
3 Rationale for the schemes and approaches to their assessment

Key points

- The main rationale for the introduction of the MRA and TTMRA was to remove barriers to goods and labour mobility caused by cross-border differences in regulations. Removal of these impediments was expected to lead to a wide range of benefits, including greater consumer choice, lower business costs, and more efficient regulation.
- The first-round benefits of mutual recognition come from the initial reduction in firms' compliance costs and workers' accreditation expenses, and the increased consumption, output and employment thus promoted. In time, a range of other benefits may emerge, such as from increased 'regulatory competition' between jurisdictions.
- There are also costs associated with mutual recognition. For example:
 - some parties may be adversely affected (such as less efficient firms because of increased competition from other jurisdictions)
 - jurisdictions will have less scope to tailor regulations to reflect local conditions and preferences, standards might be undermined by 'jurisdictional shopping and hopping', joint decision-making procedures may make it slower and more difficult to implement regulatory reforms, and there could be increased government expenditure to administer mutual recognition arrangements.
- The Commission has been asked to assess the mutual recognition schemes for their coverage, efficiency and effectiveness. These terms are interpreted as follows:
 - coverage refers to which goods and occupations are subject to the schemes, as well as the nature of the regulations covered
 - effectiveness measures how well the mutual recognition schemes achieve their stated objectives
 - efficiency refers to how well resources are used to benefit community wellbeing, which includes the extent to which outputs are produced at the least possible cost.
- Key issues for this study are whether the mutual recognition schemes generate a net benefit for the community, and what reforms could make the net benefit larger.

This chapter provides a foundation for the analysis in subsequent chapters by outlining the rationale for the Mutual Recognition Agreement (MRA) and

Trans-Tasman Mutual Recognition Arrangement (TTMRA), and how the Commission has interpreted the assessment criteria in the terms of reference.

3.1 Rationale for the schemes

While similar in many respects, regulations in Australia and New Zealand often differ. Regulations also differ between jurisdictions within Australia, for historical reasons and because individual states (and territories) have the power under the Australian Constitution to regulate many areas independently.¹ The main rationale for introducing the MRA and TTMRA was to remove the barriers that such regulatory differences create for goods and labour mobility:

The principal aim of mutual recognition [within Australia] is to remove artificial barriers to interstate trade in goods and the mobility of labour caused by regulatory differences among Australian states and territories. (Free, R. (Minister for Science and Technology) 1992, Second Reading Speech, Mutual Recognition Bill, Australian House of Representatives, Hansard, 3 November, p. 2432)

The principal aim of mutual recognition [between Australia and New Zealand] is to remove impediments to trans-Tasman trade in goods and the mobility of labour caused by regulatory differences among Australian jurisdictions and New Zealand. (McGauran, P. (Minister for Science and Technology) 1996, Second Reading Speech, Trans-Tasman Mutual Recognition Bill, Australian House of Representatives, Hansard, 4 December, p. 7624)

[The TTMRA] provides a simple, low-cost and low-maintenance mechanism for overcoming unnecessary regulatory impediments to trade in goods and the movement of skilled practitioners between Australia and New Zealand. (MED 2007)

Regulatory differences have the potential to discourage goods and labour mobility by burdening firms and individuals with regulatory duplication and inconsistency when they venture beyond their home jurisdiction. The cost implications of regulatory differences, and their economic implications, have been extensively studied in the context of non-tariff barriers to international trade in goods. Such barriers, which are analogous to the barriers created by those interjurisdictional differences targeted by mutual recognition, have been shown to reduce the gains from trade between countries and, hence, the welfare of those countries' inhabitants (box 3.1).

¹ The territories' authority to legislate was granted by the Commonwealth under its constitutional powers.

Box 3.1 Economic effects of reducing non-tariff barriers to trade in goods

Trade in goods between different countries or jurisdictions can face both *tariff* and *non-tariff* barriers. Tariff barriers generally take the form of ad valorem or specific (that is, lump sum) taxes on goods crossing borders. Non-tariff barriers can be in the form of limits, or 'quotas', on the quantity of imports allowed into a country. They can also be in the form of national or local regulations acting as 'behind-the-border' barriers. International trade negotiations taking place since World War II under the auspices of the General Agreement on Tariffs and Trade and the World Trade Organisation have achieved substantial reductions in tariff barriers to trade between countries.

