

Submission to Productivity Commission on Cost Recovery *Draft Report.*

by

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Further to my Submission(No.45) dated 23 November 2000 and appearance in hearings I make this submission on the Draft Report following the PC Circular on 12 April.

1. The Draft Report is to be commended. It is a “first” in terms of an official expose of the serious economic consequences for Australia of governments’ unbridled embrace of disguised taxation under the guise of “full cost recovery” – a trend which began in the mid 1980s.
2. The PC Draft Report (and Final Report in due course) is regrettably limited in its terms of reference to regulatory and information activities of the Commonwealth. The subject, however, is most relevant (indeed perhaps more so) to State and Local governments in Australia. It would therefore be most desirable if the Productivity Commission could explicitly say in the Final Report that the principles and thrust of its findings have wider application across all levels of government – and urge State and Local governments to consider this important subject also.
3. It is unfortunate the Bibliography does not cite important and comprehensive earlier publications in this area, which dealt in depth with economic theory questions, by the Business Council of Australia in 1993 and 1995 (ISBN 0909865566 and ISBN 0909865574 and by the Rural Industries Research and Development Corporation in 1999 and 2001 (ISBN 0642580111 and ISBN 0642582793). The latter publication, just released *Infrastructure Regulation Cost Methodologies and Processes*, is very relevant to this Inquiry (as it is to the PC Access Inquiry).
4. Chapter 6 Recommendations are excellent and should be retained in the Final Report. Most particularly Recommendation 6.1 should be central for this Report, and for any Guidelines to agencies (and Ministries of Finance and Treasuries, and State Regulator Agencies under NCP) at all levels of government in Australia to whom this Report may be directed.
5. Unfortunately, the Draft Report does not adequately stress the serious adverse impact on business costs, productivity and the international competitiveness of Australian business by the rise of “cost recovery” and “user charges” in Australia. It dwells too much on the final consumer rather than highlighting the cost of business inputs.
6. Indeed, the Draft Report conveys the flavour (no doubt unintentionally) that there is only one class of “consumers”, namely individuals.
7. However, businesses would surely be the major “consumers” as essential inputs into their operations of the government “services” subject to this Inquiry. The impact on business costs of Ramsey pricing, gold plating, misuse of monopoly power by government agencies, cost recovery “targets” and the like which all amount to

administered prices on business in excess of marginal cost (and hence a tax) should be highlighted in the Final Report. As the Report is presently drafted too little attention is given to the impact on business costs and international competitiveness.

8. The Draft Report while acknowledging marginal cost as central to any consideration of cost recovery/user charges, should go further to stress the importance of that point. The Draft Report too readily accepts the often self-serving viewpoint (of monopolists) that marginal cost is too difficult to measure in practice, and hence the nebulous concept of incremental cost should be the aim. While incremental cost (itself a concept having no basis in economic theory, being derived presumably from accountancy theory) is certainly a better outcome than “full cost recovery” for Australia’s economic efficiency, it nevertheless would be desirable for the PC Final Report to stress the overarching objective of marginal cost pricing.

Guidelines & Implementation

9. The promulgation of guidelines is important – bearing in mind they will hopefully be taken up by State and Local governments. They should clearly set out the desirable economic efficiency criteria (Chapter 6) and seek to terminate Ramsey pricing, gold plating, misuse of monopoly power by agencies and the enforcement of (often non-transparent) cost recovery percentages on agencies by Ministries of Finance and Treasuries.
10. Implementation, by the substantial up-grading of the PC Office of Regulatory Review to the status of an Independent Regulator-General (along IPART, Victorian Regulator-General, etc lines) would be the most desirable outcome so as to permit full input by consumers (including business users) into the price determination process. In other words any new up-graded Commonwealth Office of Regulatory Review must have “teeth” and it must allow for full adversarial processes so that consumers (and business users) have equal rights in price determination decisions with departments and Finance Ministries. In other words, the new ORR should have the same processes and powers as State Regulator Generals.
11. It would be nugatory and an unfortunate failure of this Inquiry if the outcome was a comfortable and cosy departmental /regulator relationship based on vaguely drafted guidelines. There should be an open and transparent process to replace the present unsatisfactory situation. It must provide opportunity for consumers and businesses to submit material to annual pricing reviews undertaken by an arms length and independent regulator, and for adversarial public inquiry processes to take place before final pricing decisions are promulgated.

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