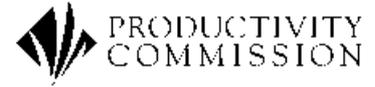




*Commonwealth  
Competitive Neutrality  
Complaints Office*



# ARRB Transport Research Limited

Investigation  
No. 6

© Commonwealth of Australia 2001

**ISBN** 1 74037 051 1

This work is subject to copyright. Apart from any use as permitted under the *Copyright Act 1968*, the work may be reproduced in whole or in part for study or training purposes, subject to the inclusion of an acknowledgment of the source. Reproduction for commercial use or sale requires prior written permission from Info Products. Requests and inquiries concerning reproduction and rights should be addressed to the Manager, Legislative Services, AusInfo, GPO Box 1920, Canberra, ACT, 2601.

**Enquiries:**

Stewart Plain  
Commonwealth Competitive Neutrality Complaints Office  
PO Box 80  
Belconnen ACT 2616

Telephone: 02 6240 3329  
Facsimile: 02 6253 0049  
E-mail: [splain@pc.gov.au](mailto:splain@pc.gov.au)

**An appropriate citation for this paper is:**

Commonwealth Competitive Neutrality Complaints Office 2001, *ARRB Transport Research Limited*, Investigation Number 6, AusInfo, Canberra.

***The Commonwealth Competitive Neutrality Complaints Office***

The Commonwealth Competitive Neutrality Complaints Office is an autonomous unit within the Productivity Commission. It was established under the Productivity Commission Act 1998 to receive complaints, undertake complaint investigations and advise the Minister for Financial Services and Regulation on the application of competitive neutrality to Commonwealth Government business activities.

Information on the Office and its publications can be found on the World Wide Web at [www.ccnco.gov.au](http://www.ccnco.gov.au) or by contacting Media and Publications on (03) 9653 2244.



## Commonwealth Competitive Neutrality Complaints Office

Level 3, Nature Conservation House  
Cnr Emu Bank & Benjamin Way  
Belconnen ACT 2617

PO Box 80  
Belconnen ACT 2616  
E-mail: [cnoffice@ccnco.gov.au](mailto:cnoffice@ccnco.gov.au)

Telephone: 02 6240 3377  
Facsimile: 02 6253 0049  
Internet: <http://www.ccnco.gov.au>

---

31 August 2001

The Honourable Joe Hockey, MP  
Minister for Financial Services and Regulation  
Parliament House  
Canberra ACT 2600

Dear Minister

In accordance with section 21 of the *Productivity Commission Act 1998* and the Commonwealth Competitive Neutrality Policy Statement, I have pleasure in submitting the results of the Commonwealth Competitive Neutrality Complaints Office's investigation of ARRB Transport Research Limited.

As ARRB is a public company whose 10 Members are representatives from each of the Commonwealth, State and Territory Governments and the Australian Local Government Association, the CCNCO has consulted with its counterpart competitive neutrality complaints offices during the course of the investigation and in the preparation of this report. The Office has also forwarded a copy of this report to our counterpart agencies in each State and Territory for them to forward to their respective governments for consideration, and to the Chief Executive of the Australian Local Government Association.

Yours sincerely

Mike Woods  
Commissioner

## Competitive neutrality policy

Competitive neutrality is a policy which aims to promote efficient competition between public and private businesses. It seeks to ensure that significant government businesses do not have net competitive advantages over their competitors simply by virtue of their government ownership. The Commonwealth, State and Territory Governments have agreed to implement this policy as part of their commitment to the National Competition Policy Reform Package.

The Commonwealth's approach is outlined in its 1996 *Competitive Neutrality Policy Statement* (CoA 1996). Competitive neutrality requirements automatically apply to Commonwealth Government Business Enterprises, designated business units of budget sector agencies and all in-house units that tender for competitive contracts. It may apply to other businesses if the benefits outweigh the costs.

The Commonwealth Government's competitive neutrality arrangements require that its designated government business activities:

- charge prices that fully reflect costs;
- pay, or include an allowance for, government taxes and charges such as payroll tax and local government rates;
- pay commercial rates of interest on borrowings;
- generate commercially acceptable profits; and
- comply with the same regulations that apply to private businesses (such as the Trade Practices Act and planning and environmental laws).