Similar progress has not occurred with respect to 'behind-the-border' barriers. These barriers comprise a range of technical, regulatory and administrative requirements which, singly or in combination, can serve to increase the price of imported goods. Non-tariff barriers can arise from regulation covering: sanitary and phytosanitary restrictions; testing and certification standards; labelling and packaging requirements; and food additive rules. Because they can impact disproportionately on local producers and foreign firms, these regulations can, at times, very effectively insulate domestic markets from foreign competition. While this is not the purpose of most regulation, the potential exists for disguised protection measures.

Given the diversity of non-tariff barriers, their measurement is difficult. A number of methods have been devised, such as counts of barriers, restrictiveness indexes, and analysis of international trade patterns or price gaps. Relying on the last approach, Bradford (2006) calculated that non-tariff barriers on imports of food for final consumption are high in most OECD countries. In the case of Australia, he estimated that such barriers added 20 per cent on average to the price of imported food, compared with 4 per cent on average for tariff barriers. Indeed, Bradford found that, along with Japan, Australia is the major OECD country where non-tariff barriers on final food imports are highest in proportion to total protection. He attributed these relatively high non-tariff barriers to 'overly strict quarantine laws'.

By introducing a wedge between lower world prices and higher domestic prices, non-tariff barriers have a detrimental effect on output, consumption and welfare, in both the protected country and its trade partners. Bradford estimated that multilateral removal of all non-tariff barriers by the eight major OECD countries he modelled would increase global GDP by 0.4 percentage points, or US\$90 billion in 1997 values. According to his modelling, Australia's GDP would rise by 0.06 percentage points if it unilaterally removed its non-tariff barriers on final food imports, and by 0.6 percentage points in the event of a multilateral removal of those barriers.

Source: Bradford (2006).

Governments in Australia and New Zealand concluded that the additional burden created by regulatory differences between and within their countries was largely unnecessary for controlling what goods could be sold and who could practise an occupation. This was because each jurisdiction's regulations generally met

community expectations, and those expectations did not differ markedly across the jurisdictions. Thus, the governments were prepared to mutually recognise compliance with each others' laws:

The underlying premise for mutual recognition [within Australia] is that the existing regulatory arrangements of each state or territory generally provide a satisfactory set of standards. Thus, on implementation of mutual recognition, no jurisdiction will be inundated with products that are inherently dangerous, unsafe or unhealthy, nor will there be an influx of inadequately qualified practitioners. (Free, R. (Minister for Science and Technology) 1992, Second Reading Speech, Mutual Recognition Bill, Australian House of Representatives, Hansard, 3 November, p. 2432)

The [TTMRA] scheme reflects the high degree of confidence which exists between Australia and New Zealand in respect of each other's regulations, regulatory systems and decision-making processes. (McGauran, P. (Minister for Science and Technology) 1996, Second Reading Speech, Trans-Tasman Mutual Recognition Bill, Australian House of Representatives, Hansard, 4 December, p. 7627)

The [TTMRA] illustrates the degree of maturity and trust that has developed in the relationship between New Zealand and Australia. (Luxton, J. (Minister for Commerce) 1997, Second Reading Speech, Trans-Tasman Mutual Recognition Bill, New Zealand Parliament, Hansard, 14 August, p. 3731)

If jurisdictions achieve the same outcomes despite having different regulations, then there could be a strong case on compliance and administrative cost grounds to rationalise those regulations into a uniform set of laws. However, Australia's experience prior to the MRA had been that regulatory uniformity was either unachievable or, if achievable, prohibitively slow to negotiate.

Historically, government, business and industry thought that uniform national regulation was the answer to ameliorating the barriers to free trade which were a product of the existence of multiple regulatory environments across the [Australian] states and territories. However, the Australian experience of uniform national regulation is that the process is either not achievable in the context of the existence of the independent sovereign states of Australia, or if achievable, prohibitively slow. (COAG 1998b)

In light of this experience, governments concluded that mutual recognition was more likely to deliver timely and widespread reductions in the burden associated with regulatory differences than were attempts to make regulations uniform across jurisdictions.

The version of mutual recognition adopted by Australia and New Zealand can be viewed as being towards the lower end of a spectrum in terms of its cost to negotiate, establish and maintain. Its establishment did not require jurisdictions to make significant changes to their standards or establish a centralised bureaucracy

for administration and enforcement.² It is particularly ‘light handed’ for goods, largely relying on case law for enforcement. Further up the spectrum is harmonisation, because it tends to be more difficult to negotiate and implement harmonised standards.³ The architects of the MRA and TTMRA anticipated that the schemes would encourage greater harmonisation in the longer term (COAG and New Zealand Government 1995; CRR 1991).

