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**PERFORMANCE OF NSW
GOVERNMENT BUSINESSES
1996-97**

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PERFORMANCE OF NSW GOVERNMENT BUSINESSES 1996-97

MICROECONOMIC REFORM

FEBRUARY 1998

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Foreword



This is the eighth issue of this publication documenting the performance of NSW Government businesses.

NSW is forging ahead with microeconomic reform.

Highlights in 1996/97 included the first phase of the national electricity market and gas access pricing arrangements.

NSW Government businesses are now more productive. Across the board there have been substantial improvements in operational efficiency, financial performance and levels of

service.

Families and businesses have benefited directly from lower prices, as the Government Charges Index contained in this publication shows. They have also benefited from better service and indirectly from dividends that have helped to fund new public investments.

The Government has undertaken a substantial corporatisation program to separate regulatory functions from business operations.

This edition contains some changes made necessary by the process of corporatisation and the development of competitive markets.

It now contains 27 agencies, an increase on last year. This is because several have appeared in their own right for the first time such as the newly corporatised transport agencies and the electricity generators and distributors.

The introduction of competition in electricity has meant that some information that was previously made public has become commercially sensitive. Balancing this, the new energy

corporations now produce detailed annual reports and other financial statements.

Despite these changes, every effort has been made to allow meaningful comparisons with previous reports.

This report shows that commonsense improvements to Government businesses are working and delivering big gains for the community.

Hon Michael Egan MLC
Treasurer

Executive Summary

New South Wales has been engaged in comprehensive reform for over a decade. Now much of the reform is pursued under the auspices of the National Competition Policy which has helped to coordinate and facilitate reforms in areas which extend across jurisdictional borders.

During 1996-97, reforms in electricity, gas, transport and water have been the focus of much of the reform initiatives.

The electricity supply industry is in a state of flux with increasing competition between entities within NSW and, now with the first stage of the national market, interstate. During 1996-97, six electricity Government Business Enterprises (GBEs) were corporatised. Reforms have seen prices of electricity for businesses fall by up to 40 per cent. Household consumers are expected to be able to choose their electricity provider in the near future.

Also, New South Wales has taken a leading role in achieving free and fair trade in gas in Australia, having already implemented an effective framework for providing third party access for natural gas distribution within its boundaries. New South Wales has been a prime mover in establishing consistent access arrangements at a national level. A key outcome of the NSW reforms will be a significant reduction in the price of gas.

Across all GBEs the benefits from microeconomic reforms continue to flow. In particular, the government charges index fell by 1.2 per cent in real terms during 1996-97. Furthermore, these GBEs made dividend payments to the NSW Government of around \$1.5 billion.

Improved labour and capital usage in government businesses has seen productivity in the six largest GBEs double over the seven years from 1989-90 to 1996-97.

Microeconomic reforms in New South Wales are delivering benefits in the form of lower prices and higher dividends. The returns from early reforms serve as encouragement to continue the reform process with vigour. [\[back\]](#)

(1) Overview of Microeconomic Reform

The Rationale for Microeconomic Reform

The foremost objective of government is to improve the living standards of its citizens manifested via increased real incomes and/or increased leisure time. This is achieved by implementing policies which improve our economic stability and trading benefits with our trading partners.

Macro policies such as fiscal, monetary and tax policies are partially able to change the performance of our industries at an aggregate level. However, micro policies concentrate on improving productivity at the firm and government business enterprise (GBE) level, streamlining regulations and improving the way the markets function. For example, improving resource allocation and efficiency.

Micro policies include labour market reform, reform of structural monopolies, reform of legislation and reform of prices.

Reforms in New South Wales have spillovers into other States and vice-versa. There are benefits in all States broadly coordinating the microeconomic reform process to synchronise the timing of reforms and facilitate reforms that spread across State borders. In the areas in which national markets currently operate or could potentially operate to realise the benefits of competition, the reforms are coordinated by way of the National Competition Policy (NCP).

Over the past three decades, productivity growth has accounted for around one half of the expansion in Australia's GDP (growth in capital, the workforce and other resources explain the remainder). Moreover, productivity growth is estimated to have accounted for around two thirds of the 80 per cent growth in per capita incomes over that period.

It is for these reasons that governments are focussed on microeconomic reform given that it underpins improvements in the economy's productivity performance which in turn delivers higher standards of living.

Benefits of Microeconomic Reform

Microeconomic reform increases the standard of living of NSW citizens and more broadly all Australians. Improvements may come from increased real income, greater leisure time being enjoyed for the same amount of output, or an increased number of jobs available.

In a report produced for the Council of Australian Governments (COAG), the Industry Commission (IC) estimated the revenue and economy-wide effects of implementing reforms recommended in the Hilmer Report, along with a set of related reforms. Specifically, the IC modelled the impact of reforms in the transport, communications and utilities sectors, in statutory marketing arrangements, government services, unincorporated enterprises and tempering of anti-competitive legislation.

The estimated economy-wide benefits of the reforms were estimated to be:

- a \$23 billion (5.5 per cent) increase in real GDP, with around half attributable to improved GBE performance. Major contributors to the GDP increase included the electricity, gas, telecommunications and rail sectors; and
- a \$9 billion gain to consumers, equivalent to \$1,500 for each Australian household; an increase in real wages of 3 per cent; and 30,000 extra jobs.

Of the reforms the IC modelled, those at the State, Territory and Local Government levels were estimated to contribute \$19 billion (or 4.5 per cent of GDP) and reforms by the

Commonwealth were estimated to contribute \$4 billion (or 1 per cent of GDP).

The extent of the reform gains has been questioned by a minority of commentators who contend that the gains are diminishing, non-linear and incorrectly attributed to microeconomic reform rather than technological advances.

Despite these contentions, the broad consensus among economists, business leaders and policy makers is that microeconomic reform, in its own right, delivers tangible benefits.

Aside from the magnitude of the benefits, the way in which benefits from microeconomic reform are manifested is an important issue. Benefits may be enjoyed through lower prices for goods and services produced by those entities subject to microeconomic reform initiatives. Alternatively, benefits may take the form of higher profits distributed to government in the form of dividends.

In the case of higher profits enjoyed by entities undergoing reform, the way in which benefits are shared depends on the type of ownership. Government businesses return the benefits of reform back to the community in two ways: lower prices and higher profits (which are paid as dividends to the government and then may be used in building hospitals, schools and infrastructure).

The IC also estimates that from the mid-1980s onwards, productivity gains have been passed on largely through lower prices. The best performing sectors in this regard were Electricity, gas and water, and Transport, storage and communication. Microeconomic reforms have been central to this improved performance. [\[back\]](#)

Table 1: Productivity Performance 1974-75 to 1994-95

Industry	Average Annual rate of MFP (per cent)	Sectoral Contributions to Annual Average Productivity Growth (per cent) ^a
Agriculture	1.2	7
Mining	-0.2	-1
Manufacturing	2.0	50
Electricity, gas and water	2.9	11
Construction	0.6	6
Wholesale trade	0.1	2
Retail trade	0.5	5
Accommodation, cafes and restaurants	-1.3	-4
Transport, storage and communication	3.3	26

Cultural and recreational services	-1.4	-3
Total	1.2	100

Source: IC (1997) *Assessing Australia's Productivity Performance*, AGPS, Canberra.

^a Productivity growth in each sector is weighted by the relative size of the sector in the first year of each period.

The reforms have exposed Australian industries and government enterprises to increased competitive pressure, heightening incentives to be cost conscious, innovative and productive.

It is evident that there is some delay between implementing reforms and realising the benefits. This is not surprising as microeconomic reforms may take some time to implement, especially when they involve the creation of a national market and accompanying infrastructure. It may take time for a new market to begin to operate efficiently and begin delivering the benefits to the community. It is partly for these reasons that benefits from microeconomic reform are only now just beginning to emerge. However, they can be expected to continue indefinitely.

National productivity indicators have recently been showing stronger and more sustained growth than could be expected on the basis of past recoveries from recession. In fact, productivity has grown at twice the rate of many other OECD countries between 1989 and 1994. Improved productivity provides room for the economy to grow faster without facing inflationary pressures.