The Commonwealth Competitive Neutrality Complaints Office is located within the Productivity Commission and is responsible for administering the Commonwealth's competitive neutrality complaints mechanism. The Office can receive complaints from individuals, private businesses and other interested parties that:

- an exposed government business is not applying competitive neutrality requirements;
- those arrangements are ineffective in removing competitive advantages arising from government ownership; or
- a particular government activity which has not been exposed to competitive neutrality should be.

---

# CONTENTS

<b>Competitive neutrality policy</b>	<b>IV</b>
<b>1 The complaint</b>	<b>1</b>
1.1 Nature of the complaint	1
1.2 Background	1
1.3 The investigation	3
<b>2 Assessment of issues</b>	<b>5</b>
2.1 Tax-free status	5
2.2 Possible subsidisation by the research division	6
2.3 Rate of return on assets	9
2.4 Privileged access to State road authority assets	11
2.5 Information asymmetry	12
2.6 Implicit government guarantee	13
2.7 Conclusion	14

---

# Abbreviations and explanations

## Abbreviations

IAC	Industries Assistance Commission
IC	Industry Commission
PC	Productivity Commission

## Explanations

Billion	The convention used for a billion is a thousand million (10 <sup>9</sup> ).
Findings	<i>Findings in the body of the report are paragraphs highlighted using italics, as this is.</i>
Recommendations	<b><i>Recommendations in the body of the report are highlighted using bold italics with an outside border, as this is.</i></b>
Requests for further information	<i>Information requests are paragraphs highlighted using italics, as this is.</i>

---

# 1 The complaint

## 1.1 Nature of the complaint

On 30 October 2000, the Commonwealth Competitive Neutrality Complaints Office (CCNCO) received a complaint from Capricorn Capital Limited — on behalf of other parties — against ARRB Transport Research Limited (ARRB).

The complaint alleged that ARRB is in breach of the competitive neutrality policy of each of its owner-governments. It cited a number of factors — including a tax free status, low rate of return and privileged access to government assets and government guarantees — as likely sources of competitive advantages arising from government ownership.

The complainant sought an investigation to determine whether ARRB enjoys competitive advantages as a result of its government status, and whether any action to bring the entity into compliance with competitive neutrality policy is required.

## 1.2 Background

ARRB Transport Research Limited was formally incorporated under the *Companies Act 1961* in January 1965. It is a public company, limited by guarantee and not having share capital, whose 10 Members are the State and Territory road management authorities, the Commonwealth Department of Transport and Regional Services and the Australian Local Government Association. The company has a Board of Directors with seven members — four who are representatives of the Member organisations, two who are independent appointees selected by the Members, and the chief executive officer of ARRB.

The original memorandum and articles of association of ARRB essentially directed it to provide a national centre for road research on behalf of the Commonwealth, State, Territory and local governments. Until the 1990s, ARRB operated primarily as a research institute, with its operations funded mostly by annual subscriptions from its member governments. To augment that funding, ARRB had some minor ‘business’ activities selling products derived from its core research work.

---

In early 1999, Members decided that ARRB should remain a public company, but with a clear directive to operate as a stand-alone commercial entity. At the same time, a majority of Members expressed a need for ongoing access to technical expertise on roads and road transport. In line with this decision to operate as a commercial entity, ARRB has been changing its Memorandum of Association to reflect its altered focus.

The need for this change has arisen because of a shift in the way government transport authorities have sourced their research requirements. Over the last 10 years or so, and in line with broader competition policy reforms, the approach of ARRB's member governments has shifted from being investors in a research body to purchasers of specific research and related services. As a result, the collective purchase of research through Austroads (an association of the road and traffic authorities in Australia and New Zealand) has superseded direct funding of ARRB.

Under this arrangement, Austroads purchases research work required by its members that they have chosen to not undertake 'in-house'. Formerly, almost all of this research would have been automatically directed to ARRB. Now, about 75 per cent to 80 per cent of the total value of the outsourced research work purchased by Austroads is allocated on a non-contestable basis to preferred suppliers, including ARRB. The balance of the outsourced research is purchased through tender, and ARRB must compete with other businesses for this work. Since the change in arrangements, ARRB has, on average, secured about two-thirds of both the non-contested and the contested work.