Uniformity is at the upper end of the spectrum because, as evidenced by Australia’s experience, it tends to be the most difficult to negotiate and implement. Nevertheless, there are cases where governments have concluded that uniformity would deliver the greatest net benefit to the community, as evidenced by recent Australian initiatives on national occupational licensing (chapter 5).

Another way of thinking about mutual recognition was outlined by Ergas (2008) at a recent conference on federalism (box 3.2).

Evidence used to support implementation of mutual recognition

Ideally, the case for mutual recognition would have been based on a comprehensive quantification of the unnecessary additional costs created by regulatory differences (and the net benefit from moving to mutual recognition). In practice, advocates of mutual recognition largely relied on the in-principle argument that regulatory differences create unnecessary burdens, supported by anecdotal evidence (COAG and New Zealand Government 1995; CRR 1991; Mumford 2004). While this standard may not be indicative of the broader picture, it does illustrate the potential significance and waste of unnecessary regulatory burdens. For example:

... manufacturers were often required to put different labels and use different packages for the same products. Each [Australian] state also had different design requirements for water meters. There were three different definitions of bread, Queensland bread

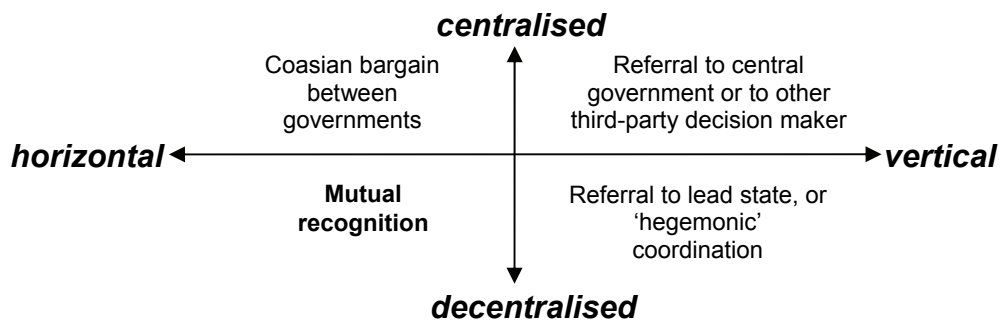
² One of the architects of the MRA, Roger Wilkins, contrasted this with the European Union’s approach to mutual recognition. He noted that the architects of the MRA ‘were familiar with the application of the [mutual recognition] concept in the ... European Union ... that ... involved an extensive bureaucratic administration and its effectiveness was dependent on the issuing of directives to ensure that minimum essential standards would apply. Those directives were subject to a variety of interpretations and required close monitoring and enforcement. We wanted a more straightforward, low maintenance approach in Australia, given the relative homogeneity of our states and territories’ (Wilkins 1995, pp. 3–4). The current European approach to mutual recognition is summarised in appendix C of this report.

³ When proposing the TTMRA, governments defined harmonisation as ‘the process whereby different standards or regulations in two or more jurisdictions are aligned. This does not mean that standards need to be identical in each jurisdiction, but rather that they are consistent or compatible to the extent that they do not result in barriers to trade.’ (COAG and New Zealand Government 1995, p. 5).

producers of half-sized loaves could not sell them into NSW, as their sale was prohibited in NSW. One state demanded that margarine be sold only in a package shaped like a cube ... (ORR 1997, p. 6)

Box 3.2 Approaches to regulatory cooperation in a federal system

At a recent conference on federalism, Ergas (2008) used the following diagram to outline four different approaches to regulatory cooperation in a federal system. The four options were characterised as lying in a two-dimensional space defined by the degree of centralisation and vertical/horizontal cooperation between different tiers of government.



Mutual recognition was described as being decentralised and largely involving cooperation between governments at the same tier. Ergas noted the following advantages and disadvantages of the four options he identified:

	<i>Coasian bargain</i>	<i>Referral to central government</i>	<i>Mutual recognition</i>	<i>Referral to lead state</i>
<i>Advantages</i>	Most effective when small number of roughly balanced units with two-way spillovers.	Most effective when spillovers are very large and widespread, but complex side payments are needed.	Allows consumers and producers to 'vote with their feet'.	Can reduce transaction costs (for example, avoid duplication of analysis).
<i>Disadvantages</i>	Invites 'hold-ups' and 'hold-outs', and induces strategic voting with inefficient outcomes.	Outcomes highly dependent on decision rule and can be inferior to no harmonisation.	Can create high transaction costs from multiple overlapping rules and concerns about race to the bottom.	Bias arising from restricted range of interests taken into account.

