



PC NEWS



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Australian Government
Productivity Commission

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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Productivity Commission News



NEW PUBLIC INQUIRY

Intellectual Property Arrangements

The Australian Government has asked the Productivity Commission to undertake a 12 month public inquiry into Australia's intellectual property system. In undertaking the inquiry, the Commission is to:

- consider whether current arrangements provide an appropriate balance between access to ideas and products, and encouraging innovation, investment and the production of creative works.
- recommend changes to the current system that would improve the overall wellbeing of Australian society.

An issues paper was released in October, a draft report will be published in April/May 2016, and the final report will be sent to Government in August 2016.

> Details of all current commissioned projects appear on page 28 and are available at www.pc.gov.au

Trade & Assistance Review 2013-14 released

The latest issue of the Commission's annual publication *Trade & Assistance Review* was released in June. The review contains the Commission's latest estimates of Australian Government assistance to industry, which totaled over \$17 billion in 2013-14. This edition of the review also outlines policy implications of the evolution and recent measurement of global value chains. New data show that more of Australia's exports ultimately end up in Europe and the United States than suggested by traditional Australian trade data. The review also identifies some issues and concerns with preferential trade agreements (otherwise known as free trade agreements) and argues there is a compelling case for the text of an agreement to be rigorously analysed *before* signing.

The Trade & Assistance Review 2013-14 can be downloaded from the Commission's website www.pc.gov.au

Commission hosts 2015 GTAP meeting

The Global Trade and Analysis Project (GTAP) produces a global database comprising a fully consistent set of input-output tables, tariffs, taxes and subsidies, and bilateral trade flows, for more than 100 countries. The database is a key input into contemporary general equilibrium analyses of global economic issues. The project is maintained by the Centre for Global Trade Analysis at Purdue University in the United States, with the support of a consortium of national and international agencies.



Between sessions at the GTAP Board meeting in Melbourne: Professor Thomas Hertel (centre) Executive Director of GTAP, with Kenichi Kawasaki (left) from the Japanese Research Institute of Economy, Trade and Industry and Lucian Cernat (right) from DG Trade at the European Commission.

The Productivity Commission hosted the 2015 GTAP Board meeting in June, in parallel with GTAP's 2015 annual conference on global economic analysis which was also held in Melbourne

GTAP's origin lies partly in the SALTER model, developed by the Productivity Commission's predecessor, the Industry Commission, to evaluate scenarios under the Uruguay Round of multilateral trade negotiations. As part of its research program, the Commission continues to support development of the GTAP database by preparing the Australian data for the project.

Australia's workplace relations framework: draft report says 'repair not replacement'

There is considerable scope for improvement in Australia's workplace relations framework, but radical reform is not required.

In December 2014 the Australian Government asked the Productivity Commission to assess the performance of the Australian workplace relations (WR) framework and identify options for improvement. A series of 5 issues papers were released in January 2015 and after extensive public consultation with stakeholders, a draft report was released in August. After further consultation the final report will be sent to Government in November 2015. The Commission is open to any new ideas or variations on its draft report recommendations.

In conducting the inquiry, the Commission recognised that a well-performing WR framework must balance the needs of businesses within the economy with the requirement to adequately compensate and protect the Australian workforce.

The architecture of the current system

Australia's WR framework comprises a complex array of labour laws, regulations and institutions. The national system directly affects millions of Australian workers. In mid-2015, around 11.8 million people worked in