As a result of these changed arrangements (coupled with a gradual decline in the value of research outsourced by Austroads evident since 1995), revenue derived by ARRB from contested and non-contested research from Austroads has steadily fallen. This has forced ARRB to move from being a research institute reliant on direct government funding, to an organisation with a commercial focus supplying a wider range of products and services to a variety of customers. In turn, this has resulted in a re-organisation of ARRB, which now has three divisions within its overall business: Research and Consulting; Product Development and Sale; and Technical Services.

ARRB's latest published Financial Report (to end December 2000) indicates annual revenues of almost \$17 million and total assets of some \$15 million. It is a significant business with a dominant presence in the Australian markets in which it operates. It is also extending its commercial operations to international markets — in 2000 its Technical Services Division earned around half its revenue from overseas sales.

---

## 1.3 The investigation

The CCNCO advised all government stakeholders in ARRB of the complaint — for State and Territory Governments this was via their competitive neutrality complaint agencies. With the agreement of those jurisdictions for which the complaint was relevant<sup>1</sup>, the CCNCO undertook the investigation of the complaint on their behalf. The CCNCO consulted with relevant complaint agencies during the course of its investigations and in the preparation of this report.

During the course of its investigation, the office held discussions with ARRB, Capricorn Capital and associated parties, the Australian Taxation Office, Austroads and representatives of Commonwealth, State and Territory road and traffic agencies responsible for contract works for which ARRB and private sector firms are in competition.

---

<sup>1</sup> The complaint was not recognised by Queensland, as ARRB is not specified in the Queensland Competition Authority Act as a government business activity to which competitive neutrality applies.



---

## 2 Assessment of issues

The complaint against ARRB specified the following areas in which it might receive an advantage because of its government ownership, and thus might be in breach of the competitive neutrality policy of its member governments:

- tax free status;
- access to research work awarded without competitive tender by its owners, from which it can cross-subsidise other work subject to competitive tender;
- low rates of return on assets;
- privileged access to assets of State road authorities, including physical assets (service compounds, equipment), intellectual property and the uncharged labour of government employees;
- access to commercially valuable information, for example data bases, policy development or future work plans of its shareholders; and
- the ‘implicit guarantee’ of government.

The merits of each of these claims are examined below.

### 2.1 Tax free status

As ARRB was originally constituted as a research institute, it was exempt from the payment of company tax. However, following a number of changes to its Memorandum of Association and a redirection of focus to commercial activities, the Australian Tax Office (ATO) reviewed that exempt status. In December 2000, the ATO advised ARRB that the 1998-99 fiscal year would be the last year for which it had tax exempt status. ARRB is now liable for all relevant company taxes.

As a ‘non-profit’ entity, ARRB was also eligible to receive a rebate on fringe benefits tax. In 1999, this rebate — equal to 48 per cent of the relevant tax payable by ARRB — amounted to some \$73 000 in a total cost base of around \$16 million. As a result of the review and subsequent finding by the ATO, ARRB is no longer eligible for this rebate.

---

The abolition of wholesale sales tax consequent upon the introduction of the Goods and Services Tax (which is payable by ARRB) has removed any advantage that ARRB may have previously had in relation to commodity taxes.

The CCNCO has confirmed with state revenue officials that ARRB is liable for, and pays, payroll tax on the same basis as non-government businesses.

In sum, while ARRB has previously benefited commercially from a range of tax exemptions, the changes outlined above have removed that advantage and, on that basis, the tax treatment of ARRB is now consistent with competitive neutrality policy principles.

## **2.2 Possible subsidisation by the research division**

ARRB operates three divisions within its overall business: Research and Consulting; Product Development and Sale; and Technical Services. Capricorn Capital claimed that ARRB's commercial activities may be unfairly advantaged if the revenue from the research work it receives on a non-contested basis from Austroads is available to subsidise the costs (and thus prices) of work where ARRB is in competition with other suppliers. In support of its claim, Capricorn referred to ARRB's Financial Report to 31 December 1999 which states:

... the rapid growth in revenue from technical services and technology sales was accompanied by delivery problems which seriously eroded planned margins and led to a poor financial result from this part of the business. ... The research business, on the other hand, performed well.

Capricorn's concern about this likely source of competitive advantage was reinforced by its belief that the research business of ARRB mostly comprises work awarded on a non-contested basis.