The IC estimates that the annual growth in multi-factor productivity in trend terms has increased from less than 1 per cent in 1989-90 to around 2.3 per cent in 1995-96. Currently, the annual increase in multi-factor productivity is running at around 2.2 per cent, levels comparable to the "golden age" of the late 1960s.

Some recent examples of the gains from reform are:

- across 73 of Australia's major GBEs in the Electricity, gas and water, and Transport, storage and communication industries average real prices fell by over 5 per cent in 1995-96, continuing an uninterrupted trend of falling average real prices since 1991-92 of 15 per cent. Customer satisfaction within most sectors improved, average profitability showed a modest improvement in 1995-96 with significant increases in payments to governments. The return on assets rose in 1995-96;
- average business costs for electricity in New South Wales have fallen by 23 per cent in real terms since 1992-93, according to the Independent Pricing and Regulatory Tribunal (IPART);
- the real price of international telephone calls fell by 40 per cent between 1989 and 1995. The liberalisation of the telecommunications market in July 1997 offers the prospect of the average international call price from Australia falling to as low as 47 cents per minute, well under half the estimated average price of \$1.11 in 1995-96;
- in aviation, by allowing international code sharing, the cost to consumers of a standard

economy airfare on international flights is estimated to have fallen by around \$200 per ticket; and

- a study by the Justice Research Centre has found that deregulation of conveyancing services has contributed to a reduction of 17 per cent between 1994 and 1996 in the average fee charged by small law firms for residential conveyance in New South Wales.

While factors other than microeconomic reform influence the rate of productivity growth, there is a considerable overlap between high productivity sectors such as those outlined above and sectors subject to comprehensive reform.

Environment for Microeconomic Reform

To a large extent contemporaneous studies are important in helping identify areas in which there is potential for microeconomic reform benefits and areas in which benefits from reform strategies have begun to produce results.

During 1996-97 several major studies were undertaken, including:

- Final Report of the Financial System Inquiry (discussed below);
- Committee of Inquiry into Sale of the NSW Electricity Assets (discussed below); and
- Review of Business Programs (the 'Mortimer' Report).

Final Report of the Financial System Inquiry (the 'Wallis' Report)

In mid-1996 the Commonwealth Government appointed Mr Stan Wallis to chair a review committee to undertake a major inquiry into the financial system, with a requirement that it report to the Treasurer by 31 March 1997.

NSW Treasury coordinated a whole-of-government submission to the Financial System Inquiry (FSI) which was submitted in October 1996. The submission presented the views of the NSW Government on a number of regulatory issues to be canvassed by the Inquiry including:

- the regulation of non-bank financial institutions;
- the merger of banks; and
- the taxation of financial transactions.

The FSI released a discussion paper in November 1996. The paper included an invitation to those who wished to provide a further submission to the Inquiry by 13 January 1997.

NSW Treasury coordinated the preparation of a supplementary NSW Government submission to the Inquiry. Its purpose was to discuss some issues raised in the Discussion Paper and emphasise that the States had been forced to impose taxes on financial transactions (which are recognised to be inefficient) because of both the constraints imposed by Commonwealth-State financial relations and the current interpretation of the Constitution by the High Court.

The FSI released its Final Report on 9 April 1997 containing 115 recommendations dealing with regulatory reform in relation to:

- conduct and disclosure;
- financial safety;
- stability and payments;
- mergers and acquisitions;
- promoting increased efficiency;
- coordination and accountability; and
- managing change.

Following a preliminary response in April 1997 (which ruled out mergers between the four major banks for an interim period), the Commonwealth Treasurer released a formal Commonwealth response broadly endorsing the FSI recommendations on 2 September 1997.

Key among the reforms announced by the Commonwealth Treasurer, are those requiring the cooperation of the States and Territories:

- the establishment of the Australian Prudential Regulation Authority (APRA) by 1 July 1999 to prudentially supervise deposit taking institutions, life and general insurance companies and superannuation funds. It will enable transfer of prudential supervision of building societies and credit unions under the Financial Institutions Scheme. Coverage may be extended to friendly societies, trustee companies and cooperative housing societies subject to the States' agreement. APRA is to be funded by the financial institutions it regulates;
- establishment of the Australian Corporations and Financial Services Commission (ACFSC) to cover financial market integrity, disclosure and other consumer protection issues. The ACFSC will expand the current charter of the Australian Securities Commission (ASC);
- implementation of a single licensing and prudential regulation regime for all deposit taking institutions; and
- facilitating the establishment of a single complaints referral service for consumers of retail financial products and services.

NSW has responded to the recommendations of the FSI by giving "in principle" support for the recommendations bar a few minor issues.

Committee of Inquiry into Sale of the NSW Electricity Assets ("Hogg" Report)

The NSW Government established the Committee of Inquiry into Sale of the NSW Electricity Assets to report on the desirability of the Government selling its electricity assets. The Committee, as outlined in its terms of reference, was to assess the sale of electricity assets with regard to the following criteria (among other things):

- direct and indirect social usefulness of these public assets;
- impact on consumers and quality of service;
- original purpose of the enterprise;
- retention versus the expected sale value;
- current structure of the market place; and
- competing demands on the NSW public sector and existing budgetary constraints.

The Hogg committee released its findings in August 1997 and overwhelmingly supported the immediate sale of NSW electricity assets (the Snowy Mountains Hydro Electric Authority was excluded from consideration). Risk was identified as the key factor in the overall

recommendation owing to:

- increased competition at the national level;
- the industry being in a state of rapid flux; and
- current buoyant conditions for privatisation.

While NCP does not address the nature of ownership, there are ramifications from microeconomic reforms. Liberalising markets generally increases the intensity of competition and the nature of ownership appears to have some influence on the ability of an entity to respond to change. The Hogg Report suggests that GBEs may not be able to respond to the changes in the market as effectively as privately owned enterprises. This is not necessarily because of better management in privately owned enterprises but simply because of the non-commercial demands placed on the entity through the political process.

Progress of Microeconomic Reform in New South Wales

The NCP brings together a broad range of reforms in respect to timing of implementation and the overall package of reforms. NSW has embarked on an ambitious program of microeconomic reform.

New South Wales has implemented a wide range of reforms in 1996-97 across numerous industries. Broadly, the reforms include among other things:

- repeal of legislation requiring registration of some types of agricultural activities, thus reducing administration and compliance costs for businesses;
 - contracting out of specialist skills held by NSW government departments in the areas of health, road and transport technologies;
 - new enterprise agreements which include performance based enhancements;
 - licensing arrangements in water and electricity to manage pollution; and
 - improved water pricing policies. [\[back\]](#)
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(2) Aggregate Performance of NSW Government Businesses

NSW Government businesses supplying electricity, transport and water account for almost 70 per cent of total revenue collected by GBEs. These businesses also represent around 75 per cent of total GBE employment. Consequently, improvements in labour productivity in these areas have a relatively large impact on the overall performance of GBEs. The following GBEs are included in the three sectors outlined above:

- Pacific Power, Macquarie Generation and Delta Electricity;
- Advance Energy, Australian Inland Energy, Energy Australia, Integral Energy, Great Southern Energy and North Power;
- State Rail Authority, State Transit Authority, Rail Access Corporation, Rail Services Authority and FreightCorp; and
- Hunter Water Corporation and Sydney Water Corporation.

Figure 1 shows that, since 1989-90, NSW GBEs have significantly improved their labour productivity resulting in an improvement in weighted productivity of over 100 per cent.