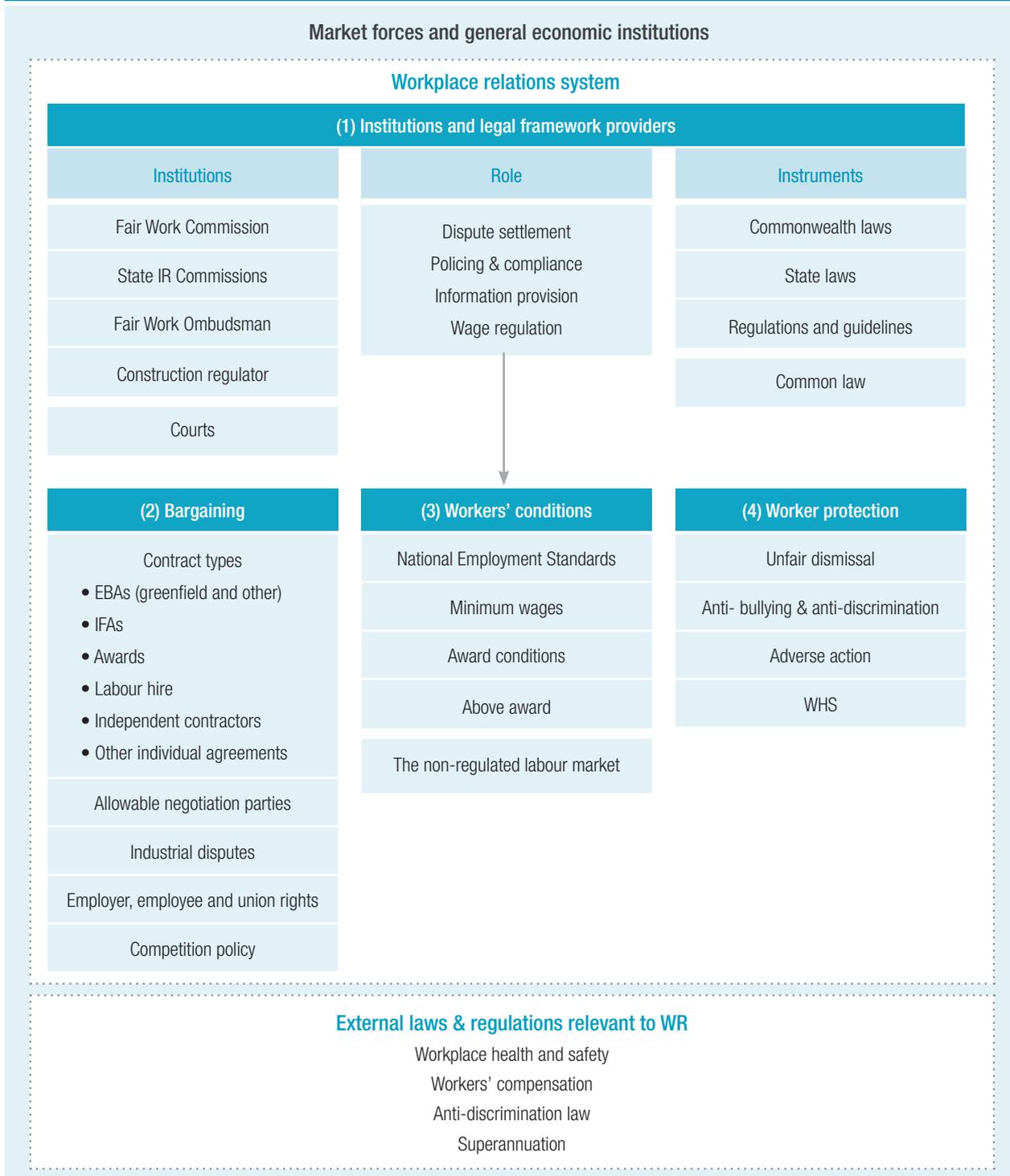
more than 2 million workplaces around the country. Of these people, 70 per cent were covered directly by federal workplace laws, and others are indirectly affected. The Fair Work Commission (FWC), the Fair Work Ombudsman (FWO) and Fair Work Building and Construction are the key national regulators, and the Federal Court is the principal judicial body.

The Fair Work Act covers most aspects of the way in which parties should deal with each other in their employment relations, and in setting a variety of minimum standards. An extensive body of common law sits beside the statutory framework. Reflecting the regulatory underpinning of the system, wages and conditions for most national employees must be at, or above, the safety net of those set in 122 awards.

The Commission's draft report found: 'People are confused by the workplace relations system, and some parties that should have a bigger voice in it – consumers, the unemployed and underemployed – have marginal influence. There are unquestionable inefficiencies, remnant unfairness, some mischief and absurd anachronisms. In this messy context, there is an understandable tendency to imagine that there must be a much neater and coherent system, and that it would be desirable to start with a clean slate. The view from the bulk of stakeholders and from the Commission's analysis is that such a view would be misplaced. The system needs renovation, not a 'knockdown and rebuild'.'