Comprehensive quantification of the problem created by regulatory differences (and its solution) would have been difficult because it had to be based on the *incremental* cost imposed by regulatory differences, netting out costs that would have occurred regardless. Unfortunately, financial record keeping by firms is not primarily set up to enable compliance costs to be disentangled in this way. Similarly, government accounts may not be well suited to identifying incremental administrative costs. Nor

is it always straightforward to measure the incremental burden individuals face.

The barriers to quantification were evident not only when the MRA and TTMRA were proposed, but also in subsequent evaluations of the schemes (COAG 1998b; ORR 1997; PC 2003). This was particularly apparent for goods, because mutual recognition operates in a more decentralised way for goods than it does for occupations. However, past evaluations do provide examples of where progress has been made in removing barriers to cross-border commerce. Most notably, the ORR (1997) identified specific improvements in the four years after the MRA was first applied, although these may not be entirely attributable to mutual recognition (table 3.1).

The 1998 review of the MRA used the ORR's analysis as its primary evidence to support continuation of the scheme for goods (CRR 1998). For occupations, the 1998 review cited general comments from professional associations indicating that it had become easier for registered practitioners in the medical, veterinary and legal professions to obtain registration in other jurisdictions. Occupation-registration bodies were quoted as having improved their communication with counterparts in other jurisdictions.

In the 2003 review of the MRA and TTMRA, the Commission noted that its assessment was constrained by a lack of data and problems in disentangling the effect of mutual recognition from other factors (PC 2003). However, anecdotal evidence indicated that there had been improvements since the previous review, most notably in resolving the issues underpinning special exemptions. The Commission reported that all consumer-product safety standards (except child restraints for cars) had been aligned, and that electromagnetic compatibility requirements had been harmonised, making it no longer necessary to have exemptions for those areas of regulation.

Table 3.1 Examples of improvements in the initial four years of the MRA

<i>Product</i>	<i>Relevant regulators</i>	<i>Trade barrier</i>	<i>Change from 1993 to 1997</i>
Bread	Various regulators	Different standard sizes	Non-standard sizes can be sold
Eggs	State/territory egg boards	Different grading and stamping requirements	Deregulation of the egg market continued
Dried fruits	State/territory dried fruit boards	Different grading requirements	Accelerated the negotiations for national standards
Abattoir meats	State/territory health departments or meat authorities	Some jurisdictions such as Queensland required a fee to be paid and/or permission from a regulator before meat could be sold	No longer need permission or have to pay a fee
Game meat	State/territory departments of health, meat authorities or equivalent	Interstate meat could not be sold. Production often banned within jurisdictions	These meats are now sold in NSW, Victoria and Queensland following agreement about uniform minimum standards. But production still banned in some states, such as NSW
Oysters	State/territory fisheries departments	In NSW, interstate oysters had to be soaked (deuration) for 36 hours before sale	This requirement has been dropped
Fruit and vegetables	Various regulators	Fruit and vegetables imported into Queensland had to meet grading and packing requirements before sale permitted	Queensland Act repealed in 1993
Pressure vessels	Various regulators, NSW Workcover Authority etc	State/territory regulatory authorities differed on the design, construction and testing of equipment	National standards developed and in process of being implemented through legislation in various state/territories
Packaging & labelling	Various regulators	Different requirements	National standards being developed
Consumer products	State/territory departments of consumer affairs or equivalent	Product bans	Cases where bans have been removed, such as repeal of NSW product safety regulation for safety footwear

Source: ORR (1997).

Anticipated impacts of the schemes

Those who proposed the MRA and TTMRA claimed that the mutual recognition schemes would deliver a wide range of benefits.⁴ Rather than simply listing these claims, it is instructive to outline the reasoning behind them. This can be done by considering how the schemes change the incentives faced by firms and workers. By reducing regulatory duplication and inconsistency affecting cross-border movements of goods and labour, the MRA and TTMRA will tend to:

- reduce the price that firms need to charge in order to cover the costs of selling a product into another jurisdiction
- lower the compensation that workers need in order to cover the costs of obtaining accreditation in another jurisdiction.⁵

Precisely how parties respond to this change in incentives depends on numerous factors — such as firms’ production technologies, workers’ willingness to move, and consumers’ preferences — but, in broad terms, it will trigger a series of effects that could improve the wellbeing of each jurisdiction’s community as a whole.