The CCNCO has previously argued that, in most circumstances, the appropriate basis for assessing a fully commercial entity's financial performance is the rate of return on its aggregate business activity. Subject to achieving a satisfactory overall rate of return, the pricing policies (and resultant returns) for particular products or activities are commercial decisions for the organisation concerned.

However, in this case, Capricorn Capital argues that, as the source of the alleged cross-subsidy derives from that part of ARRB's research business where its government status may confer an advantage, it is potentially a competitive neutrality issue. The CCNCO has assessed this aspect of Capricorn's complaint.

---

Assessing any advantage potentially accruing to ARRB's commercial activities requires that the non-contested work be considered in the context of ARRB's total activities. It also requires an assessment of the scope for non-contested research work to generate the margins needed to cross-subsidise ARRB's other activities. Finally, the CCNCO must assess if any advantage conferred upon ARRB is derived solely as a result of its government status.

In 2000, the latest year for which data are available, non-contested research work from Austroads accounted for less than 15 per cent of ARRB's total revenue of \$16.8 million<sup>1</sup>. Accordingly, the capacity for any excessive margins on non-contested work to materially cross-subsidise other areas of ARRB would seemingly be quite limited.

Additionally, ARRB's consolidated accounts do not support the view that its research division produces margins of sufficient size to cross-subsidise ARRB's other business activities that compete in the marketplace. This assessment is reinforced by ARRB's Corporate Plan and its Business Plan for 2000-2002, which notes the need to generate sufficient income from the Product Development and Sale and the Technical Services Divisions to underwrite the financial health of the research arm.

There are a number of reasons why non-contested research is unlikely to deliver excessive margins to fund cross-subsidies.

The research business of ARRB operates from a structural base that can provide the facilities for research tasks that may be only required occasionally. As a result, these facilities are typically under-used (a legacy of its time as a national research institute) and, according to ARRB, fixed costs for non-contested research work are relatively high. Moreover, ARRB claims that the members of Austroads expect ARRB to provide more output for each project dollar than other suppliers because this was always the case with a grant funded organisation. ARRB maintains it has little discretion in practice to decline such projects, even where they are marginal or non-commercial.

Further, both Austroads and ARRB noted that much of the non-contested research is in the form of small, short-term contracts, with an average project value of about \$40 000. For these projects, overheads (such as the cost of constructing bids) are relatively high, the ability to amortise costs is limited and margins are correspondingly circumscribed. In this regard, Austroads indicated to the CCNCO that, based on its negotiations with ARRB — the budget and/or scope of non-

---

<sup>1</sup> For the most recent work program (for 2001-2002), Austroads estimated that the work allocated to ARRB on a non-contested basis would total around \$2 million.

---

contested projects are usually negotiated between Austroads and ARRB — it considers the non-contested research allocated to ARRB does not generate excess margins for ARRB.

The potential for ARRB to cross-subsidise any of its other business activities appears further constrained by the contract conditions that Austroads imposes on ARRB. Austroads advised the CCNCO that it imposes payment terms for research contracts awarded to ARRB that are more onerous than those it generally applies to private suppliers, and that this is the result of having common government members of Austroads and ARRB. Austroads noted that these terms would result in a slower cash flow for ARRB than for equivalent work provided by other research providers.

Given the relative size and the nature of the non-contested research work, the CCNCO considers that it is highly unlikely that any surplus that may derive from ARRB's non-contested research could be used to provide a material cross-subsidy to its contestable operations.

Moreover, to the extent that any cross-subsidisation were possible, it is not clear that this would be attributable to an advantage of being 'government'.

Discussions with Austroads confirm that the work allocated on a non-contested basis is confined to work that Austroads' members have deemed appropriate to direct to those organisations with which they have formed a strategic alliance in that area of work. A decision to allocate work on this basis is only reached after all members of Austroads have deliberated on the merit of doing so and have agreed that the recipient organisation is most qualified to undertake that work. Previous institutional arrangements for procuring research for government road agencies contributed to ARRB's past success in attracting non-contested research. However, under current arrangements, there is no obligation for governments to direct work to ARRB other than on the basis of ensuring that it has the ability to achieve a satisfactory research outcome.