The architecture of the current system is highly elaborate and broad ranging



The system is not dysfunctional

The draft report suggests that Australia's labour market performance and flexibility is relatively good by global standards, and many of the concerns that have pervaded historical arrangements have now abated. Strike activity is low, aggregate wages are responsive to economic conditions, wage contagion seems to be

a thing of the past, and there are multiple forms of employment arrangements that offer employees and employers flexible options for working. However, there are weaknesses in the system that can impede service quality to consumers, limit the prospects for the unemployed when the economic cycle slows, stymie innovation, and reduce the credibility of enterprise bargaining.

Several major deficiencies in the WR framework need addressing

Reform of institutional arrangements

The performance of Australia's workplace relations system relies strongly on the capabilities and functioning of its main institutions.

The Commission found that the Fair Work Ombudsman is performing well. However, while the Fair Work Commission undertakes many of its functions effectively, the legalistic approach it adopts for award determination gives too much weight to history, precedent and judgments on the merits of cases put to it by partisan lobbyists. A preferred approach to award determination would give greatest weight to a clear analytical framework supported by evidence collected by the FWC itself. As well, the appointment process for FWC members can lead to inconsistencies in some of its decisions, and should be reformed.

The safety net

The safety net comprises three main instruments that set floors for wages and conditions: the national minimum wage, the National Employment Standards and awards (including penalty rates).

Minimum wage setting in Australia

The national minimum wage is usually adjusted by the FWC each year following an annual review. The current national minimum wage rate is \$17.29 per hour for adults. This sets a floor on the wage rates of most Australian workers, although there are lower rates for younger workers, apprentices and trainees, and some people with disabilities.

The FWC also makes annual adjustments to the rates of pay specified in modern awards, which mostly start at equal to or just above the national minimum.

The Commission estimates that around 7.2 per cent of employees are paid at up to the hourly minimum wage rate.

Returns to labour of some important employment categories – independent contractors, working business operators and unpaid family members – are not influenced by the minimum wage and are entirely market determined.

Enhancing minimum wage determination

Minimum wages in Australia are set by an FWC Expert Panel, taking into account changes in economic conditions and representations, especially from the government, business and union stakeholders. It generally awards modest rises in minimum wages, and its predecessors have occasionally suspended increases during economic downturns.

While the need for a national minimum wage is widely accepted in Australia, including by the Commission, employer groups, unions and governments regularly disagree about its appropriate level. There are also ongoing disputes among economists about how minimum wages affect employment and poverty.

Economic theory and some international empirical studies suggest that increases in minimum wages can reduce jobs and/or hours worked, but they also indicate that employment gains are possible in some circumstances.

The Commission's draft assessment is that modest increases in Australia's minimum wage are unlikely to measurably affect employment, but that marked increases in the minimum wage bite (that is, the minimum wage as a proportion of median wages) would reduce employment. How, and at what rate, such effects manifest will vary depending on economic conditions and other policy settings.

