



PC update

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Australian Government
Productivity Commission

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The Productivity Commission is the Australian Government's independent research and advisory body on a range of economic, social and environmental issues affecting the welfare of Australians.

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Strengthening evidence-based policy in the Australian federation

Much emphasis is currently placed on the importance of a sound evidence base in policy formulation. A recent Productivity Commission roundtable discussed how evidence-based policy is implemented in Australia, and how it might be done better.

What role does evidence play in policy making? How can the availability and quality of evidence be improved to shape better policies? What institutional frameworks and government processes best support an evidence-based approach? These issues were the subject of a Productivity Commission roundtable 'Strengthening evidence-based policy in the Australian federation' held in Canberra in August 2009. Keynote addresses to the roundtable were presented by Professor Jeffrey Smith from the University of Michigan and Dr Ron Haskins, Senior Fellow at the Brookings Institution. The full proceedings will be published in early 2010.

What role does evidence play?

In his address to the roundtable, Professor Brian Head (University of Queensland) identified three enabling factors that drive evidence-based policy: good data, high-level analytical skills, and political support. However, he observed that even when government is able to draw on reliable information and sound analytical skills, 'the politics of decision-making inherently involves a mixing of scientific evidence, value preferences, and practical judgments about feasibility and legitimacy'.

"Evidence and analysis should play an important role in policy making ... but the *realpolitik* of public policy involves a much richer array of influences", Gary Banks.

Drawing on his experience with the United States Congress, Ron Haskins observed that the prime influences on most policy formulation were inertia (vested interests wishing to maintaining the status quo), the entrenched ideological viewpoints of the major political parties (with research evidence having little chance of changing decisions) and, perhaps most significantly in the United States, the personal views and political strength of individual politicians of influence in Congressional committees.

Nevertheless, several speakers emphasised that evidence can, at times, play an important role in policy development. Haskins described how evidence of the perverse

effects of the existing welfare programs, and the compelling and comprehensively better results under 'workfare', were decisive in winning US Congressional support for the Clinton administration's 1996 welfare reform legislation. Professor Bruce Chapman (Australian National University) explained how, in Australia, statistical evidence – and the timely coalescence of a network of like-minded policy advisers – were influential in motivating the introduction of the Higher Education Contribution Scheme and the Working Nation reform package. Peter Dawkins (Victorian Department of Education and Early Childhood Development), outlined how robust analysis and drawing on the available strong evidence base about the potential impact of human capital on participation, productivity and economic growth shaped the development of the human capital reform agenda, a central focus of COAG's National Reform Agenda.

Enhancing an evidence-based approach to policy

Roundtable participants generally agreed that a number of measures could increase the role that evidence and evaluation could play in policy formulation, including:

- ensuring adequate framing of the policy problem, including whether government intervention is the most effective response
- improving data collection and analytical capacity within both government and non-government organisations
- increasing the independence, transparency and accessibility of evidence ▶



Is there a 'gold standard' in evidence?

In suitable cases, randomised controlled trials (RCTs) provide the most reliable method of evaluating program effectiveness. Prof Andrew Leigh (Australian National University) argued that RCTs 'are an underused tool in the policy drawer' in Australia, and reticence among policy makers to subject policy interventions to such evaluation should be overcome.

Professor Jeffrey Smith encouraged the use of evidence in policy formulation, but warned that evaluation methodologies – including RCTs – have significant limitations. Results must be interpreted thoughtfully; average results can mask important differential impacts on different groups; and spill-overs and scaling issues in moving from a small trial group to the broader economy need careful enumeration. Smith stressed that the quality of the data was as important as the methodology.

RCTs are not always appropriate or feasible, and other quantitative and qualitative analysis can also be important. Grant Scobie (New Zealand Treasury) and other participants noted that local evidence could only play a minor role in many significant policy questions, such as major institutional reforms and for interventions with economy-wide effects, such as industry assistance and macroeconomic policy. International experience and theoretical analysis was often valuable in such cases. There was general agreement that different kinds of evidence are useful in different circumstances, and often multiple forms and sources of evidence may be desirable.

- recognising the value of multiple sources of evidence and advice, and improving the link between policy makers and the research community
- learning from policy failures, as well as from evidence about 'what works'.

Evidence alone is not enough

Professor Patricia Rogers (RMIT) argued that several types of evidence are needed, including assessments of communities' and participants' needs and strengths, and information on the nature and extent of service delivery. She said that improving the quality of evidence about effectiveness is not a matter of using a particular methodology, but about systematically checking its internal and external validity, including paying attention to differential effects of interventions on different groups and in different situations.

“There is no such thing as *the* effect of a policy – treatment effects are heterogeneous ... and outcomes will vary with the features of the treated units and the policy and economic environments ... Experiments are no substitute for thinking”,
Prof Jeffrey Smith.

Robert Griew (Department of Education, Employment and Workplace Relations) emphasised that a substantial evidence base alone does not guarantee good policy:

It is not enough to assert the importance of evidence, as if the nature of evidence itself is unproblematic. It is also important to be clear about whose evidence, what evidence and evidence for what purpose? We need to know not only what works, but how it works and why.

Griew argued that strong evidence will not redeem policies that are poorly integrated with the context of the communities they are developed to serve. Building close relationships with practitioners, in both policy formulation and evaluation, is also required.

Institutions matter

In his introduction to the roundtable, Productivity Commission Chairman Gary Banks noted:

“For evidence and evaluation to contribute materially to the selection of policies, it must be supported by institutional frameworks that embed the use of evidence and encourage, disseminate and defend good evaluation ... The institutional framework should also ensure that the resources allocated to evaluation are commensurate with the potential benefits.”

Mary Ann O'Loughlin (COAG Reform Council) argued that an evidence-based approach is at the heart of the COAG Reform Agenda, which covers a broad suite of

Improving evaluation of major projects

In his presentation to the roundtable, Henry Ergas expressed concerns about the extent and quality of project evaluation in Australia. 'Very significant increases have occurred in public infrastructure investment in recent years, involving projects worth billions of dollars of taxpayers' money, yet little attention has been paid to the systematic evaluation of the costs and benefits of these projects', he said. 'If the benefits do not outweigh the costs, capital productivity will decline, and living standards will fall over the longer term. Although there is a long history of use of cost-benefit analysis (CBA), emphasis is currently placed on other, less rigorous, approaches to project evaluation.'

Ergas argued for the following three reforms to improve project evaluation processes:

- increased transparency – including public disclosure for all CBAs
- enhanced auditing – including independent review of all CBAs for 'mega projects' and improved post-completion review of projects
- improved CBA techniques – many complex technical issues are still to be resolved.

reforms in education, health, competition and regulation, environment and Indigenous reform.