ARRB's current success in attracting this work therefore appears to be the result of Austroads' confidence in the quality of its research and its ongoing close relationships with the purchasing agencies making up Austroads.

That said, the preceding discussion highlights a potential conflict arising from ARRB's shift to a commercial focus and its *de facto* role as a source of public interest research. It seems there may be an expectation by governments that ARRB will do some work on a less than fully commercial basis. To the extent that this occurs, it may detract from ARRB achieving its objective of operating on a commercial footing — an objective agreed by its Board and expressed in its most recent Corporate Plans.

---

If a continuing objective of the member governments is for ARRB to maintain a public interest research capability beyond that required for its commercial purposes, the issue of how best to accommodate this will assume increasing importance as ARRB moves towards its goal of a fully commercial operation. An explicit policy from Members to establish a transparent method for funding such non-commercial activities would assist ARRB in planning its commercial future.

In this context, ARRB currently maintains the M G Lay Library and Information Service (a facility included in its asset base) which is available for use by any government or private source, and which is a non-commercial function. ARRB members have explicitly recognised its non-commercial nature, as they annually negotiate an agreement with ARRB to contribute to its continuing operation.

## **2.3 Rate of return on assets**

Capricorn Capital noted in its complaint that ARRB's Financial Report for the year ended December 1999 indicated a total operating profit before income tax for 1999 of \$341 000 on net assets of \$7.9 million. This represents a pre-tax rate of return on net assets of some 4.3 per cent. For the preceding 18 months — ARRB changed from a fiscal year reporting base to a calendar year base in that period — comparable figures indicate it incurred a loss of \$434 000 on net assets of \$7.5 million.

The most recent results for the 12 months to December 2000 show an operating profit before income tax of \$560 000 on net assets of \$11.2 million — a pre-tax rate of return of 5 per cent.

In discussions with the CCNCO, Capricorn Capital referred to a range of specific projects where ARRB had significantly undercut what Capricorn considered were highly competitive, fully-costed bids by private suppliers. This pricing by ARRB, which Capricorn considered could not deliver a commercial rate of return, was proffered as further evidence that ARRB is acting in breach of its competitive neutrality obligations.

The CCNCO notes that companies in all industry sectors may sometimes price individual bids that will yield low or negative returns for particular strategic reasons. Accordingly, the appropriate basis for assessing financial performance is to use the rate of return for the aggregate activities of ARRB. Indeed, most of Capricorn's argument focuses on this.

In this regard, it is clear that ARRB's recent performance has not been commercially satisfactory. Capricorn Capital considered an appropriate weighted

---

average cost of capital for the type of business ARRB is involved in would be in the vicinity of 12 to 16 per cent. While not having a view on precisely what an appropriate rate of return would be, the CCNCO has confirmed with ARRB that this is an appropriate target range. The returns reported above by ARRB fall well short of that target range. (The CCNCO has not referred to the rate of return on shareholders equity because ARRB is a public company with no share capital. Further, its Articles and Memorandum of Association specifically preclude payment of dividends or a distribution of capital to its members.)

Performances for 1998 and 1999 (and the results for 2000 released since the complaint was lodged) were also below the rate of return target sought by ARRB members. According to ARRB, the shift from being a body funded directly by grants to one having to survive on a commercial basis has entailed transitional costs that have adversely affected its rate of return, and compounded the effects of a difficult market environment.

Of material significance have been substantial abnormal costs incurred during its change of direction. For example, in 1998, following the Board's acceptance of ARRB's Corporate Plan 1997-1999 (directing ARRB to operate on a commercial footing), it retrenched almost 20 per cent of its staff, a move which resulted in over \$700 000 in redundancy expenses, and wrote off over \$250 000 in obsolete stock. In addition, the legacy of past superannuation arrangements has required major increases in employer contributions to sustain the scheme's viability (starting in 1999 and continuing over the life of the 2000-2002 Corporate Plan). The annual provision needed to bring that scheme back to viability involved an increase in employer contributions of over \$300 000 in 1999 and over \$730 000 in 2000. Adjustments of this size were of sufficient magnitude to compromise ARRB's capacity to deliver an acceptable rate of return.