Figure 1: Labour Productivity for major NSW Government businesses

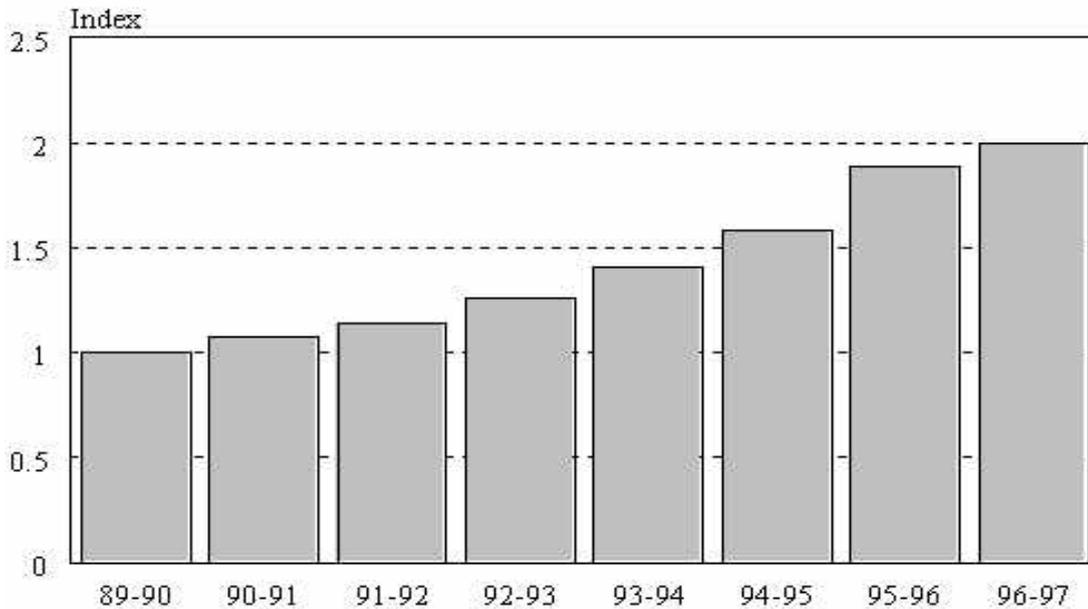


Figure 2 shows that these input cost savings have largely been passed on to consumers (rather than being paid as dividends to government) and have facilitated a move to more appropriate rates of return for government businesses.

Figure 2: Dividend and Tax Equivalent Payments from Non-Budget Sector Enterprises (Nominal Dollars)

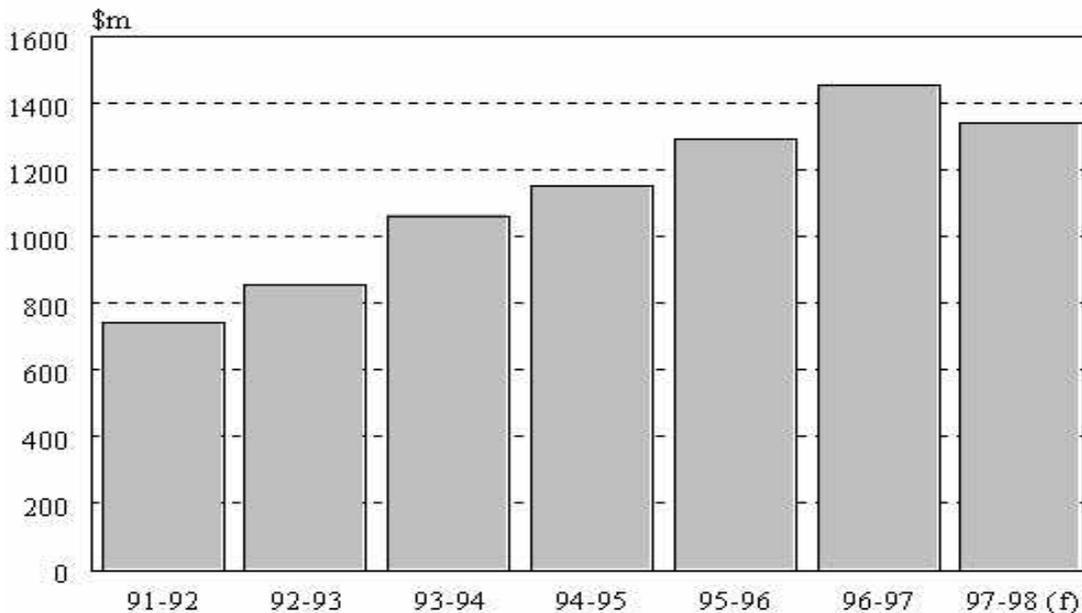
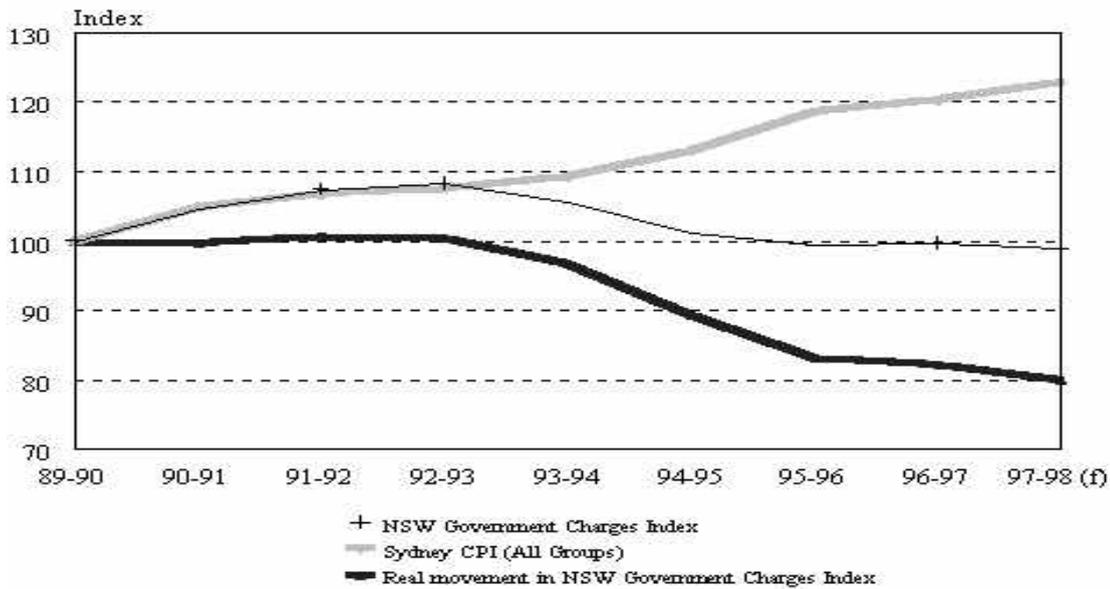


Figure 3 shows that, in real terms, the NSW Government Charges Index (GCI) fell by 1.2 per cent in 1996-97 and in cumulative terms since 1989-90 the GCI has fallen by almost 20.1 per cent. It is projected that the GCI will fall by a further 2.8 per cent in 1997-98 in real terms.

Figure 3: NSW Government Charges Index



To some extent the GCI understates the fall in government charges since it reflects charges to household consumers in the main. Business charges, which in some instances are subject to long term contracts, have experienced large reductions and these are not incorporated in the GCI.

For example, businesses holding contracts with electricity suppliers have, to date, enjoyed large reductions in electricity prices. These individual contracts account for around a quarter or more of electricity revenue which is not in the scope of the GCI.

Table 2 shows the output, employment and productivity performance of the six largest GBEs between 1989-90 and 1996-97.