The COAG Reform Council will monitor, assess and report on the performance of all governments in achieving the outcomes and benchmarks specified under the National Agreements and National Partnerships. O'Loughlin said such an outcomes-focused, evidence-based approach provides strong incentives for reform by highlighting and rewarding good practice and encouraging responsibility for addressing relatively poor performance.

An 'evaluation club'?

The need for institutional arrangements to promote reliable funding and dissemination of rigorous evidence was strongly endorsed by roundtable participants. Jeffrey Smith described the effectiveness of the Institute of Education Sciences in the US Department of Education in transforming the quality of education research, including through its What Works Clearinghouse, which provides access to, and assessment of, evidence on the effectiveness of policy interventions in the education sector.

Ron Haskins and other speakers noted the emergence of groups devoted in part to earmarking funding for rigorous evaluation as part of the legislation initiating new policies, such as the US Coalition for Evidence-Based Policy; and of 'evaluation clubs' in which quality evaluations could be selected and funded, and results disseminated and pooled, such as the International Initiative for Impact Evaluation.

In a case study of another effective institution for the dissemination and evaluation of available evidence, Professor Sally Green (Australasian Cochrane Centre) described how the Cochrane Collaboration prepares and disseminates systematic reviews of research evidence in the health-care services.

A number of participants suggested that Australian governments could play a stronger collaborative role in promoting, funding, improving and using data collection and evaluations across jurisdictions, including the possibility of a COAG-led 'evaluation club'.

Concluding comments

In summing up the roundtable proceedings, Professor Jonathan Pincus (University of Adelaide) stressed that value judgements are required about policy objectives, independent of any evidence of 'what works'. 'Slavery was abolished because it was immoral, not because it didn't work', he noted. He identified three steps in the policy formulation process: determining which objectives are worth pursuing; identifying what policies work towards those objectives, and for whom; and deciding which policies actually get implemented.

Participants concluded that the roundtable had usefully focussed attention on practical methodological and institutional improvements that might help to strengthen the use of evidence to shape better policies – including those designed to solve 'wicked' (large scale, complex and seemingly intractable) policy problems. ■

Strengthening Evidence-based Policy in the Australian Federation

- > Productivity Commission Policy Roundtable 2009
- > Opening address by Gary Banks and presentations by Dr Ron Haskins and Prof Jeffrey Smith are available on the Commission's website.
- > Full proceedings will be published in early 2010.

Are we overcoming Indigenous disadvantage?

Only limited progress has been made in bridging the gulf in circumstances between Indigenous and other Australians, said Commission Chairman Gary Banks in a presentation marking the release of the 2009 *Overcoming Indigenous Disadvantage* report. Edited highlights of his comments follow.

It is now seven years since governments made a commitment to work together in new ways to tackle the root causes of Indigenous disadvantage. In an important break with the past, in 2002 COAG requested the Steering Committee for the Review of Government Services to prepare a regular report to monitor national Indigenous outcomes. My expectation when presenting the first *Overcoming Indigenous Disadvantage* (OID) report in 2003, was that many of the disparities evident at that time would have narrowed by now. Six years and three reports later, improvement has been clearly achieved for only about 20 per cent of the indicators. For 10 per cent of the indicators, things have actually got worse.

There are a number of caveats however. Perhaps, most importantly, for half the indicators in the report the data are still not good enough for us to *know* whether there has been any progress. (If we look at the extent of progress among only those indicators for which trend data are available, the 'improvement' ratio doubles to 40 per cent). In addition, much of the data only go to 2006, and therefore cannot shed light on more recent outcomes.

Role of the report

The OID report is structured around a strategic framework of outcome indicators, based on a preventative model. The framework contains high-level goals and related indicators, and a second tier of indicators in 'strategic areas' – policy areas where action is needed if the high level indicators are to be achieved.

“Disadvantage has multiple dimensions and multiple causes, many of which interact. For example, educational outcomes for Indigenous children depend not only on the effectiveness of schooling services, but also on students’ health and, importantly, the circumstances of their homes and communities”, Gary Banks.

The reporting framework for the 2009 report has been amended to include the six COAG 'closing the gap' targets, and the lower tier has been modified to align it more closely with the COAG Working Group on Indigenous Reform 'building blocks'. While some extra indicators have been added, none have been lost.

What progress at the 'headline' level?

The report, like its predecessors, reveals wide gaps in outcomes between Indigenous and other Australians across virtually all indicators. In many areas, there has been little or no improvement over time. For some indicators – notably in economic areas – outcomes for both Indigenous and non-Indigenous people have improved, suggesting that progress can be achieved more widely.

In relation to the six COAG targets, the story is mixed:

- *Life expectancy* – the latest estimates indicate that the gap between Indigenous and non-Indigenous life expectancy at birth was 12 years for males and 10 years for females. While significantly lower than previous estimates, this is still unacceptably large, and does not necessarily imply an actual improvement. There are no



Photo courtesy of Reconciliation Australia and Wayne Quilliam (Indigenous Governance Awards 2008)

Overcoming Indigenous Disadvantage: Reporting Framework

1. Priority outcomes



2. COAG targets and headline indicators

COAG targets	Headline indicators
<ul style="list-style-type: none"> • Life expectancy • Young child mortality • Early childhood education • Reading, writing and numeracy • Year 12 attainment • Employment 	<ul style="list-style-type: none"> • Post secondary education — participation and attainment • Disability and chronic disease • Household and individual income • Substantiated child abuse and neglect • Family and community violence • Imprisonment and juvenile detention

3. Strategic areas for action



trend data for life expectancy except for the Northern Territory, where the gap in life expectancy increased slightly for males and decreased for females over the period 1967 to 2004.

- *Young child mortality* – Indigenous infant mortality rates have improved in recent years, while child mortality rates have been largely unchanged. Mortality rates for Indigenous infants and young children remain two to three times higher than for all infants and young children.
- *Early childhood education* – there are limited data on Indigenous preschool participation, and it is difficult to draw any conclusions about participation rates.
- *Reading, writing and numeracy* – there has been negligible change in Indigenous students' performance over the past ten years. Gaps between Indigenous and non-Indigenous students have not narrowed and increase with remoteness and at higher year levels.
- *Year 12 attainment* – the proportion of Indigenous 19-year-olds completing year 12 or equivalent has increased, but the non-Indigenous rate has also increased, leaving the gap unchanged.

- *Employment* – the employment-to-population ratio for Indigenous people has increased. However, a similar increase for the rest of the population left the gap unchanged.