The first-round benefits will come from the initial reduction in firms’ compliance costs and workers’ accreditation expenses, and the greater consumption, output and employment this stimulates. This is illustrated in box 3.3 using a simplified model for goods. The actual distribution of benefits across different groups is undoubtedly more complex than represented in the model. Firms could profit by:

- retaining some of the reduction in compliance costs to increase profit per unit of existing output
- increasing sales volume by passing some of the fall in compliance costs on to consumers as lower prices, which may also generate greater economies of scale
- workers sharing with employers part of the decline in their cross-border accreditation costs.

Workers could gain by:

- retaining part of the savings from their lower accreditation costs
- increased employment as firms increase their sales volumes

⁴ The claimed benefits were outlined by CRR (1991) and COAG and New Zealand Government (1995) in discussion papers proposing the MRA and TTMRA, respectively.

⁵ The term accreditation means official recognition by an occupation-registration body that a person meets the requirements to practice an occupation. Employers may pay the cost of accrediting a worker in a new jurisdiction directly to the relevant occupation-registration body, and so the compensation required to cover this cost might not pass through the worker’s hands.

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- employers sharing part of the reduction in their compliance costs with employees as higher wages.

Consumers could benefit due to:

- lower prices on their initial level of consumption as firms and workers share part of the decline in their compliance/accreditation costs with consumers
- increased consumption (including deferred consumption in the form of savings) in response to lower prices and greater earnings from employment and the ownership of firms.

However, while the first-round impacts could make each jurisdiction's community as a whole better off, it does not follow that everyone will gain. One of the principal architects of the MRA — Gary Sturgess (1994), then Director General of the NSW Cabinet Office — argued that the main beneficiary, at least in the early stages, would be small firms, because they find it much harder to deal with cross-border differences in regulations.

Another notable distributional impact may be that less-efficient firms experience falling sales and prices in the face of increased competition from other jurisdictions (illustrated in box 3.3). This does not necessarily provide a case against mutual recognition, since the community as a whole would gain, but it may justify using some of the gains to foster structural adjustment (for example, through the retraining of unemployed workers).

In time, a range of other benefits may also emerge (box 3.4). These could involve ongoing structural reform and so might deliver more significant benefits in the longer term than do the first-round impacts (CRR 1991). Most notably, mutual recognition is likely to encourage greater 'regulatory competition' between jurisdictions to find ways of reducing compliance and accreditation costs while still meeting community expectations through regulation.

Mutual recognition is likely to encourage greater regulatory competition because it gives firms the opportunity to supply goods to multiple jurisdictions while only complying with the standards of the jurisdiction with the lowest compliance costs. Individuals may also stimulate regulatory competition because mutual recognition makes it easier for them to move to jurisdictions with lower accreditation costs.

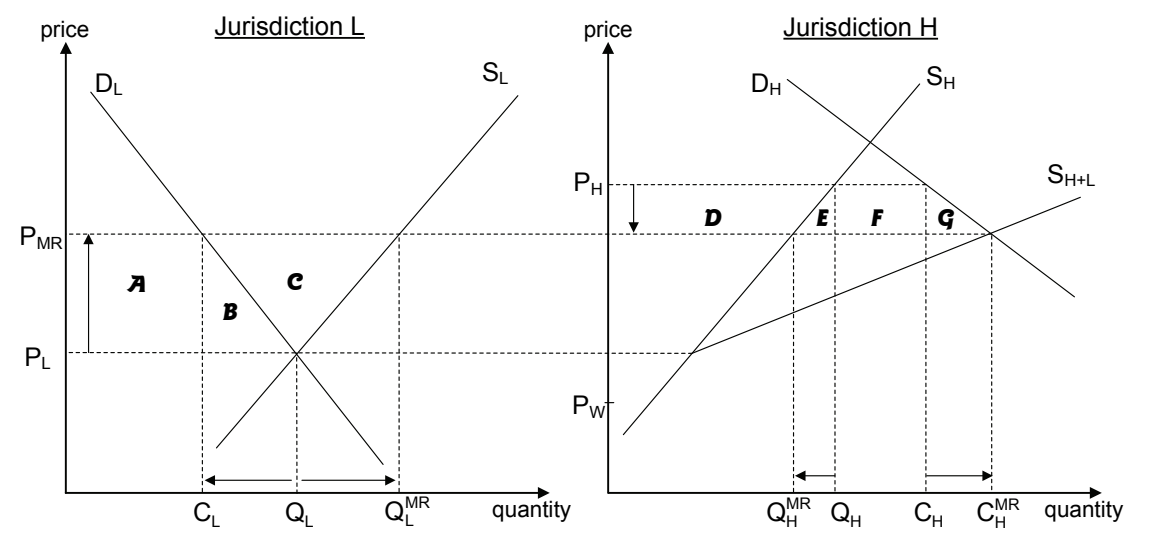
Box 3.3 First-round impacts of mutual recognition in goods markets