Table 2: Employment, Productivity and Output Performance of the 'Big Six' New South Wales GBEs

	(1)	1989-90	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97 to 1997-98	% Change 1989-90
Employment										
Electricity Generators	(2)	7,283	6,710	6,482	5,870	5,757	5,595	3,503	3,328	-54%
Electricity Distributors		15,395	15,008	13,641	12,752	11,644	11,394	8,744	7,972	-48%
Hunter Water Corporation		1,128	1,082	995	934	799	740	715	620	-43%
State Rail Authority		28,842	24,602	24,447	22,803	21,270	20,184	19,742	15,938	-43%
State Transit Authority		5,428	4,914	4,423	3,897	3,740	3,795	4,101	4,303	-21%
Sydney Water Corporation		9,582	9,357	9,142	8,429	7,324	5,945	5,099	4,743	-50%
		67,658	63,675	59,170	54,885	50,538	47,677	41,904	34,924	
Index of Output										
Electricity Generators (Gwh)		100	102	103	108	109	112	118	113	13%
Electricity Distributors (Gwh)		100	105	104	109	111	115	118	119	19%
Hunter Water Corporation (properties served)		100	102	104	105	108	111	107	109	9%
State Rail Authority (aggon gas mass um)		100	101	98	93	95	100	101	103	3%
State Transit Authority (passenger carried)		100	101	98	97	97	93	97	100	0%
Sydney Water Corporation (properties served)		100	99	100	101	103	105	104	108	8%
Productivity (Output relative to Employees)										
Electricity Generators		6.5	7.2	7.4	8.8	9.0	9.4	14.1	14.2	149%
Electricity Distributors		2.3	2.5	2.8	3.1	3.4	3.4	4.8	5.3	132%
Hunter Water Corporation		145.4	154.3	170.9	185.2	221.5	245.9	245.4	287.9	98%
State Rail Authority - CityRail		20.8	22.1	23.0	22.5	23.4	29.9	31.0	31.0	49%
State Rail Authority - CountryLink		2,288.1	2,497.4	2,174.0	2,125.4	2,341.1	2,058.0	2,228.4	2,323.4	2%
Finight Corp		1,047.0	1,140.0	1,220.0	1,472.0	1,777.0	2,074.0	2,335.0	3,302.0	209%
State Transit Authority		38.4	43.0	44.2	52.0	54.4	51.4	49.4	48.8	24%
Sydney Water Corporation		145.1	144.4	152.0	143.4	195.2	244.8	290.3	314.9	117%
Weighted Total Output Change (%)	(3)									9%
Total Employment Change (%)										-45%
Weighted Productivity Change (%)	(4)									101%

Notes

- (1) Employment measured as equivalent full time persons as at 30 June.
- (2) Figures revised from 1990-91 due to change in treatment of Sydney's aboriginal hydroelectricity authority employees. Transit Unit staff included in 1994-95 employment number.
- (3) Output weighted by the 1992-93 dollar value of output from each agency.
- (4) Average productivity of each agency weighted by final year employment.
- (5) CountryLink data series has been revised

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(3) Performance Measurement of NSW Government Businesses

In a well functioning market, price changes provide signals about the quality of and demand for goods and services. The outputs of government agencies are typically traded in markets where prices are either not free to adjust or do not exist. Consequently, an alternative to the price mechanism is needed to indicate performance improvements and guide resource allocation decisions.

Measures of performance provide:

- a catalyst for policy ideas;
- information to facilitate accountability;
- a means of identifying areas for review;
- a means of monitoring policy implementation and success;
- information on potential productivity improvements for an agency;
- a means of analysing the interrelationship between agencies and between programs, to allow governments to coordinate policy across agencies. For example, the

- interrelationships between policing, courts and correctional services;
- information to promote yardstick competition in government agencies which face little direct competition in input or output markets;
- a powerful internal management tool for agencies - they provide managers with an idea of how efficient they are, explain reasons for poor performance and can identify appropriate 'leading performers';
- guidance for structural change; and
- assistance for the resource allocation and/or budgeting process by providing a means of allocating funding between competing needs based on performance and need, rather than historic precedent.

Several government exercises are developing consistent indicators for the performance of government agencies. For example, the IC's International Benchmarking Program, Steering Committee on National Performance Monitoring of Government Trading Enterprises 1996, Steering Committee for the Review of Commonwealth/State Service Provision 1995 and this publication *The Performance of NSW Government Businesses*. These exercises provide useful information to compare the performance of agencies with similar agencies in New South Wales, Australia and overseas.

The publications provide some technical and economic efficiency measures. However, the main indicators of efficiency are usually unit cost per unit of service or partial productivity measures, such as service per employee.

Partial indicators can vary for reasons other than efficiency; for example, government agencies may deliver services in different environments, have a different mix of clients or use different input mixes. Focussing on partial measures such as output per employee, for example, can be misleading because it only tells part of the story - how labour is moving with production. It says nothing about capital.

As a consequence of the shortcomings of partial indicators, governments are turning to more comprehensive techniques such as Data Envelopment Analysis (DEA), Total Factor Productivity (TFP) and Shareholder Value Added (SVA). The techniques combine information on the major services (outputs) and inputs of government agencies to provide better measures of performance. The key features of these techniques are outlined in Table 3 below.

Table 3: Basic features of SVA, TFP and DEA

	Measures	Features
SVA	Economic profit - operating profit after tax and a charge for debt and equity (also known as Economic Value Added)	<ul style="list-style-type: none"> • financial analysis tool • separates a firm's operations from its financing • deducts the opportunity cost of capital(debt and equity) from operating profit • uses a cash flow format where possible
TFP	Productivity - ratio of outputs (weighted by revenue shares)	<ul style="list-style-type: none"> • index number technique • handles multiple inputs and outputs

	to inputs (weighted by cost shares)	<ul style="list-style-type: none"> • - requires prices of inputs and outputs
DEA	Technical efficiency - identifies best practice within the sample and measures efficiency relative to best practice units	<ul style="list-style-type: none"> • linear programming technique • handles multiple inputs and outputs • does not need prices (useful for non trading Budget Sector agencies)

NSW Treasury is increasingly using these techniques to monitor the performance of major agencies. It is encouraging agencies to use the techniques to identify reasons for poor performance that would otherwise go unnoticed, such as management practices, scale of operations or government regulation.

A comprehensive SVA framework has been developed jointly by NSW Treasury and the State's government businesses. This framework is being implemented in two stages and is being phased in over a three year period for 37 government businesses, with final implementation by June 1999.

NSW Treasury has developed a new financial tool, called Profit Composition Analysis, which links TFP and profit changes. It provides a framework for measuring the distribution of productivity gains amongst a firm's major stakeholders - its customers (prices), workforce (wages) and owners (dividends). A pilot study has been undertaken for a NSW water supply business. Further pilot studies are planned for other government businesses supplying major infrastructure services and DEA will be used to help specify service targets for the major government service providers in 1998-99.

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(4) National Competition Policy

In 1995, the Council of Australian Governments (COAG) agreed to undertake microeconomic reforms in accordance with an agreed framework, the National Competition Policy (NCP). The framework ensures that all States focus on similar reforms thereby maximising the benefits of microeconomic reform at the national level. In particular, the agreement coordinates reforms for sectors with national markets such as electricity, gas, water and road transport.

The NCP is focussed on creating competitive markets which deliver benefits to business and consumers and as such does not stipulate the type of ownership arrangements for GBEs. However, the competitive neutrality principle in the package requires that where government businesses sell goods and services into competitive, or potentially competitive markets, prices are set so as to eliminate any net competitive advantages stemming from government ownership.

The progress of the NSW Government in implementing microeconomic reform under the auspices of the NCP is important in several respects.

Firstly, the implementation of these reforms promises to increase consumer choice and

facilitate the efficient allocation of resources in the economy. Secondly, and most obviously, the competition payments from the Commonwealth Government hinge on the effective implementation of reforms, as assessed by the National Competition Council (NCC). This should, in the long run, enhance the State Budget position by extracting better value from the expenditure side and, through economic growth, enhancing the revenue side.

The NCP program is contained in three inter-governmental agreements, which are discussed below.

Conduct Code Agreement (CCA)

The CCA sets the competitive landscape on which the reforms are to take place. The CCA requires that the Competition Code, a schedule in the *Trade Practices Act 1974* (TPA), is applied by all Australian governments through enacting legislation. In particular, the Competition Code requires the application of Part IV of the TPA which relates to restrictive trade practices and unconscionable conduct.

The *Competition Policy Reform (NSW) Act 1995* enacted the Competition Code and has applied since 21 July 1996. All persons, unincorporated associations, corporations, professions, government agencies and government businesses are required to comply with the Competition Code.

Initially, government businesses were subject to a grace period permitted by the Australian Competition and Consumer Commission (ACCC). This expired on 1 July 1997.