Things that work

Not everything that matters can be captured in indicators. The OID report includes many examples of 'things that work' – activities and programs that are making a difference, often at the community level. These usually have four common elements:

- cooperative approaches between Indigenous people and government, often also involving the non-profit and private sectors
- community involvement in program design and decision-making – a 'bottom-up' contribution, rather than just relying on 'top-down' direction
- ongoing government support – human, financial and physical
- good governance – in Indigenous communities and organisations, and within government itself. ▶



Photo courtesy of Reconciliation Australia and Wayne Quilliam (Indigenous Governance Awards 2008)

The policy challenge

At the broadest level, there are two challenges for government in overcoming Indigenous disadvantage. The first is developing and implementing effective policies and programs. The second is generating the information needed to assess whether policies are working and how much progress has been achieved. The two challenges are closely related: good policy development depends on good information.

Despite considerable advances over the past seven years, there are no trend data for about half of the 50 indicators in the OID report. Moreover, the data for many indicators do not support reliable comparisons across jurisdictions or geographic areas. Better data on outcomes for Indigenous people in remote regions relative to urban centres is particularly important.

While the outcome indicators in the report provide important information, for policy-making purposes there is no substitute for detailed evidence-based assessments and reviews of specific programs. In an important development, COAG has agreed to establish a national clearing house on best practice and success factors in Indigenous service delivery. It is designed to provide a central repository of rigorously assessed evidence, giving governments and the wider community ready access to quality information about 'what works'. It is also intended to improve the coordination of research and identify future research and evaluation priorities.

If the clearing house lives up to this promise, it could be a very powerful tool for policy learning. However, it will be useful only to the extent that governments get serious about generating relevant data, undertaking rigorous evaluations, and sharing the results.

Things that work – some examples

The **Yappera Centre** in suburban Melbourne, funded by the Australian Government since 1998, assists Koori families to participate in childcare and kindergarten. The Committee members are all Koori and the Centre is linked to organisations providing additional services such as speech therapy, parent/carer programs and health services.

Deadly Vibe, a magazine for Indigenous students published by Vibe Australia (an Aboriginal media agency) with funding from the Australian Government, encourages Indigenous students to stay at school. The magazine, targeted at school-aged children, promotes healthy lifestyle messages through articles focusing on the achievements of Indigenous people in sport, music, the arts and education.

The **Cape York Family Income Management project** was designed by Indigenous people to build financial literacy, stabilise family functioning, and reduce household and individual debt in a culturally sensitive way. The project is run by local people and overseen by representatives from each community, Australian Government agencies, Westpac, and Cape York Partnerships. Outcomes include debt reduction, increased spending on food and reduced spending on alcohol

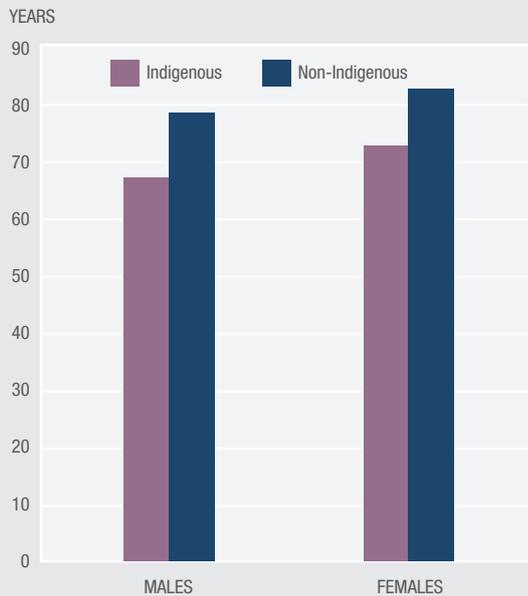
and gambling, better access to medication, and reduction in stress and conflict.

The **Murri Court** is a Queensland Magistrates Court that sentences Indigenous offenders pleading guilty to an offence. The court takes into account cultural factors by providing a forum where Indigenous elders have input into the sentencing process and provide insight into the impacts of offending on the local community. The legal processes of the Murri Court are more informal and, where possible, sentences have a rehabilitative focus.

The **Clontarf Foundation Program**, set up in three Alice Springs schools, provides teenage Indigenous boys with quality football coaching, specialist physical conditioning, health education and mentoring in life skills, linked to attendance and performance at school. To remain in the program, participants must attend school regularly; apply themselves to study, and meet the academy's requirements for behaviour and self discipline. After the introduction of the program, average attendance rates for the Alice Springs schools increased from 70 per cent in 2007 to 87 per cent in 2008.

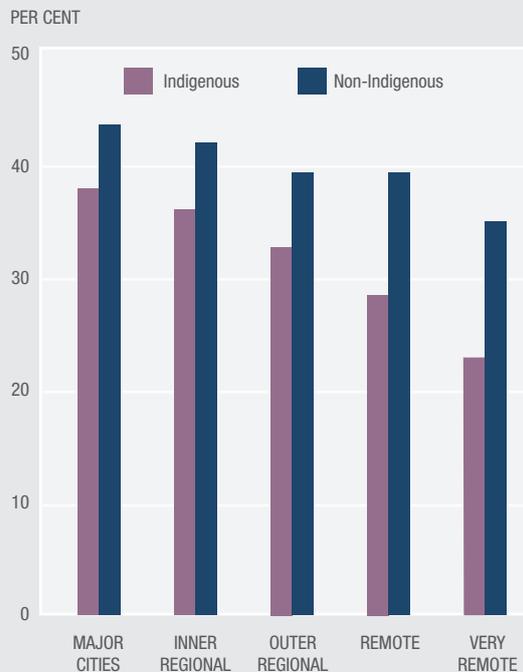
Source: *Overcoming Indigenous Disadvantage Key Indicators 2009*

Figure 1: Life expectancy at birth, Australia, 2005-07



Source: Figure 1: *Overcoming Indigenous Disadvantage Key Indicators 2009*, figure 4.1.1

Figure 2: Preschool participation rates, children aged 3-5 years, Australia, 2006



Source: Figure 2: *Overcoming Indigenous Disadvantage Key Indicators 2009*, figure 4.3.1

“The most important determinant of a school’s performance is the calibre of its leadership and the quality of its teaching ... The most difficult schools and students within the public system should at least be receiving a fair share of the more able teachers. But this is obviously not the way the system currently works.” Gary Banks.