The first-round impacts of mutually recognising goods standards can be illustrated with a simplified partial-equilibrium model as shown below. It is assumed that the relevant good is identical regardless of who produces it, there are two jurisdictions — L and H — considering mutual recognition, and the rest of the world is willing to sell them the good for a constant per-unit return of P_W (small economy assumption).

If every jurisdiction had unique goods standards and this increased the cost of others exporting into its market, 'foreign' firms would need to set their export prices to recover this extra cost. For example, the rest of the world may need to charge P_H to get a net return of P_W (the world price) from exporting to jurisdiction H. Consumption in H would then be C_H , of which Q_H would be supplied by domestic firms, and the remainder ($C_H - Q_H$) imported from the rest of the world (based on where the P_H line intersects the demand and supply curves, D_H and S_H). If there was a similar regulatory barrier to the rest of the world exporting to jurisdiction L, that jurisdiction would neither import nor export the good, and all consumption would be met by the local output of Q_L at price P_L .

Suppose jurisdictions L and H mutually recognised each other's goods standards, so that there was no longer an additional cost in exporting to each other's markets. Jurisdiction L would then be able to export to H for a lower price than the rest of the world. This would change the supply curve in jurisdiction H to S_{H+L} , which would lead to the price in L and H converging towards P_{MR} . Consumers in H would increase their consumption to C_H^{MR} . Firms in L would export ($Q_L^{MR} - C_L$) to H (equal to H's imports of $C_H^{MR} - Q_H$).

Both jurisdictions would gain overall, but the distributional impacts would differ. In jurisdiction H, consumers would gain from a lower price and increased consumption (this gain would have a value equal to area **D+E+F+G**), but local firms would lose due to lower prices and output (area **D**). The net benefit in jurisdiction H would have a value equal to area **E+F+G**. Conversely, consumers in jurisdiction L would lose because they pay a higher price and consume less (loss of area **A+B**) but firms would achieve a higher price and output (gain of area **A+B+C**). As a result, there would be a net benefit in jurisdiction L equal to area **C**. In principle, the losers in each jurisdiction could be compensated by redistributing benefits so that no group is worse off.



Box 3.4 Longer-term benefits from mutual recognition

In addition to the first-round impacts of mutual recognition, a variety of other beneficial changes may emerge over time. They include:

- greater competition among firms that will increase ongoing pressure on them to find innovative ways to further reduce costs and prices, improve quality, and gain a competitive edge
- increased sales volumes due to lower prices and the contraction of less-efficient competitors that may enable firms to capture further economies of scale, with some of the resulting reduction in per-unit costs potentially being passed on to consumers as more price reductions and to workers as further wage increases
- more competition among workers that will provide added impetus for them to find ways to lift their productivity and improve the range and quality of services they provide
- lower barriers to cross-border movements of goods and labour that could enable consumers, workers and employers to enjoy greater choice and variety
- the abovementioned factors may also make economies more flexible and resilient to adverse shocks.

Advocates of the MRA and TTMRA have also noted that the mutual recognition schemes increase 'regulatory competition' between governments by giving firms and workers greater discretion over which jurisdiction's regulatory regime they comply with. Over time, this could deliver sizeable ongoing benefits to the community by creating:

- increased pressure on governments to find ways to reduce the compliance and accreditation costs associated with meeting community expectations through regulation (this effect could be significant because it may affect regulations that also apply to goods and workers that do not cross borders)
- increased discipline on jurisdictions contemplating new regulations to ensure there would be a net benefit to the community
- improved cooperation and dialogue between regulators across jurisdictions.