In relation to the Competition Code Agreement and application of the TPA, there are two important aspects:

- New South Wales must notify the ACCC within 30 days of any legislation or provision in legislation which is reliant on s51 of the TPA; and
- New South Wales may, under s51 of the TPA, exempt conduct that would ordinarily be subject to part IV of the TPA. However, the Commonwealth Minister may table regulations under s51(1C)(f) which in effect removes the exemption. Any exemption is permitted by the NCC providing that there are net benefits to the community and that objectives of the legislation or regulation can only be achieved through restricting competition.

The NSW Dairy Corporation and the Sydney Organising Committee for the Olympic Games (SOCOG) have been exempted for certain activities since the introduction of the Competition Code. Under the Competition Policy Reform (NSW) Regulation 1996 and *SOCOG Amendment Act (NSW) 1996* respectively, certain marketing arrangements were exempted, until 1998, to ensure they do not contravene the TPA or the Competition Code.

Competition Principles Agreement (CPA)

The CPA lists six principles applying to government businesses which are designed to enhance competition in markets for goods and services. In essence, the principles stipulate:

- prices surveillance of monopoly and near monopoly activities;
- introduction of competitive neutral pricing by government businesses competing with each other or the private sector;
- structural reform of government businesses through separating regulatory from core operating activities, and for the latter, separating competitive, or potentially

- competitive activities from monopoly activities;
- review and, where appropriate, reform of all existing legislation which restricts competition;
- third party access to significant infrastructure facilities; and
- application of the above competition principles to local government businesses.

NSW progress in conforming with these principles is summarised below.

Independent Prices Oversight

The CPA requires signatories to have independent prices oversight of monopoly and near monopoly government business activities. New South Wales meets this requirement through IPART, whose functions are to:

- set maximum prices and review pricing of scheduled NSW Government monopoly services, which include electricity, water, public transport and gas;
- undertake general reviews of industry, pricing or competition as required by the Premier; and
- register agreements for access to public infrastructure assets and arbitrate disputes about such agreements.

IPART undertook the following activities in 1996-97:

1. Price regulation:

- electricity capital contributions and recoverable works;
- public transport fares for CityRail and STA services;
- prices for miscellaneous customer services for Sydney Water Corporation;
- electricity prices (July 1997); and
- bulk water prices (1997-98).

2. Advice to the Government on industry issues:

- pricing principles for local water authorities;
- bulk water prices;
- pricing of public passenger transport services;
- regulation and licensing of air services in New South Wales; and
- pricing principles for CountryLink.

3. Access to public utility infrastructure services:

- completion of a determination on conditions of access by third parties to AGL's gas distribution networks;
- publication of practice notes for use in arbitration undertaken by IPART;
- successful resolution of an access dispute between the National Rail Corporation and the Rail Access Corporation of NSW; and
- establishment of a register of access arrangements.

The recent IPART determination on AGL's operating terms and conditions provides for:

- a substantial reduction in its charges for transporting gas. Average charges will fall from \$2.26 to \$1.05 per GJ by 1999-2000 (a fall of almost 60 per cent in real terms); and

- elimination over three years of the cross-subsidy from business customers to households, while keeping price increases to households capped well below increases in the CPI.

Competitive Neutrality

The objective of the competitive neutrality principle is to ensure that where government businesses sell goods and services into competitive markets, their prices are adjusted to eliminate any net competitive advantages attributable to government ownership. Government signatories to the CPA are to ensure their businesses adopt:

- a corporatisation model;
- full Commonwealth, State and Territory taxes or tax equivalents;
- debt guarantee fees (which in effect restore the true cost of debt); and
- regulations to which private sector businesses are normally subject.

The above requirements are exempted only where it can be shown that there is a net public benefit from not implementing competitive neutrality. While each party is free to determine its own agenda for the implementation of competitive neutrality principles, a policy statement on competitive neutrality, including an implementation timetable and complaint mechanism, was required by June 1996.

In June 1996, in accordance with the CPA, the NSW Government published its *Policy Statement on the Application of Competitive Neutrality*.

New South Wales recognises the possibility of competition between general government enterprises from different States and Territories, and has indicated support for the development of nationally consistent guidelines for pricing and costing.

A State Owned Corporation (SOC) model has been adopted to achieve these reforms. It requires the entity to adhere to commercial disciplines and function on the basis that government, and more broadly the community, are shareholders. It is embedded in a Financial Policy Framework which requires government businesses to be subject to:

- the application of a SVA framework;
- regular performance monitoring (including in some cases TFP);
- the payment of State taxes and Commonwealth tax equivalents;
- the payment of risk related borrowing fees; and
- explicitly funded Community Service Obligations (CSO).

Despite these commercial objectives, SOC's remain accountable to the relevant Minister and Parliament. The CPA offers discretion on ownership and does not require privatisation of government businesses.

By way of the *State Owned Corporations (NSW) Act 1989*, two types of SOC structures have been created - the company SOC and the statutory SOC. Both have a Board of Directors, share capital and a memorandum and articles of association similar to a public company limited by shares. The full extent of the *Corporations Law* applies to company SOC's. Statutory SOC's are in the main exempt from the *Corporations Law* except for provisions relating to officers' duties and liabilities.

Corporatisations to date have spanned electricity generation and distribution, ports, transport and waste services. During 1996-97, the following government businesses were

corporatised:

- Snowy Mountains Hydro Electricity Authority;
- NSW Lotteries;
- Coleambally Region Irrigation Areas & Districts; and
- Murrumbidgee Region Irrigation Areas & Districts.

Budget agencies with business activities which are not corporatised and which therefore do not have commercial disciplines imposed, are required to introduce charges which reflect full costs by 1997-98. This requirement also applies to government businesses not already under the Financial Policy Framework or those not currently subject to IPART price regulation.

Competitive Neutrality Complaints Mechanism

As part of the competitive neutrality obligations, the States were required to develop arrangements for responding to complaints. The arrangements outlined in the *Policy Statement on the Application of Competitive Neutrality* consisted of two stages:

- firstly, the party lodging a complaint is to approach the relevant government agency to clarify and attempt to resolve the matter (this first step also acts as a sieve to eliminate trivial complaints or misunderstandings); and
- secondly, and only if necessary, to refer the matter for independent assessment by a third party complaints mechanism wherever the complainant is not satisfied with the response of the agency involved. The necessary arrangements for IPART dealing with generic complaints and the State Contracts Control Board dealing with tendering complaints are in the course of being implemented.

Structural Reform of Public Monopolies

The NCP requires the separation of operating activities from the regulatory functions of government businesses before the business is subjected to competition. It then requires operating activities to be separated into monopoly and near monopoly on the one hand, and competitive or potentially competitive activities on the other, with a view to promoting the latter because of greater community benefits generally ensuing.

Where natural monopoly activities exist, there is to be independent prices oversight (as discussed above) so as to optimise community benefits.

There has already been substantial structural reform of the electricity and rail industries in New South Wales.

New South Wales has restructured the regulatory and operating sectors of the electricity industry, with the operating sector further divided into its natural monopoly (transmission and distribution) and potentially competitive components (generation and retail). The passage through the NSW Parliament of the *Electricity Supply (NSW) Act 1995*:

- established a unified legislative framework for the industry;
- provided for transmission and distribution of network service provision;
- fostered competitive retail electricity supply; and
- regulated the wholesale electricity market.

In addition, New South Wales through the *Transport Administration Amendment (Rail*

Corporatisation and Restructuring) Act 1996, has separated the operation of rail services from the ownership, provision of access and the maintenance components of the State Rail Authority. Four transport entities now exist:

- State Rail Authority - focussed on providing customer services;
- Rail Services Authority - responsible for track maintenance;
- Rail Access Corporation - responsible for managing the rail network and administering access by public and private operators; and
- FreightCorp - responsible for non-passenger freight services.

To accord with the Related Reforms Agreement, New South Wales is required to structurally reform the electricity, water, gas and road transport industries. Reform of these industries is discussed below.