Edited highlights of a speech by Gary Banks AO, presented as the third lecture in Reconciliation Australia’s ‘Closing the Gap Conversations’, Canberra, 7 July 2009. ■

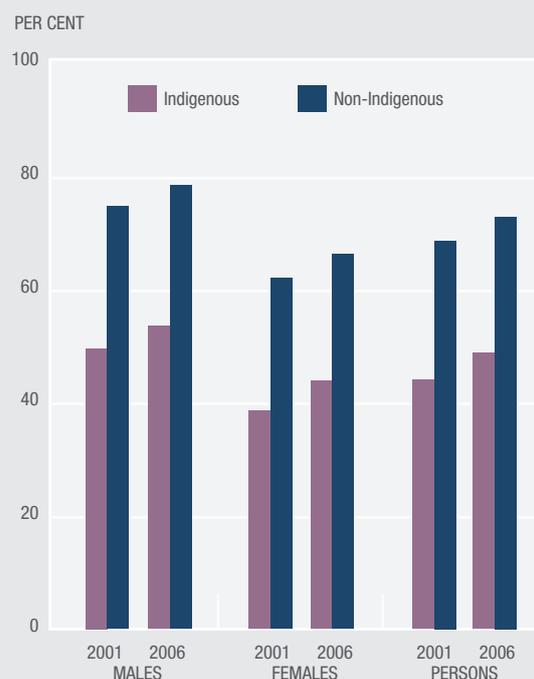
Overcoming Indigenous Disadvantage Key Indicators 2009

> Published by the Steering Committee for the Review of Government Services, chaired by Gary Banks.

> The Productivity Commission provides the Secretariat for the Steering Committee.

> www.pc.gov.au/gsp/reports/indigenous

Figure 3: Employment to population ratio, Australia, 2001 and 2006



Source: Figure 3: *Overcoming Indigenous Disadvantage Key Indicators 2009*, figure 4.6.1

Executive remuneration

The Commission's discussion draft on executive remuneration proposes a 'package' of regulatory and corporate governance reforms that would enhance the effectiveness and credibility of boards in setting executive pay.

The Productivity Commission has been asked to undertake an inquiry into the regulatory framework governing executive remuneration in publicly listed companies in Australia. The catalyst for the inquiry was community concern about strong growth in executive remuneration and some well-publicised examples of large termination payments, despite poor company performance. After wide consultations and public hearings, the Commission released a discussion draft in September. Consultations on the draft, and further public hearings, will be undertaken prior to completion of the Commission's final report to Government at the end of the year. On releasing the discussion draft, Commission Chairman Gary Banks said: 'The way forward is not to by-pass the central role of boards by capping pay. Rather, regulatory and corporate governance reforms are needed to strengthen the integrity of pay-setting by boards and enhance shareholder engagement.'

Some facts

Executive remuneration has grown strongly since the early 1990s. Executive pay for larger companies appears to have grown fastest from the mid-1990s to 2000, and increased by more than another 50 per cent to 2007. Remuneration fell in 2007-08, but it is unclear yet whether this decline has continued. Virtually all recent growth has come from performance ('incentive') pay.

Executive pay varies greatly across Australia's 2000 public companies. For the top 20 CEOs, it averages almost \$10 million compared to less than \$200 000 for CEOs of the smallest companies. And the ratios with average earnings range from 150 to 3.

Remuneration levels vary significantly across industries, being highest in the finance, telecommunications and consumer sectors, and lowest in the information technology and utility sectors.

A major reason for rapid growth in executive pay has been the greatly increased scale of Australian companies in a more dynamic and global environment, which has raised the importance of having the most highly-talented executives. (Increased company size explains almost one third of the increase in executive pay.) The shift to incentive pay has also increased total remuneration because of the 'risk premium' it entails. However, a further contributor in some periods and for some companies, has been failure to properly design incentive-pay arrangements and instances of board weakness in resisting substantial termination payments.

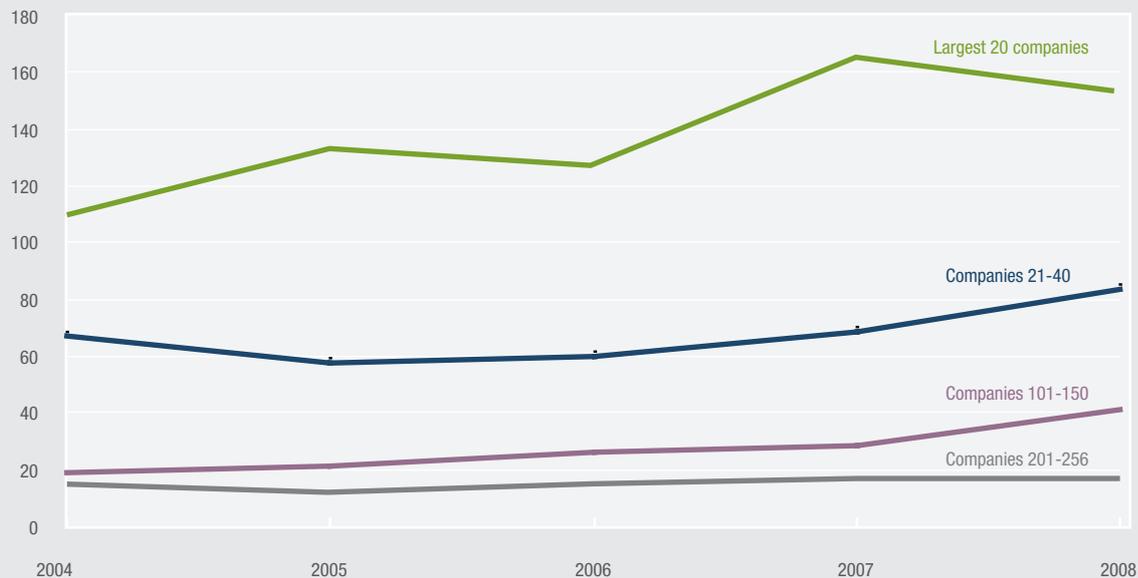
Strong corporate governance is the key

Instances of excessive payments and perceived inappropriate behaviour can reduce public confidence in the corporate sector and impact on equity markets. Having examined a number of alternative measures proposed by inquiry participants, the Commission is convinced that the way forward is not to by-pass the central role of boards in remuneration setting through prescriptive regulatory measures such as pay caps. And a binding shareholder vote on the remuneration report, though supported by many, would be unworkable given the report's complexity and coverage, and would compromise the board's authority to negotiate with executives. However, the Commission found a strong case for making changes to corporate governance that



Earnings multiples vary with company size

RATIO OF CEO REMUNERATION TO AVERAGE EARNINGS



Riskier pay requires a risk premium

Incentive pay can promote alignment of managerial and shareholder interests. However, from the perspective of executives it:

- introduces uncertainty about the level of remuneration eventually received (because performance hurdles are not trivial or are susceptible to forces outside their control)
- can constrain their ability to diversify their wealth, exposing them to portfolio risk
- usually involves deferment of pay (and thus losses from delaying access to it).

Thus, executives will require a 'risk premium' compared to a fixed cash salary and will discount deferred pay.

would enhance the effectiveness and credibility of boards, taking into account the need to minimise potential costs and the scope for unintended consequences.

The Commission is proposing and seeking comment on a number of reforms aimed at minimising the scope for conflicts of interest in remuneration setting and to strengthen board accountability more generally (see page 12). Many of these complement reforms proposed by the Australian Prudential Regulation Authority for the financial sector, but with wider application.

