is as the name suggests, a 'universal service obligation'

Suggested Improvementa: Pecuniary penalties have not proven to be a sufficient deterrent in ensuring service provision, in that they do not adequately compensate customers who have suffered as a result of delays in servicing and connections of services, This can to be addressed in two ways; by increasing the level of pecuniary penalty, as well as attaching service expectations to licensing agreements where failure to meet obligated levels of service may result in license cancellations.

It is essential that the USO is applied to the telecommunications industry as a whole, with funding for it's application being derived from licensing fees and industry levies, ensuring that the obligation is as the name suggests, a 'universal service obligation'