In its report on the first tranche payments, the NCC considered that New South Wales had met its reform commitment to reform monopolies under Clause 4 of the CPA in a number of areas apart from those mentioned above. These included:

- NSW Lotteries Commission;
- Murrumbidgee and Coleambally Region Irrigation Areas & Districts schemes;
- Sydney Market Authority;
- Valuer General's Office; and
- The Office of the Public Trustee.

Legislative Review and Reform

New South Wales has prepared a comprehensive program of review of legislation restricting competition. Around 200 pieces of legislation were identified and listed for review before the year 2000 in the June 1996 statement.

While acknowledging the general comprehensiveness of the NSW legislative review program, the NCC drew attention to a need to review the *Casino Control Act 1992*.

The NSW Government's position is that there is a public benefit from the current Act, in that the reduction in the risk of criminal influence and exploitation of gambling plus the up-front payment for an exclusive 12-year licence outweighs the cost of restricting competition. The arrangements were arrived at following extensive debate within the Parliament and the community at a comparatively recent time. Any decision to introduce variations to these conditions, let alone introduce a free market for casino licences, would be controversial and potentially costly for the taxpayer.

The NCC does not consider the New South Wales case sufficient for exclusion from review, but has reserved judgment until July 1998. New South Wales will have discussions with the NCC prior to July 1998 on the casino legislation.

Treasury and the Cabinet Office conducted a review of the TAB privatisation proposals in accordance with competition policy requirements.

Current TAB privatisation plans propose the vesting of exclusive licences with the TAB to undertake the following activities:

- provision of off-course totaliser wagering in New South Wales;
- operation of a State-wide linked jackpot system on certain gaming machines in

- registered clubs; and
- provision of a centralised monitoring system for gaming machines in registered clubs and hotels.

The above review culminated in the preparation of a Report which identified the following net public benefits:

- facilitating a more competitive and efficient national wagering market;
- ensuring the accrual of privatisation rents to the NSW Government (but not at the cost of consumers); and
- preserving continuity in meeting social policy objectives.

In late 1997, the NSW Parliament passed the *Totalizator Legislation Amendment Bill* which amended a range of statutes necessary to facilitate the privatisation proposal. These amendments included exemptions from the TPA for the exclusive licence arrangements referred to above. As part of the process of notifying the ACCC of the exemptions, an advance copy of the Net Public Benefit report was forwarded to both the ACCC and the NCC in accordance with Clause 2 of the Conduct Code Agreement.

Another issue which the NCC is currently discussing with the NSW Government is rice industry marketing arrangements. The NCC is critical of the NSW Government decision to continue the current vesting arrangements for the domestic marketing of rice, and considers that the decision does not meet the spirit of the CPA. The NCC's view is based largely on the fact that the independent review panel recommended the deregulation of the domestic vesting arrangements, while leaving monopoly export arrangements intact.

The NSW Government has agreed to consider the policy concerns of the NCC. Recognising this, the NCC did not penalise New South Wales in the first tranche payments, deciding to reassess the position prior to July 1998 for the second tranche payment. The NSW Government understands that the NCC is considering withholding a one-off payment of \$10 million if the rice decision stands.

Some 52 reviews were scheduled for 1995-96. As at 31 December 1996, 36 legislative reviews had been completed and a further 15 were underway. From the 1996-97 program, five reviews have been completed, 47 are in progress, and three are yet to commence. Eight pieces of legislation are under consideration for national review.

Benefits arising from the completed reviews include:

- reductions in administrative arrangements;
- reductions in compliance costs; and
- repeals of unnecessary legislation.

Third Party Rights to Negotiate Access

One requirement of the CPA (Clause 6) is to provide third party access to significant infrastructure facilities with a view to facilitating upstream or downstream competition of net benefit to the economy. Duplication of this capital investment would not be in the public interest as more often than not the current infrastructure has the capacity to carry more customers and service providers. Therefore, it is necessary to remove the monopoly control of the infrastructure from the incumbent and permit access to third parties.

Access is to be provided where:

- it would not be economically feasible to duplicate the facility;
- the facility is of national significance; and
- safe use by the third party can be ensured at an economically feasible cost.

In August 1995, the NSW Government released a framework for the establishment of State access regimes. The essential features of the framework include the following:

- the NSW third party access regime will apply to infrastructure of less than national significance, but considered of State significance to New South Wales;
- third party requests for access should in the first instance, be resolved by voluntary negotiations between the access seeker and the entity owning or managing the infrastructure, according to Government protocols which ensure compliance with the principles set out in Clause 6 of the CPA;
- in all areas where such regimes are established, IPART will handle dispute resolution matters and will advise where necessary on pricing and related access issues; and
- there will be a right of appeal on an IPART decision to a court, but only on matters of law and not on the grounds of deficient economic analysis.

Electricity

Third party access provisions were incorporated in the State Electricity Market Code, effective from May 1996, and apply equally to the high voltage transmission network operated by TransGrid and the various distribution networks in New South Wales. The Code, which governs the operation of the interim State wholesale market, provides for IPART to arbitrate on any disputes arising from third party access negotiations. It has received interim authorisation from the NCC and will eventually be replaced by a National Code.

Rail

The NSW rail access regime to be established covers the former SRA's rail network. Third party access provisions will permit new rail operators to enter the market and compete with public operators in such areas as coal and grain haulage. Agreement in principle has been reached between the NSW Government and the NSW Minerals Council on the phase-out of the monopoly rent component in Hunter Valley rail freight charges for coal and on transparent charging arrangements in the future.

The third party access regime applicable to the NSW rail network was introduced in August 1996. As with the gas regime, it will require NCC approval for accreditation as an effective State regime. Approval has been sought but has not yet been obtained.

The track and other fixed rail infrastructure are vested in a new entity, Rail Access Corporation (RAC), which will set terms for access to private and public operators. This arrangement is well in advance of any requirements at the national level. The separation is designed to drive efficiencies in network asset management and represents a first step in progressing towards an open access policy for private train operators.

Gas

New South Wales developed an access regime for gas distribution services as a transitional measure prior to the introduction of the National Code. The NSW Access Code was modelled on the national framework, but with certain variations (for example, IPART has greater discretion over reference tariffs). New South Wales applied for certification of its

regime in October 1996. The NCC's recommendation to certify the regime was approved by the Commonwealth Treasurer in August 1997. The NSW Code will be replaced by the National Code according to an agreed timeframe.

Local Government

New South Wales has made significant progress in applying the competition principles to local government, particularly in developing guidelines for implementation.

Application of competitive neutrality policies and principles to local government will be comprehensive, with a threshold of \$2 million in gross operating income requiring separate cost centres and the application of corporatisation principles. Below this threshold, local government businesses are required to apply full cost attribution principles and set prices which reflect full costs where practicable, unless a net public benefit from not doing so can be demonstrated.

A complaints mechanism for local government business activities has been established involving the business in the first instance, and then the Department of Local Government where the complaint cannot be readily resolved. Some 10 complaints have been considered by the Department since May 1996.

Agreement to Implement the National Competition Policy and Related Reforms (RRA)

The RRA spells out the conditions under which the Commonwealth Government will provide financial assistance to the States, subject to there being no major deterioration in Australia's economic circumstances.

Commonwealth assistance is provided by way of:

- maintaining the real per capita guarantee of the FAGs pool on a rolling three year basis; and
- making \$4.2 billion (1994-95 dollars) of Competition Policy Payments over nine years to the States and Territories in three tranches, on a per capita basis and in a way that is independent of the Commonwealth Grants Commission process.

Based on the NCC assessment of NSW's compliance, New South Wales is expected to receive \$1.4 billion in financial assistance (around 34 per cent of total Competition Policy Payments). In 1997-98, \$72.6 million was received following the NCC's recommendation to the Commonwealth.

Apart from stipulating the conditions for payment, the RRA also seeks to include specific industry reforms which have been the subject of separate agreements. These reforms are crucial in securing the full benefits of microeconomic reform because of Australia's industry structure and geographic factors, and are discussed below.

Electricity

Since the Heads of Government meeting in May 1992, New South Wales has been formally committed to reforming the electricity supply industry and establishing a competitive market along the eastern sea board.