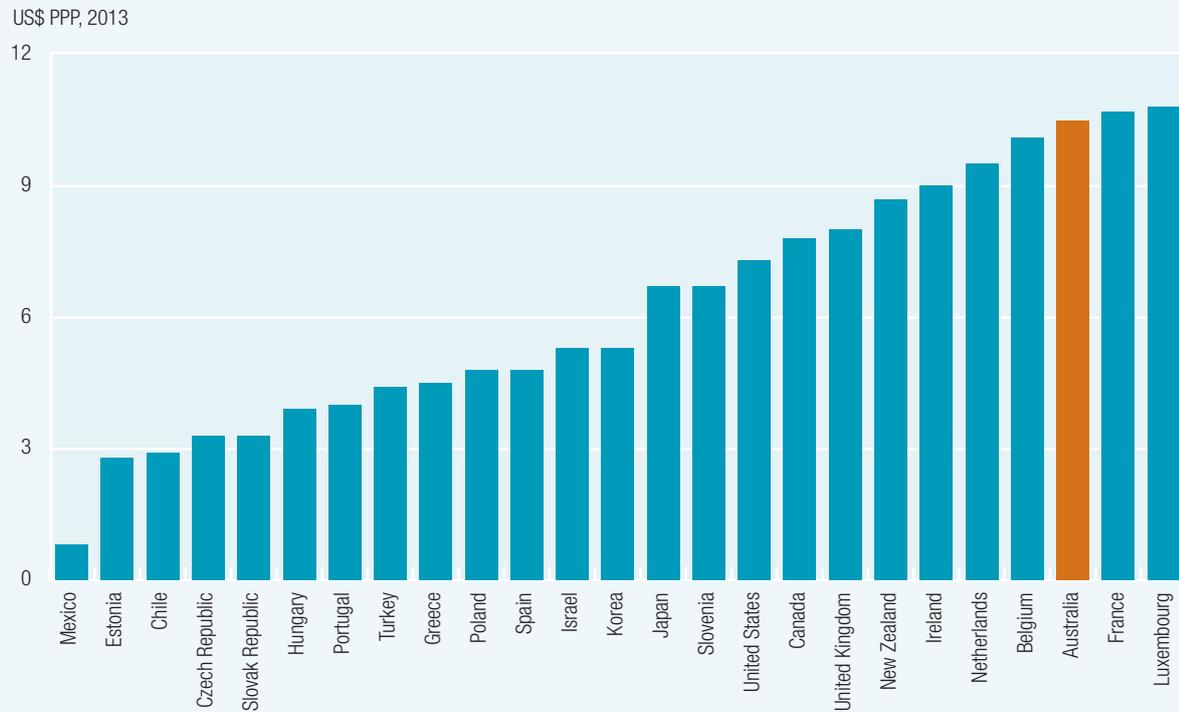
Analysis of the distribution of minimum wage earners by household income indicates that:

- *Minimum wage earners* reside most frequently in middle income groups. This is because many higher-income households have some family members (for example, dependent students) in low paid jobs.
- *Employees* in the lowest income groups are significantly more likely to be on the minimum wage than those in higher income groups. While most people in the lowest quintile are not in work (and therefore do not receive any wages), almost half of those who are in work are paid at a minimum rate.

Australia's national minimum wage is high by international standards, but has declined over the past decade