Sources: Carroll (2006); COAG and New Zealand Government (1995, 2006); CRR (1991); Sturgess (1993, 1994).

One of the anticipated benefits of regulatory competition was that it would create greater impetus to harmonise regulations where there were genuine concerns about mutually recognising different jurisdictions' standards. However, harmonisation may also be sought for less worthy motives. It could enable governments to avoid the pressure of regulatory competition, extend overly onerous and costly (gold-plated) regulations to all jurisdictions through a 'race to the top', and reduce the scope for policy innovation. This provides a potential rationale for maintaining mutual recognition over the longer term, rather than regarding it as an interim step on the path to uniform regulations across all jurisdictions.

While there are likely to be benefits from mutual recognition, there are also costs to consider. For example:

- jurisdictions will have less scope to tailor regulations to reflect local conditions and preferences, particularly if it would increase compliance/accreditation costs beyond those of other jurisdictions
- firms and workers may have an incentive to engage in jurisdiction ‘shopping and hopping’ — the practice of using the jurisdiction with the easiest or cheapest standards to enter markets in other jurisdictions — that reduces the quality and/or safety of goods and services supplied. To some extent, this risk was addressed in the design of the mutual recognition schemes⁶
- joint decision-making procedures associated with the mutual recognition schemes could make it slower and more difficult to implement regulatory reforms within a given jurisdiction
- in order to benefit from mutual recognition, firms and workers will have to incur the cost of becoming informed about the relevant procedures, and complying with them
- governments will incur additional administration costs, such as to fund coordinating bodies, and to cover the costs of employing officials for the purpose of implementing mutual recognition procedures and attending intergovernmental meetings
- regulators may not implement mutual recognition arrangements appropriately.

An assessment of mutual recognition, therefore, needs to weigh up not only the benefits, but also the associated costs. This issue is discussed further below in the context of assessing efficiency, but it should be noted that some of the abovementioned costs — such as the additional administration costs for governments and information costs for individuals — are likely to be relatively small.

⁶ When designing the MRA, governments sought to prevent a ‘race to the bottom’ in goods standards by allowing individual jurisdictions to temporarily exempt products from mutual recognition for up to 12 months, and gave Ministerial Councils the authority to make such exemptions permanent by a two-thirds majority vote, thus preventing a ‘rogue’ jurisdiction from undermining standards (Sturgess 1993, 1994). Similarly, one jurisdiction can refer concerns about occupational standards in another to a Ministerial Council for a determination based on a two-thirds majority vote (COAG and New Zealand Government 2006).

3.2 Interpretation and application of assessment criteria

The terms of reference for this study require the mutual recognition schemes to be assessed for their coverage, efficiency and effectiveness. The Commission's interpretation and application of these criteria are outlined below.

Coverage

The word 'coverage' is interpreted as referring, strictly speaking, to the question of what goods and occupations are subject to mutual recognition. But it is also interpreted as meaning the broad 'scope' of the two schemes — the range of laws, regulations and activities that are within reach of mutual recognition.

As noted in chapter 2, the mutual recognition schemes cover most occupations for which some form of legislation-based registration is required. In contrast, there is an extensive system of exemptions for goods, involving three separate types — permanent, temporary and special exemptions. In addition, the categories of exceptions and exclusions ensure that certain laws — including in relation to how goods are sold and occupations are practised — are not subject to mutual recognition.

The Commission's 2003 review examined the coverage of the MRA and TTMRA, and in most cases concluded that existing arrangements were largely appropriate. However, a number of changes were suggested, and it was noted that others may be warranted, depending on post-2003 developments. Thus, it is timely for this study to revisit the issue of coverage. This is done by considering whether potential changes to coverage would improve the effectiveness and efficiency of the schemes, including in areas already subject to mutual recognition.

Effectiveness

Effectiveness measures how well the mutual recognition schemes achieve their stated objectives. As noted previously, governments stated that their principal aim was to remove impediments to cross-border goods and labour mobility caused by regulatory differences. This was expected to lead to the wide range of benefits mentioned above, such as greater consumer choice, lower business costs, and more efficient regulation.

A key basis for judging effectiveness is, therefore, the extent to which goods and workers cross borders without being burdened with regulatory duplication and

inconsistency. In some cases, this is relatively straightforward to observe directly. For example, the records of occupation-registration bodies could be used to measure the share of workers from other jurisdictions who register under mutual recognition, and so avoid regulatory duplication and inconsistency. However, such detailed records are unlikely to exist in the goods area.