ARRB operates from a facility developed in the early 1970s as a research institute. It was originally envisaged that test tracks etc might be required, and sufficient land was purchased to cover that possibility. Such facilities are not required in its present guise, and this inflated asset base has also adversely affected ARRB's rate of return. To address this, ARRB completed a revaluation and sale of unused parts of its site during 2000. The realised value was over \$500 000 above previous book value, and the resultant receipts have commensurately increased ARRB's operating profit after tax for 2000. However, the sale represents a one-off injection of receipts and any long-term improvement in ARRB's return on assets remains dependent on an improvement in its trading performance.

To improve its rate of return on assets, ARRB is seeking to reduce its dependence on research business. ARRB views this as an essential priority for its longer-term commercial viability. Its Corporate Plan 2000-2002, however, provides for

---

substantial internal investment in research capability (beyond that required for purely commercial purposes) to meet Members' expressed need for ongoing access to technical expertise in roads and road transport. The CCNCO notes that the scale of this internal investment will have a material effect in lowering ARRB's profit and rate of return over that period, and again highlights a potential conflict between Members expectations of ARRB and its desire to operate as a commercial entity.

ARRB's rate of return for 1998, 1999 and 2000, and that foreshadowed over the balance of the Corporate Plan 2000-2002, is below an acceptable commercial rate of return. However, the CCNCO has noted in previous publications that the commercial rate of return requirement is not a single year target, but rather is an average that should be achieved over a reasonable period. Failure to earn a commercial rate of return in any particular year, or even over several years during the establishment phase of a business, may not necessarily constitute a breach of competitive neutrality.

In view of ARRB's change of direction and the transitional circumstances involved in that change, the CCNCO considers that the recent rate of return performance of ARRB and that foreshadowed in the 2000-2002 Corporate Plan does not reflect a deliberate attempt to gain competitive advantage through these means. That said, ARRB should aim to generate significantly higher returns beyond the current Corporate Plan.

## **2.4 Privileged access to State road authority assets**

Capricorn Capital expressed concerns that ARRB's government status may confer upon it advantages in the use of State road authority compounds and other assets — advantages of commercial worth unavailable to its competitors.

CCNCO discussions with government road authority personnel indicated that all significant technical services contracts are allocated on the basis of public tender. As part of that public process, ARRB is subject to the same conditions and treatment as all other bidders. Once contracts are let, the road authorities stated there would be no difference in the form or degree of assistance offered to ARRB compared with any of its competitors.

The CCNCO followed up on one instance brought to its attention where, in 1999, ARRB had the use of a road authority compound to store its vehicle during the evaluation period of a tender in Western Australia. In that case, a probity assessment of the tender process considered the event was of no material significance to the tender evaluation. To avoid any suggestion of preferential treatment, Main Roads WA subsequently advised ARRB that, in future, storing its

---

equipment at Main Road depots will not be allowed at times other than during the term of a contract they may have with Main Roads.

More generally, representatives of various road authorities told the CCNCO that the short-term storage of contractors' equipment in their compounds is a service offered to any potential contractor. (Main Roads WA noted that in many areas of Western Australia — as in other States — the only secure compounds are those of the State road authority.) In this regard, the ARRB is treated no differently from other contractors.

## 2.5 Information asymmetry

The complaint against ARRB claimed that it has access to information not available to its competitors as a consequence of its government status and the resulting close relationship it maintains with government road authorities and members of Austroads. Capricorn alleged that this is likely to confer upon ARRB an advantage in being aware of material details of forthcoming contracts (and thus in preparing for and winning competitive tenders for that work).

Implicit in the concern that ARRB may receive preferential treatment in the award of technical services contracts by road authorities is the perception that this may occur as a *de facto* funding process to support ARRB's research capabilities. However, the CCNCO found no evidence to substantiate this view.

Government road authority representatives advised the CCNCO that companies likely to bid for tendered work maintain regular contact with the authorities. They held that ARRB is no exception, and is treated the same as its competitors.

In addition, road authority personnel noted that all jurisdictions have strict guidelines governing the conduct of public tenders. For example, the New South Wales Road Transport Authority noted that it has in place internal systems and controls designed to ensure it complies with NSW Government Procurement and Competition Policy Guidelines (which encompass competitive neutrality). Moreover, these systems and controls are subject to regular internal audits to assess compliance and effectiveness and detect any systemic weaknesses.