New South Wales has been one of the leaders in reforming the electricity industry, operating

a competitive market for trade in wholesale electricity since May 1996. The NSW retail market is now open to participation by any licensed electricity retailer, and the ability of customers to purchase electricity from any supplier is gradually being extended.

New South Wales has also been at the forefront of moves to establish a fully competitive electricity market in Australia. On 4 May 1997, New South Wales, Victoria, and the ACT established the first stage of an interim national market in advance of the fully competitive market. This was achieved through harmonisation of the arrangements in NSW and Victorian electricity markets to enable electricity generators to compete to supply power to retailers in the three jurisdictions, and indirectly to South Australia. New South Wales has substantially restructured its electricity generation and distribution arrangements to provide for greater competition in electricity supply.

The case for privatisation has been examined by the Hogg Committee, which made recommendations on the need for regulatory change, regardless of the timing of privatisation. These recommendations are currently under consideration.

The NSW electricity industry has been restructured to separate the regulatory components from the operating components. Generation, transmission, distribution and retail make up the operating components. The distribution and transmission network components exhibit natural monopoly characteristics (it is not economical to duplicate "poles and wires"), however, generation and retail components are seen as contestable.

The *Electricity Supply (NSW) Act 1995* was introduced during 1995-96 and provided the legislative framework for the establishment of the wholesale electricity market, competitive retail electricity supply and transmission and distribution network service provision.

Under the RRA, to satisfy the requirements for the first tranche payment, New South Wales is to:

- effectively implement an interim national electricity market by 1 July 1995, or on such other date as agreed between the parties; and
- agree to subscribe to the National Electricity Management Company and National Electricity Code Administrator.

In this regard, New South Wales has reached agreements with the relevant parties:

- to subscribe to National Electricity Code Administrator and the National Electricity Market Management Company;
- to the structural separation of generation and distribution; and
- ring-fencing the "retail" and "wires" businesses within distribution areas.

The NCC has deemed that New South Wales has complied with its first tranche payment requirements in the case of electricity.

New South Wales has progressively introduced competition to large retail customers: from June 1997 customers with electricity consumption above 750 Mwh (generally energy intensive businesses) were able to choose to buy power from any electricity retailer in the market.

At present, around 40 per cent of electricity demand is contestable and it is planned that by July 1998 customers with consumption above 160 Mwh (supermarkets and the like) will become contestable. All retail customers are expected to become contestable by July 2000.

The full National Electricity Market is expected to commence on 24 May 1998 by which time it is envisaged that Queensland and Tasmania will join the ACT, Victoria and New South Wales. All parties will be subject to:

- the National Electricity Code; and
- National Electricity Law.

Gas

New South Wales has taken a leading role in achieving free and fair trade in gas in Australia. It has already implemented an effective framework for providing third party access for natural gas distribution within its boundaries and has been a prime mover in establishing consistent access arrangements at a national level. The NSW regime is consistent with the proposed national framework and will operate until the national regime comes into effect. New South Wales has endorsed the substance of the draft National Access Code and has agreed to implement it within the timetable agreed by COAG.

A key outcome of the NSW reforms will be a significant reduction in the price of gas. This will flow from AGL's proposal for providing third party access established in accordance with the NSW regime. The proposal sets out AGL's undertaking on the terms and conditions for access to its gas distribution system. The determination on AGL's terms and conditions provides for:

- a substantial reduction in the cost of transporting gas. Average charges will fall from \$2.26 to \$1.05 per GJ by 1999-2000 (a fall of almost 60 per cent in real terms); and
- elimination over three years of the cross-subsidy from business customers to households, while keeping price increases to households capped to well below increases in the CPI.

Water

Water reform promises to be a main focus in the second tranche assessments.

The water reform framework is based on the February 1994 COAG Strategic Framework for Water Reform. It embraces pricing reform based on the principles of consumption based pricing and full cost recovery, the reduction or elimination of cross-subsidies and making subsidies transparent. The framework also involves the clarification of property rights, the allocation of water, institutional reform and public consultation and participation.

Implementation is expected to result in a restructuring of water tariffs and reduced or eliminated cross-subsidies for metropolitan and town water services, with the impact on domestic customers of water services being offset by cost reductions achieved by more efficient, customer driven, service provision.

In the case of rural water services, the framework is intended to generate the financial resources to maintain supply systems should users desire this and through a system of tradeable entitlements to allow for water to flow to higher value uses subject to social, physical and environmental constraints.

Major urban authorities

In June 1996, IPART released its medium term (four years) price path for Sydney Water Corporation. A two-part tariff is in place with property based charges eliminated for the

residential sector from October 1995.

Bulk water charging

Rural New South Wales consumes about 80 per cent of all water consumed in the State. Until 1994-95, users on regulated streams paid water charges to 70 per cent of the costs of 'running the river'. Capital costs of water storage and major works were regarded as sunk costs and maintenance costs were met by Government.

In September 1995, bulk water pricing was referred to IPART. IPART has recently conducted a review of the pricing of resource management, supply and licensing of bulk water by the Department of Land and Water Conservation (DLWC). The bulk water report, released in September 1997, is to apply to prices for 12 months from 1 July 1997.

IPART has noted that in the past, water was allocated to agricultural use at prices that did not generally cover the operating and management costs of water services, let alone the high capital costs of the infrastructure.

IPART has found that bulk water prices should recover the appropriate share of total operations, maintenance and administration costs, capital charges and external environmental costs. Joint costs should be apportioned to users on the basis of the principle that the beneficiary pays and this should be worked out on a regional basis.

IPART has introduced region-specific two-part tariffs for regulated rivers with greater emphasis on the usage component so that prices are better linked to consumption. Prices for regulated rivers will increase by up to 20 per cent (except the Murray and Murrumbidgee regions where revenues are maintained at the current level) and up to 15 per cent for unregulated rivers.

COAG requirements are for full cost recovery of water and related costs by 2001. While this will require substantial CSO payments borne by the Budget, the prognosis is for improved cost recovery in the longer term from users and optimisation of land use through more effective price signals.

Whether or not full cost recovery will be achieved by 2001 will depend on the asset valuation and pricing methodology that is adopted, in the context of the original COAG agreement. Work has been underway throughout 1996-97 with a view to clarifying requirements in this regard.

Road Transport

Road transport has in the past been a source of regulatory inefficiencies. In particular, charges have not been reflective of road network usage and safety standards have varied across jurisdictions.

The National Road Transport Commission was established to develop and implement a national approach to problems affecting heavy vehicles including:

- uniform heavy vehicle charges;
- uniform arrangements for transportation by road of dangerous goods;
- vehicle operation reforms covering national vehicle standards, road worthiness, mass and loading laws, oversize and overmass vehicles, and road rules; and
- a national heavy vehicle registration scheme.

New South Wales implemented the heavy vehicle charges and the associated permit reforms by State legislation on 1 July 1996 and is progressing the required reforms in other areas along with other jurisdictions.

The NCC has determined that New South Wales has complied with its first tranche road transport reform commitments. [\[back\]](#)

(5) Other Related Reforms

Infrastructure

The infrastructure programs of the NSW Government play a key role in the growth and development of the NSW economy by providing the basic infrastructure required by the business sector and households.

State Governments dominate public infrastructure, owning about two thirds and are responsible for providing the greatest range of infrastructure services such as:

- transport and communications;
- housing and community services;
- health and education; and
- energy services.

The direct responsibility for the provision and management of the majority of State infrastructure assets has rested with GBEs. The significance of private sector investment in infrastructure is gradually increasing. This is reflected in the fact that the private sector's share of new gross infrastructure investment is higher than its share of the stock of infrastructure. Private sector involvement, generally, reduces the funding burden for the State and improves the efficiency of infrastructure investment and operation through:

- equitable sharing of risks between private sector and Government;
- a market-based approach to investment decisions;
- cost reflective pricing;
- greater response to consumer preferences; and
- a commercial culture with strong pressures for efficiency gain.