The role of boards and the 'principal-agent problem'

The diverse shareholdings in public companies necessitates separation of ownership from management of the company. Employing specialist managers can bring large benefits, but there is the potential for them to pursue their own objectives rather than those of the company and its shareholders. This is the 'principal-agent problem'. The primary mechanism for ensuring managers act in the company's (and therefore shareholders' interests) is shareholders electing boards to monitor performance and oversee company direction on their behalf.

The Commission considers that, collectively, these changes would strengthen corporate governance and alignment of interests — giving shareholders better information and more 'say' on pay. In doing so, they should reduce the likelihood of remuneration outcomes in the future that shareholders would find objectionable, and help secure greater confidence in the corporate sector within the wider community. However, there will be compliance costs as well as more subtle behavioural consequences. To 'stress test' its proposed reforms and ensure that the right balance can be achieved, the Commission will be consulting widely before finalising its report to Government in December 2009. ▶

Executive remuneration: the Commission's preliminary recommendations

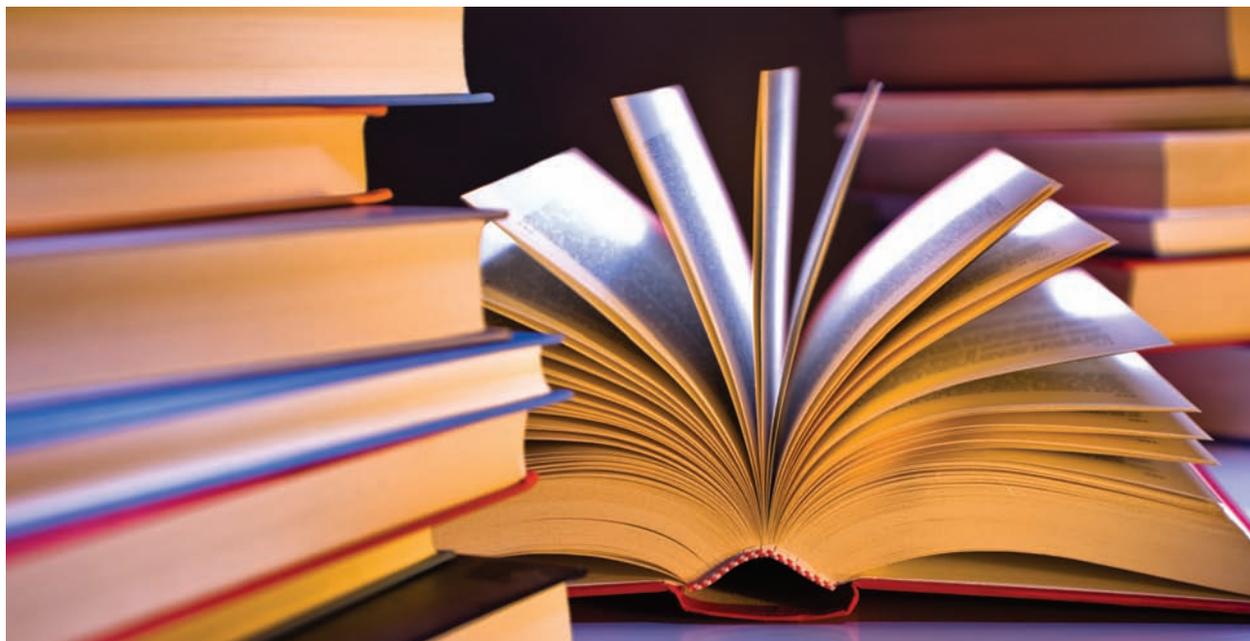
Improving board accountability and capacities:
End the 'no vacancy' rule (which allows the board to limit new nominations even if the maximum number of positions has not been filled)
Avoiding conflicts of interest:
Require remuneration committee independence for the ASX top 300 companies
For smaller companies, promote remuneration committee independence on an 'if not, why not' basis
Prohibit executives and directors voting their own shares on remuneration matters
Prohibit executives and directors voting undirected proxies on remuneration matters
Oblige all directed proxies on remuneration matters to be cast
Prohibit executives hedging unvested equity pay and equity pay subject to holding locks
Enhancing disclosure and communication:
Improve information content and accessibility of remuneration reports
Confine remuneration report to key management personnel
Require remuneration advisers to be independent of management, particularly for the ASX top 300 companies
Require remuneration advisers to be disclosed, on an 'if not, why not' basis
Encourage institutional investors to disclose their voting on remuneration reports
Promoting efficient remuneration principles:
Remuneration 'check list' for boards
Remove taxation at departure for deferred long-term equity incentives
Encouraging shareholder engagement:
Confirm legality of electronic voting
Companies be required to formally explain a 25 per cent or greater 'no' vote on the remuneration report
'No' votes above a specified threshold on two consecutive remuneration reports to trigger a board election

Executive Remuneration – Public Inquiry

- > Issues paper released April 2009. Discussion draft released 30 September 2009. Final report to Government 19 December 2009.
- > Public hearings on the discussion draft will commence in Melbourne on 27 October 2009, and in Sydney on 9 November 2009.
- > Discussion draft submissions due 6 November 2009.
- > Contact: Alan Johnston Ph: 03 9653 2147
- > Email: exec_remuneration@pc.gov.au
- > www.pc.gov.au/projects/inquiry/executive-remuneration

Restrictions on the parallel importation of books

The Commission's final report on the parallel importation of books into Australia, released in July, found that the restrictions place upward pressure on local book prices and are not the most efficient and effective form of support for Australian writing and publishing.



The parallel importation of books that have been published in Australia is subject to legislative restrictions. The Commission was asked to assess the effects of these restrictions on the community and to determine whether they should be retained. In preparing its report, the Commission drew on a range of evidence, including views put forward in over 560 submissions and in consultations with participants from industry and government, as well as its own extensive analysis of international book prices.

What are the effects of the restrictions?

From the available evidence, the Commission concluded that the Parallel Import Restrictions (PIRs) place upward pressure on book prices and that, at times, the price effect is likely to be substantial. The magnitude of the effect will vary over time and across book genres.

Most of the benefits of protection under the PIRs accrue to publishers and authors, but the demand for local printing is also increased. Most of the costs are met by consumers who fund these benefits (in a non-transparent manner) through higher book prices.