Various indirect indicators are also used in this study because it is often difficult to directly observe the extent of the incremental regulatory burden from crossing borders. In this regard, the mutual recognition schemes are judged to be more effective, the greater the extent to which:

- regulators comply with their obligations under the mutual recognition schemes
- firms and workers are aware of, and able to assert, their rights under the schemes (including through appeals mechanisms)
- there are no design flaws in the mutual recognition schemes (such as ambiguous legislative wording) that could unintentionally allow regulatory duplication and inconsistency to persist.

Another basis for judging effectiveness is the extent to which the expected benefits of mutual recognition are realised. Relevant indicators include changes in:

- cross-border movements of goods and labour
- interjurisdictional competition among firms, and associated reductions in business costs and prices, and gains in product quality and innovation
- level of consumer choice
- the prevalence of inappropriate or overly costly regulations
- cross-jurisdiction cooperation and dialogue among regulators.

In examining such indicators, it is important to isolate the impact of mutual recognition from changes caused by other factors. This study is concerned with the *incremental* impact of the MRA and TTMRA, above what would have occurred regardless of the schemes' existence.

Efficiency

Efficiency, in its broadest sense, refers to how well resources are used to benefit the wellbeing of the community as a whole. This broad interpretation is known as 'economic efficiency' and has three components — the degree to which outputs are produced at least possible cost, resources are allocated to uses that generate the greatest community wellbeing at a given point in time, and over time (box 3.5).

Box 3.5 **Components of economic efficiency**

Economic efficiency is about maximising the wellbeing of the community. It requires satisfaction of three components.

Productive efficiency is achieved when output is produced at minimum cost. It includes technical efficiency, which refers to the extent to which, in the production of any good or service, it is technically feasible to reduce any input without decreasing the output, and without increasing any other input.

Allocative efficiency is about ensuring that the community gets the greatest return (very broadly defined) from its scarce resources. A nation's resources can be used in many different ways. The best or 'most efficient' allocation of resources is the one that contributes most to community wellbeing.

Dynamic efficiency refers to the allocation of resources over time, including allocations designed to improve economic efficiency and to generate more resources. This can mean finding better products and better ways of producing goods and services, which may involve investments in education, research, development and innovation. Dynamic efficiency can also refer to the ability to adapt efficiently to changed economic conditions, a capacity for optimally modifying output and productivity performance in the face of economic 'shocks'.

For the purpose of this study, the community is defined to comprise both Australia and New Zealand. Thus, efficiency is assessed collectively for the Australian jurisdictions and New Zealand, while noting differences in the impacts on, and the preferences and interests of, individual jurisdictions.

The MRA and TTMRA have the potential to improve efficiency (and hence community wellbeing) by:

- reducing the resources needed to meet community expectations through regulation (by cutting the waste of unnecessary regulatory duplication and inconsistency and, in the longer term, by fostering best-practice regulation)
- encouraging goods and labour to be allocated to uses more highly valued by the community (by lowering regulatory barriers to goods and labour mobility).

This potential will only be realised if the benefits the community derives from the mutual recognition schemes outweigh the associated costs. As noted previously, the costs of mutual recognition include a loss of autonomy that limits jurisdictions' capacity to tailor regulations to reflect local conditions and preferences, joint decision-making procedures that may make it slower and more difficult to implement regulatory reforms within a given jurisdiction, and the added expenditure to fund coordination bodies and personnel.

Some of the benefits and costs cannot be readily quantified because there is no associated market with observable prices, or the beneficiaries or losers are diffuse. For example, it is difficult to put a financial value on the loss of regulatory autonomy associated with mutual recognition. Therefore, the quantitative analysis in this study is supported by a qualitative assessment of some aspects of the schemes. For example, the Commission notes there has been long-standing community and political support in Australia and New Zealand for initiatives that integrate their economies, even in cases where this has involved some loss of autonomy.

The terms of reference for this study direct the Commission to not only assess the overall efficiency of the MRA and TTMRA, but also to consider how administrative provisions can be changed to support more efficient operation of the schemes. The annual rollover of TTMRA special exemptions is mentioned as an example. This is considered in chapter 7 as part of the analysis of special exemptions. Potential efficiency improvements to other administrative provisions are considered throughout the report, including for occupation registration in chapter 5, temporary goods exemptions in chapter 6, and governance in chapter 11.