Any impropriety in the conduct of a tender and its award to a bidder would be a matter for the relevant state contract audit process or complaint mechanisms dealing with tender processes. In this regard, the CCNCO was referred to a dispute concerning preferential treatment allegedly afforded ARRB for a contract in Western Australia to verify the quality of pavement construction of third party contractors. Main Roads WA advised that this was investigated separately by them,

---

and that no evidence was found to support the claim that ARRB had either received, or was considered for, preferential treatment because of its ‘government’ status.

In one area though, ARRB does have preferential access to information. The Austroads secretariat advised the CCNCO that the head of ARRB has a non-voting (observer) seat on the Austroads council and, as such, is eligible to receive all the council papers. As a result, the head of ARRB would know the forward research work program of Austroads.

That said, forward work programs only contain a general description of the research work that Austroads would be seeking, and do not include details of any consequent tender requirements. In the view of the Austroads secretariat, this lack of detailed specification would mean any commercial advantage derived from prior knowledge of the Austroads’ research requirements would be quite minor.

## **2.6 Implicit government guarantee**

Capricorn Capital alleged that ARRB might, because of its government status, receive favourable treatment in regard to performance risk and credit risk.

However, this allegation was not supported by tender and contract documents reviewed by the CCNCO, nor by discussions it held with various state road authority representatives. Those documents made no concessions or granted any exemption to ARRB with regard to insurance requirements, performance bonds, liquidated damages etc when compared with its competitors. In addition, the CCNCO has reviewed correspondence between ARRB and a state road authority where it was apparent that ARRB’s ‘government’ status conferred no benefit in alleviating the penalties it was liable for as a result of non-performance under its contract.

Similarly, no evidence of an implicit government credit advantage was apparent to the CCNCO for multi-million dollar bank loans taken out by ARRB.

ARRB was incorporated under the *Companies Act 1961* as a company limited by guarantee, and its Memorandum of Association clearly states that the liability of its members is limited. In the event the company were forced into dissolution, the members would each only be liable to the extent of a sum not exceeding (the current equivalent of) ten pounds sterling. This provides little legal basis to justify any favourable insurance or indemnity treatment.

---

## 2.7 Conclusion

In the past, ARRB received tax exemptions that were inconsistent with the principles of competitive neutrality. However, with the introduction of the Goods and Services Tax, removal of company and fringe benefit tax exemptions by the ATO and compliance with the requirements of State revenue offices, the CCNCO has found that ARRB currently has no competitive advantage in terms of tax treatment.

The CCNCO found no support for the claim that revenue from non-contested research work is used to cross-subsidise the commercial work of ARRB. Given the nature of the non-contested research work and its small share of overall revenue, the CCNCO considers that it is highly unlikely that ARRB's non-contested research could be used to provide a material cross-subsidy to its contestable operations.

ARRB's rate of return for 1998, 1999 and 2000, and that foreshadowed over the remaining period of the Corporate Plan for 2000-2002, is below a commercial rate of return. However, ARRB is still in the process of changing from a direct-funded research institute to a fully commercial business. In making this transition, the legacy of its immediate past and the process of establishing a market presence are material circumstances affecting its rate of return. In view of this, the CCNCO considers that ARRB's recent rate of return performance does not reflect a deliberate attempt to gain competitive advantage through these means. The CCNCO notes, though, that sustained failure to achieve an appropriate rate of return would represent a breach of competitive neutrality principles.

The CCNCO found no evidence that ARRB's 'government' status gives rise to preferential treatment in the allocation of either research contracts from Austroads, or of competitively tendered contracts from government road authorities. In addition, state road authorities advised the CCNCO that, once ARRB had won contracts from them, it received no preferential treatment that could deliver material commercial gains in the conduct of its contract obligations.

The CCNCO found no evidence to support the view that ARRB receives any commercial advantage in relation to the assessment of its credit and performance risk rating as a consequence of its 'government' status.

However, the CCNCO draws attention to the potential for non-commercial public interest research undertaken by ARRB to conflict with its capacity to operate successfully as a commercial entity. If this is indeed a demand upon ARRB by its member governments then, to assist ARRB in planning its commercial future, Members might consider explicitly specifying such a demand and how funding for such non-commercial activities should be negotiated.