Some of the effects represent transfers from book purchasers to local book producers, but the restrictions also lead to economic inefficiencies (such as higher production costs) and a significant transfer of income from Australian consumers to overseas authors and publishers. ►

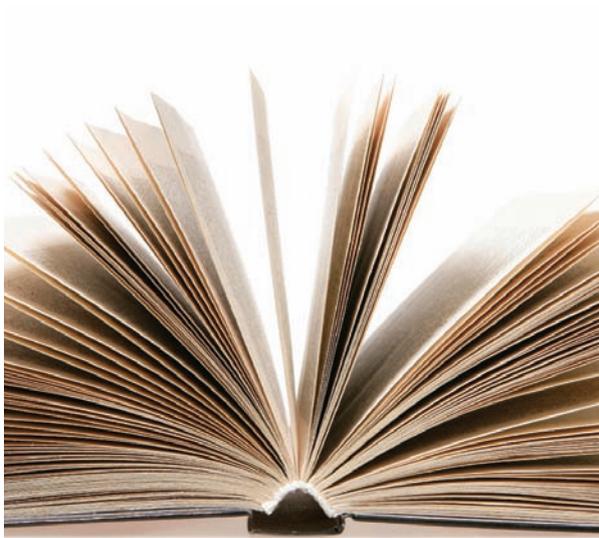
The Australian books sector

The books sector is of considerable importance to the Australian economy and community. Sales of new books currently total around \$2.5 billion a year. The market is split 60:40 between trade books (adult and children's) and educational books.

Australians obtain books from a number of sources, including local book retailers, online retailers, second-hand book stores, libraries and friends and family. Online book sales are increasing, but only account for a small share of the overall market.

The Commission estimates that around one-third of all trade books sold in Australia are Australian-authored, and that more than two-fifths of trade books (whether written by local or foreign authors) are locally published. Most of Australia's larger trade publishers are local arms of foreign companies, as are the main specialist education publishers.

A significant proportion of the books published in Australia is also printed here. There are two main plants: one in Adelaide and the other in regional Victoria. They produce predominantly monochrome paperbacks; most colour printing is sourced off-shore.



What is the rationale for government assistance?

The benefits derived by individuals from reading books are generally reflected in demand for those books (that is, in the prices consumers are willing to pay for them). However, books can also have a broader cultural value, generating benefits to the community as a whole. These cultural 'externalities' provide the strongest rationale for government support for the books industry.

In the Commission's judgement, externalities supported by PIRs are unlikely to be large. Nor are the restrictions the

Parallel import restrictions

The reproduction and first sale of books in Australia is governed by the *Copyright Act 1968*. In addition to the core copyright protections, the Act contains Parallel Import Restrictions (PIRs) that protect publishers and authors who hold the Australian rights to a title from competition by foreign copyright holders who could supply foreign editions of that title more cheaply.

Under the PIRs, if the Australian territorial rights holder releases a book in Australia within 30 days of it being published elsewhere, booksellers cannot import commercial quantities of the same book.

The publishers who benefit from territorial protection can be Australian businesses, Australian arms of international companies or international companies operating from other countries. Likewise, the works of both Australian and foreign authors can be protected from parallel imports into Australia.

The Commission's recommendations

- Repeal of the Parallel Importation Provisions (PIRs)*, with three years notice to facilitate industry adjustment.
- Immediate review of current financial assistance for encouraging Australian writing and publishing, with any changes to be implemented prior to the repeal of the PIRs.
- A review of the new arrangements to be conducted after five years.
- To assist in this review, the ABS should undertake a revised version of its 2003-04 industry survey as soon as possible and update it prior to the review.

* The Commission is recommending removal of restrictions on the importation of legitimate works produced by foreign copyright holders – not of unlawful reproductions of works.

most efficient and effective means of supporting Australian writing and publishing. The bulk of the assistance to copyright holders under the PIRs leaks offshore; and the portion flowing to the Australian industry does not target cultural externalities well: works assisted by the PIRs are not differentiated by cultural significance; and some of the assistance supports the printing industry, rather than writing and publishing.

On the release of the report, the Commission's Deputy Chairman, Mike Woods, said: 'Support for Australian authors provided by the restrictions is poorly targeted. Consumers pay higher prices for books, regardless of their cultural significance, and these costs generate greater benefits for overseas publishers and authors than for local writers. In effect, Australian consumers are subsidising foreign book producers.'

In the Commission's view, where support for cultural externalities can be justified, direct subsidies to Australian authors and publishers would deliver assistance more transparently and without the leakage associated with the import restrictions, and would generate net benefits for Australia as a whole. ■

Restrictions on the Parallel Importation of Books

- > Productivity Commission Research Report
- > Released July 2009

Reducing the costs of Australia's anti-dumping system

The Commission's draft report on Australia's anti-dumping and countervailing system recommends a number of improvements to reduce the system's overall cost to the community.

Australia's anti-dumping and countervailing system, which is based on WTO agreed rules and procedures, seeks to remedy injurious effects of 'dumped' imports on Australian industries. In the past, Australia was a major user of anti-dumping measures, but usage has declined significantly in recent years. Most of the current measures apply to a relatively narrow range of basic industrial chemicals and plastics, metal products and food and beverages – the bulk of which are inputs to further manufacturing processes. And most are against suppliers from the Asian region, Chinese firms in particular.

The Australian Government asked the Productivity Commission to undertake an inquiry to determine whether the system should be retained and, if so, how it should be configured to best serve the interests of the community as a whole.

In its draft report the Commission found that the anti-dumping system provides some benefits to a small and decreasing range of import-competing industries but imposes greater costs on the rest of the economy. However, the net economic cost is seemingly very small. And the scope for Australian industries to fall back on the system to address what are perceived by many to be 'unfair' trading practices may have lessened resistance to more significant tariff reforms. On the release of the draft report, Commissioner Philip Weickhardt said 'a few key reforms to the system would further reduce the costs and strengthen the case for the system's retention'.

A public interest test is needed

The key change proposed by the Commission is the introduction of a 'bounded' public interest test to prevent the imposition of anti-dumping measures that would be disproportionately costly. The test would have a starting presumption in favour of measures where there has been injurious dumping or subsidisation. But it would also

identify specific circumstances where measures would, *prima facie*, not be in the public interest – where they would be damaging to competition or ineffectual in removing injury; or would impose large costs on downstream users relative to the benefits for the applicant industry.

The key change proposed by the Commission is the introduction of a 'bounded' public interest test to prevent the imposition of anti-dumping measures that would be disproportionately costly.

Other proposed changes to the current arrangements include: allowing only one three-year extension of measures beyond the initial five-year term; requiring annual adjustments to the magnitude of measures; and eliminating over-collection of duties at the time of importation. To provide time for adjustment, the Commission has proposed a two-year delay before the public interest test and some other key changes take effect.

Public hearings on the draft report will be held in October, and a final report will be sent to the Australian Government by 24 December 2009. ■

Australia's Anti-dumping and Countervailing System

- > Draft Inquiry Report
- > Released September 2009
- > Contact: Alistair Davidson 02 6240 3210
- > Email: antidumping@pc.gov.au

Stop Press:

Commission staff win prestigious award

The prize for best contributed paper at the 2009 Australian Conference of Economists was awarded to Commission staff members John Salerian, Andrew Barker and Tim Murray for their paper 'Developing a partial equilibrium model

of an urban water system'. The final version of the paper is scheduled for release as a Commission Staff Working Paper in December. ■

Market mechanisms for recovering water in the Murray-Darling Basin

The Productivity Commission has been asked to report on market mechanisms for recovering water in the Murray-Darling Basin. An Issues Paper, outlining a range of matters on which the Commission is seeking information, was released in August 2009.