Much of the increased private sector involvement in New South Wales has involved Build, Own, Operate and Transfer (BOOT) type arrangements. BOOT type arrangements are schemes where the private sector builds, owns, operates and then transfers the infrastructure, usually after 20 to 30 years, to the public sector. They are a form of structured financing with many complex contractual relations based on equitable risk sharing. In New South Wales thus far, they have been used to provide transport, electricity, water and sewerage infrastructure. A BOOT usually involves the interaction of the following parties:

- the Government, through an agency such as the Roads and Traffic Authority;
- the ownership vehicle, comprising of a concession company and a trust;
- debt financiers, usually a major trading bank; and
- equity investors in shares in a concession company or units in a trust (in the case of the M2 Motorway for example).

The private sector ownership vehicle usually obtains its revenue stream directly through charges to the users of those facilities. The main examples are the toll road contracts. The

private sector in these cases has come to assume the full market risk as well as all the construction and operational risks. Generally the toll road company is issued with a franchise to levy tolls on traffic using the road for a period of about 30 years. The normal commercial default conditions apply to these contracts. That is, there is no government obligation to step in if the company encounters financial difficulties.

The NSW Government has increasingly encouraged the private sector to assist in the provision of infrastructure as evidenced by its issuing of *Guidelines for Private Sector Participation in the Provision of Public Infrastructure*. The broad policy in this regard is that:

- the involvement of the private sector in the provision of infrastructure must show a net benefit to the community;
- privately financed infrastructure will be subject to competitive bidding;
- risks and returns must be appropriately shared between the government and the private sector;
- preference will be given to projects which are financially free-standing without any government capital contributions; and
- the extent of any government financial support for the project needs to be defined.

Under the *Public Authorities (Financial Arrangements) (NSW) Act 1987*, the Treasurer has responsibility for approving agencies to enter into joint financing arrangements. NSW Treasury advises the Treasurer on the joint financing obligations proposed by the sponsoring agency and agrees on the terms and conditions for contract negotiations.

New South Wales has contracted nearly \$6 billion of BOOTs up to 30 June 1997, covering over 23 projects. The majority of this expenditure has been associated with the provision of tolled motorways. There has also been sizeable investment in the development of rail projects and water treatment plants for metropolitan Sydney. In 1996-97 contracts were signed for three items of privately financed public infrastructure as outlined in Table 4.

Table 4: Privately Financed Public Infrastructure Contracts (1996-97)

Project	Total Cost (\$ million)	Government Contribution (\$ million)
Randwick Hospital car park	23.4	0.7
Olympic Village	444.6	196.5
Olympic Stadium	620.0	101.0
Total	1088.0	298.2

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(6) Performance of NSW Government Businesses

[Advance Energy](#)
[Australian Inland Energy](#)
[Delta Electricity](#)
[EnergyAustralia](#)
[FreightCorp](#)
[Great Southern Energy](#)
[Department of Housing](#)
[Hunter Water Corporation](#)
[Integral Energy](#)
[Land Titles Office](#)
[Macquarie Generation](#)
[Newcastle Port Corporation](#)
[NorthPower](#)
[NSW Lotteries](#)
[Pacific Power](#)
[Port Kembla Port Corporation](#)
[Department of Public Works and Services](#)
[Rail Access Corporation](#)
[Rail Services Authority](#)
[State Forests](#)
[State Rail Authority](#)
[State Transit Authority](#)
[Sydney Ports Corporation](#)
[Sydney Water Corporation](#)
[Totalizator Agency Board](#)
[Transgrid](#)
[Waste Service NSW](#)

(7) Glossary, References and Footnotes

The performance of each organisation is measured by a number of unique indicators, as well as more generic indicators, which are defined below.

All dollar amounts have been converted to 1996-97 prices, using the Sydney year-average Consumer Price Index, apart from the current and forecast year estimates which are in 30 June 1996 dollars (consistent with the approach in previous publications). Removing the impact of inflation assists analysis of the underlying trends in the indicators.

Efficiency Indicators

Employment

Effective Full Time Staff, derived by adding full-time staff to the full-time equivalent of any part-time staff.

Output per Employee

Where appropriate, physical output divided by employment. In other cases, real revenue per employee is reported. Annual changes in this indicator are one measure of efficient utilisation of labour resources in the enterprise.

Staff hours lost to industrial disputes:

Reported as an aggregate number of hours lost to industrial disputation or as an average figure per employee.

Customer service indicators

Market share

An indicator of the agency's performance within its industry. This indicator is not relevant for all agencies. Shifts in market share are indicative of competitive strategies within the agency and of external changes, including market deregulation, to the operating environment.

Real price index

A single index constructed for each agency to identify how customer charges have moved in relation to the Sydney Consumer Price Index. The index commences at 100 in 1988-89.

An increase in the index reflects a real increase in charges; an unchanged figure indicates that the movement in charges equals the change in the CPI; while an index trending downward measures real decreases in charges to consumers.

The 1994-95 Performance Book saw the introduction of a new method of reporting on the Real Price Index. For those agencies appearing both in the Government Charges Index (GCI) and the Performance Book, a series constructed from the movement in charges reported in the GCI is used.

The change was implemented to ensure consistency between the GCI and the data reported by agencies in the rest of the Performance Book.

A consequence of this change is that forecasts of the Real Price Index are not available.

The Government Charges Index does not contain separate price movements for each of the

electricity agencies. Therefore, the indexes supplied by the various electricity agencies were utilised.

Financial Indicators

Operating result

Unless otherwise stated, an above-the-line pre-tax profit. It consists of operating income (including investment income but excluding extraordinary items such as asset sales) less operating expenses (including interest but excluding corporate taxes and dividends).

Contribution to government

Contributions of the agency to the Consolidated Fund. Ideally, enterprises pay to the New South Wales Government the equivalent of corporate tax, plus a dividend, equal to a reasonable rate of return on capital (less earnings retained to meet endorsed enterprise objectives). The amounts should be separately identified, where appropriate.

Asset sales

Total revenue from the extraordinary sale of enterprise assets in the financial year.

Where asset sales are used to renew asset stock in the enterprise the overall rate of return on assets may be lifted. Proceeds from asset sales may also be used to retire external debt.

Return on (total) assets

Operating result before interest and tax as a percentage of total revalued assets. In some cases, historic cost valuations have been used (as footnoted). Return on assets is a fundamental indicator of performance in Government enterprises and enables economic comparisons between industries and sectors.

Return on operating (core) assets

Operating EBIT from core assets plus Government funded Social Programs, as a percentage of operating assets. This indicator measures the performance of the operating asset base.

Return on equity

Operating result before tax but after interest, as a percentage of equity. Equity is defined as total assets less total liabilities. Although an imperfect indicator for non-corporatised Government enterprises, return on equity measures the rate of return on public capital invested in an agency.

Gross external debt

The gross amount owed to parties' external to the agency, including that amount repayable to the Government of New South Wales.

Trends in external debt are an indicator of longer-term enterprise performance and future financial viability. A priority of the present New South Wales Government is the reduction of external debt.

Debt to equity ratio

Gross external debt as a percentage of equity. A declining ratio is generally desirable when interest rates are high or uncertain. A lower ratio indicates a higher rate of internal funding and less vulnerability to adverse interest rate movements.

Times interest earned

Earnings before interest and tax (EBIT) divided by the total interest expense measures gearing in the income stream, that is, the ability of the enterprise to meet its interest charges from its earnings.

Social programs

The value of New South Wales Government payments to the enterprise in return for meeting the provision of Social Programs. It is intended that all Social Programs be fully identified and financed in transfers between the State and the agency.

The elimination of implicit concessions assists in creating a level playing field for the agency in its industry and allows the agency to provide services in a commercial environment.

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Report by the Independent Committee of Inquiry on National Competition Policy (the 'Hilmer' Report).

Industry Commission (September 1997), *Assessing Australia's Productivity Performance* p. 84.

ibid p. 83.

ibid pp. 2-8.

ibid p. 25.

DEA can also be used for units operating in markets. DEA has been used to measure the technical efficiency of government businesses, in particular electricity distributors in New South Wales.

IPART (1997), pp. 1-5.

National Competition Council (1997), p. 33.

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