© MDBA, Murray River at Bottle Bend NSW, photographer Arthur Mostead

The Murray-Darling Basin is suffering considerable environmental stress due to the combined effects of prolonged drought and overallocation of water for consumptive uses. Climate change is likely to exacerbate the problem in the future.

Under an intergovernmental agreement signed in 2008, management of the Murray-Darling Basin will be coordinated under a Basin Plan to be developed by the newly-constituted Murray-Darling Basin Authority. To be introduced in 2011, the plan will set sustainable diversion limits for each Basin catchment, which is likely to substantially reduce the amount of water available for irrigation and other consumptive uses.

To ease the transition, the Australian Government, under its *Water for the Future* strategy, is funding the *Restoring the Balance* program for purchasing water entitlements for environmental use, and the *Sustainable Rural*

Water Use and Infrastructure program to reduce losses from the distribution system and increase on-farm water use efficiency.

The *Restoring the Balance* program is the central focus of the Commission's study. The program uses an open tender process as the main mechanism for purchasing water entitlements. To the end of July 2009, the Australian Government had purchased over 500GL of entitlements of varying reliability.

The Commission's approach

The Australian Government has asked the Commission to:

- review the mechanisms used nationally and internationally by governments to purchase water entitlements or similar property rights, including reverse tender processes
- identify appropriate, effective and efficient market mechanisms that could be used to diversify the range of options for purchasing water entitlements under the *Restoring the Balance* program
- identify impediments to new and established water purchase mechanisms and how these could be overcome.

As well, the Commission has been asked to consider the potential for synergies between water purchases and infrastructure investment. The Commission must also consider the community-wide impacts of the matters it reviews.

The Commission has undertaken a number of visits within the Basin and met with irrigators, industry associations, government agencies, and environmental and community groups. A draft report will be released in November 2009. Public submissions on the draft report can be lodged until early December 2009. The final report will be sent to Government on 24 January 2010. ■

What is a water entitlement?

A water entitlement is an ongoing entitlement to a share of water from a specified consumptive pool. Each water entitlement is given an allocation of water based on conditions and availability. High reliability entitlements generally receive a 100 per cent allocation in a high proportion of years.

Market Mechanisms for Recovering Water in the Murray-Darling Basin

- > Commissioned Study
- > Issues Paper released August 2009
- > Contact: Rick Baker 03 9653 2146
- > Email: water_recovery@pc.gov.au

Reducing regulatory burdens on business

The Commission's latest regulatory review recommends a range of measures aimed at reducing the regulatory burden imposed on businesses providing social and economic infrastructure services.

Unnecessary or poorly designed regulation is costly and undermines the ability of business to respond to changing market conditions. The Productivity Commission has been asked to undertake a series of annual reviews of the burdens on business from the stock of Commonwealth regulation. The third of these reports, 'Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services' was released in September.

The report found that regulation of the sector – which includes the aged care, health, child care, education and training, information media and telecommunications, energy and transport industries – is particularly heavy. In some industries, such as aged care and child care, regulation is required to protect the needs of frail or vulnerable users. Government funding of education, health and aged care requires additional regulation to ensure that public funds are properly spent. And in the telecommunications and energy industries, where natural monopolies exist, regulation is designed to promote competitive behaviour.

The Commission found that while much of the regulation in these industries aims to minimise risk and ensure service quality, it can also have unintended consequences including reducing business flexibility and adding unnecessary costs to the operation of businesses.

Inconsistency of regulations across jurisdictions in the transport, education and energy industries remains a continuing concern, despite government agreements for reform. The report argued that there is a need to move beyond these high level agreements, to significantly reduce the regulatory burden faced by businesses in these industries.

The Commission's report contains over forty recommendations aimed at improving the regulatory framework. Substantial reductions in reporting burdens might be achieved in some cases by extending the principles and methodology of standard business reporting. And regulation-making processes should be more consultative and transparent. Other recommendations include:

- Exploring options for relaxing supply constraints in the provision of aged care services.
- Improving accreditation arrangements for child care providers, and information provided to parents.
- Reducing the sports anti-siphoning list (which restricts the major sporting events that can be 'siphoned' off to subscription television), and revising the local content and local presence rules and the disclosure standard for radio.
- Ensuring that the Australian Energy Market Agreement has clearer commitments to competition reviews and ongoing price monitoring and to undertake more analysis of the practicalities of passing on to consumers the cost increases associated with the Carbon Pollution Reduction Scheme. ■

Annual Review of Regulatory Burdens on Business

> The Commission's five-year cycle of regulatory reviews covers the following areas:

2007 Primary sector (completed)

2008 Manufacturing sector and distributive trades (completed)

2009 Social and economic infrastructure services (completed)

2010 Business and consumer services

2011 Economy-wide generic regulation, and regulation not addressed earlier in the cycle

> Completed reviews are available on the Commission's website.

Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services

> Research Report

> Released September 2009



Promoting productivity and efficient infrastructure

The Productivity Commission has made short submissions to two current Parliamentary inquiries: one into productivity growth in Australia; the other into the proposed National Broadband Network.

Raising productivity growth

In a submission to the inquiry into raising the level of Australia's productivity growth, conducted by the House of Representatives Standing Committee on Economics, the Commission argued that a broad-based reform program is required to improve Australia's productivity performance. The National Reform Agenda provides an appropriate reform framework. While recognising the constrained fiscal environment in the short term, policy settings should be based on a commitment to an open and competitive economy, ongoing regulatory reform and efficient investment in human and physical capital.

The Commission's submission noted that Australia's MFP growth has averaged 1.1 per cent per year over the last four decades – placing Australia at about the middle of the OECD rankings. Largely as a result of the microeconomic reforms of the late 1980s and 1990s, MFP growth surged to 2.3 per cent per year over the second half of the 1990s, with Australia rising to second place in the OECD rankings. However, MFP growth has subsequently declined and, while some decline is to be expected, the extent of the fall, especially since 2003-04, is surprising.

The submission outlined Commission analysis suggesting that most of the recent decline could be accounted for by developments in 3 sectors:

- mining – declining resource quality and large capital investment that has not yet translated into output
- electricity, gas and water – significant capital investment and reduced rainfall
- agriculture – prolonged drought.

Though important in the long run, developments in infrastructure, education and training, and R&D, are unlikely to have had an influence on Australia's recent productivity decline. ■

Productivity Commission Submission to the House of Representatives Standing Committee on Economics Inquiry Into Raising the Level of Productivity Growth in the Australian Economy

> www.pc.gov.au/research/submission/productivity-growth

National Broadband Network

The Australian Government recently announced that it will build and operate a new fast-speed National Broadband Network (NBN), for an estimated cost of up to \$43 billion. Previous Commission work on the link between ICT and productivity emphasises the importance of competition among users to drive the adoption of profitable applications, and the need for a supportive regulatory environment.

In a submission to the Senate Select Committee on the National Broadband Network, the Commission, drawing on its earlier work, suggested a number of approaches that could reduce the risks and costs associated with the NBN project, including:

- using the proposed implementation study to undertake an economy-wide cost-benefit analysis of the project to ensure it best meets the nation's interest – with Tasmania and the designated Regional Backbone Blackspots providing opportunities for pilot studies to gather evidence to guide the implementation of the full project

- separating the investment and financing decisions for the project, and ensuring the financing vehicle transfers the risks to those best able to manage them
- ensuring an efficient regulatory framework that does not deter new investment or innovation, and complies with the principles of competitive neutrality
- meeting any social objectives through transparent, budget-funded CSOs, rather than through cross subsidies funded by artificial pricing structures. ■

Productivity Commission Submission to the Senate Select Committee on the National Broadband Network

> <http://www.pc.gov.au/research/submission/national-broadband-network>

Commission news



New Commissioner

The Australian Government has announced the appointment of Patricia Scott as a full-time Commissioner to the Productivity Commission. Patricia previously headed the Department of Broadband

and Digital Economy, and prior to that, the Department of Human Services. Earlier in her APS career, she was Deputy Secretary of the Department of Industry, Science and Tourism and held senior positions in Prime Minister and Cabinet, and Treasury.

New public inquiry: Wheat export marketing arrangements

The Assistant Treasurer and the Minister for Agriculture, Fisheries and Forestry have announced that the Productivity Commission will undertake an inquiry into the operation of the new wheat export marketing arrangements. An issues paper will be released in mid October and a draft report in mid March 2010. The final report will be presented to Government by 1 July 2010.



Industry visit: Murray-Darling Basin

Recent industry visits for the Commission's study into water recovery in the Murray-Darling Basin included a trip to the Gwydir River valley near Moree in NSW. Pictured are (from left) Commissioner Judith Sloan; Michael Murray (CEO, Gwydir Valley Irrigators Association Inc); Tony Weir (Productivity Commission) and Commissioner Neil Byron.

Recent releases

All publications can be downloaded from the Commission's website www.pc.gov.au

September 2009

Executive Remuneration in Australia
Discussion Draft

Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services
Research Report

Australia's Anti-dumping and Countervailing System
Draft Inquiry Report

Productivity Commission Submission to the House of Representatives Standing Committee on Economics Inquiry Into Raising the Level of Productivity Growth in the Australian Economy

August 2009

Market Mechanisms for Recovering Water in the Murray-Darling Basin
Issues Paper

July 2009

Productivity Commission Submission to the Senate Select Committee on the National Broadband Network Restrictions on the Parallel Importation of Books into Australia
Research Report

Overcoming Indigenous Disadvantage: Key Indicators 2009
Steering Committee for the Review of Government Services Provision

June 2009

Annual Review of Regulatory Burdens on Business: Social and Economic Infrastructure Services
Draft Research Report

Performance of Public and Private Hospital Systems
Issues Paper

The Productivity Commission's Executive Pay Inquiry: An Update on the Issues
Chairman's Speech

Current commissioned projects

7 October 2009

Log on to the Commission's [website www.pc.gov.au](http://www.pc.gov.au) for full details of all current projects.

Wheat Export Marketing Arrangements – Public Inquiry

Issues paper to be released October 2009. Draft report due March 2010.
Final report to Government by 1 July 2010.
Contact: John Salerian Ph: 03 9653 2190 Email: wheatexport@pc.gov.au
www.pc.gov.au/projects/study/wheatexport

Market Mechanisms for Recovering Water in the Murray-Darling Basin – Commissioned Study

Issues paper released August 2009. Draft report to be released November 2009.
Final report to Government January 2010.
Contact: Rick Baker Ph: 03 9653 2146 Email: water_recovery@pc.gov.au
www.pc.gov.au/projects/study/water-recovery

Contribution of the Not-for-Profit Sector – Commissioned Study

Issues paper released April 2009. Draft report to be released October 2009.
Final report to Government December 2009.
Contact: Scott Austin Ph: 02 6240 3253 Email: nfp@pc.gov.au
www.pc.gov.au/projects/study/not-for-profit

Executive Remuneration – Public Inquiry

Issues paper released April 2009. Discussion draft released September 2009.
Public hearings October/November 2009. Final report to Government December 2009.
Contact: Alan Johnston Ph: 03 9653 2147
www.pc.gov.au/projects/Inquiry/executive-remuneration

Performance of Public and Private Hospital Systems – Commissioned Study

Issues paper released June 2009. Draft report to be released October 2009.
Final report to Government December 2009.
Contact: Greg Murtough Ph: 03 9653 2163 Email: hospitals@pc.gov.au
www.pc.gov.au/projects/study/hospitals

Australia's Anti-dumping and Countervailing System – Public Inquiry

Issues paper released April 2009. Draft report released September 2009.
Public hearings October 2009. Final report to Government late December 2009.
Contact: Alistair Davidson Ph: 02 6240 3210 Email: antidumping@pc.gov.au
www.pc.gov.au/projects/inquiry/antidumping

Gambling – Public Inquiry

Issues paper released December 2008. Draft report to be released October 2009.
Public hearings November/December 2009. Final report to Government February 2010.
Contact: Monika Binder Ph: 02 6240 3238 Email: gambling@pc.gov.au
www.pc.gov.au/projects/inquiry/gambling-2009

Performance Benchmarking of Australian Business Regulation: OHS and Food Safety – Commissioned Study

Issues papers released April 2009. Food safety: draft report to be released October 2009, final report to Government December 2009. OHS: draft report to be released January 2010, final report to Government March 2010.
Contact: Sue Holmes Ph: 02 6240 3351 Email OHS: ohs@pc.gov.au Email Food Safety: foodsafety@pc.gov.au
www.pc.gov.au/projects/study/regulationbenchmarking/ohs-food-safety

Annual Review of Regulatory Burdens on Business – Commissioned Study

The Commission is undertaking a series of annual reviews of the burdens on business from the stock of Commonwealth regulation. In 2009 the Commission reviewed regulations affecting social and economic infrastructure services. In 2010 the Commission will review regulations affecting business and consumer services.

Contact: Les Andrews Ph: 02 6240 3251
www.pc.gov.au/projects/study/regulatoryburdens