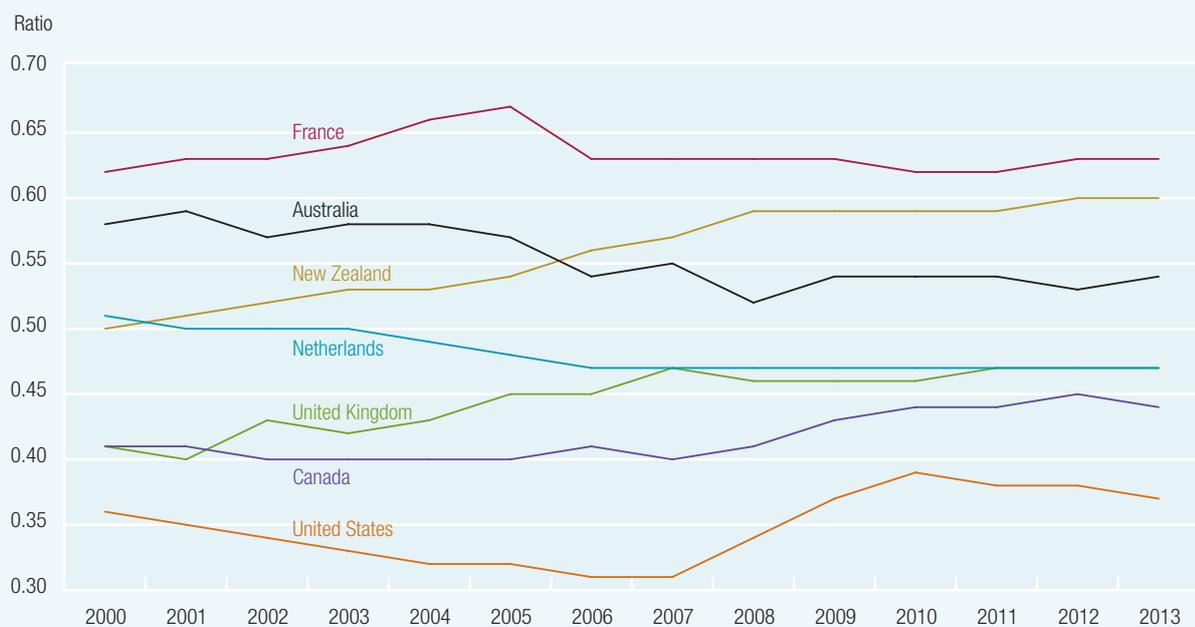
Minimum wage rates in OECD countries

\$US/hour PPP, 2013



Changes in adult minimum to median wages for several OECD countries

2000-2013



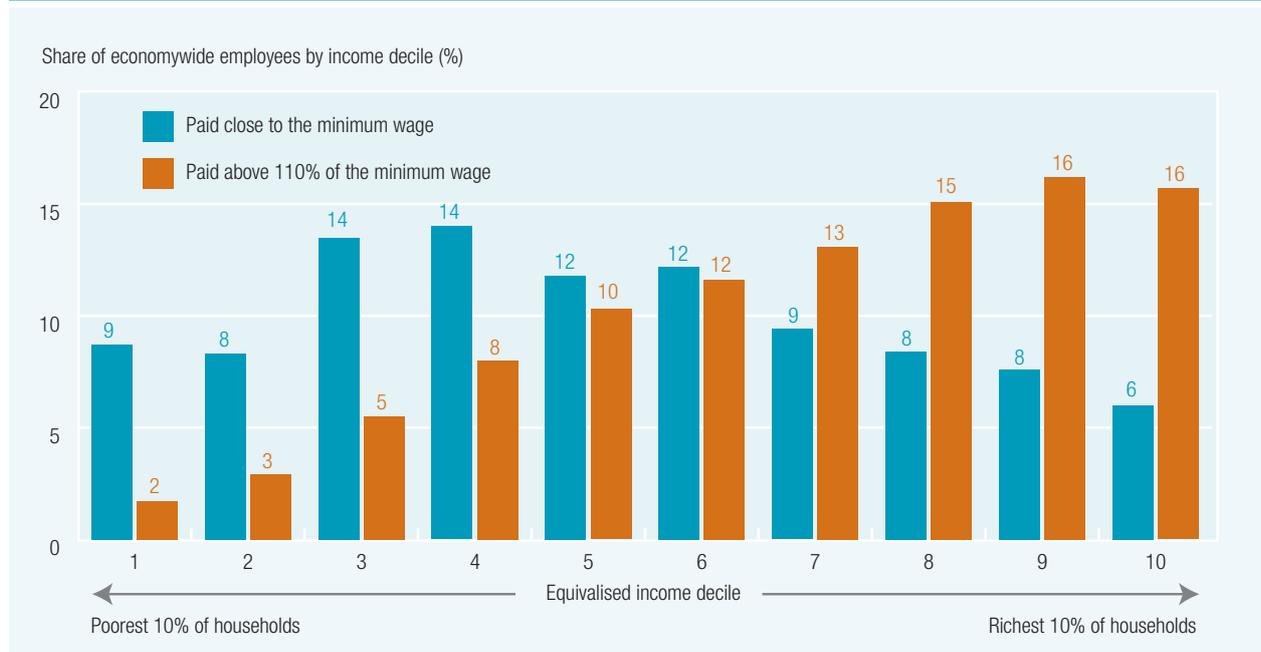
Data sources and notes: see Productivity Commission 2015, *Workplace Relations Framework*, Draft Report, figures 8.1 and 8.2.

Although many minimum wage workers do not reside in low-income households or work on the minimum wage for long, changes in minimum wages will affect the living standards of the lowest income households, though the extent of this depends largely on household structures. Single person working households with a part-time employee on the minimum

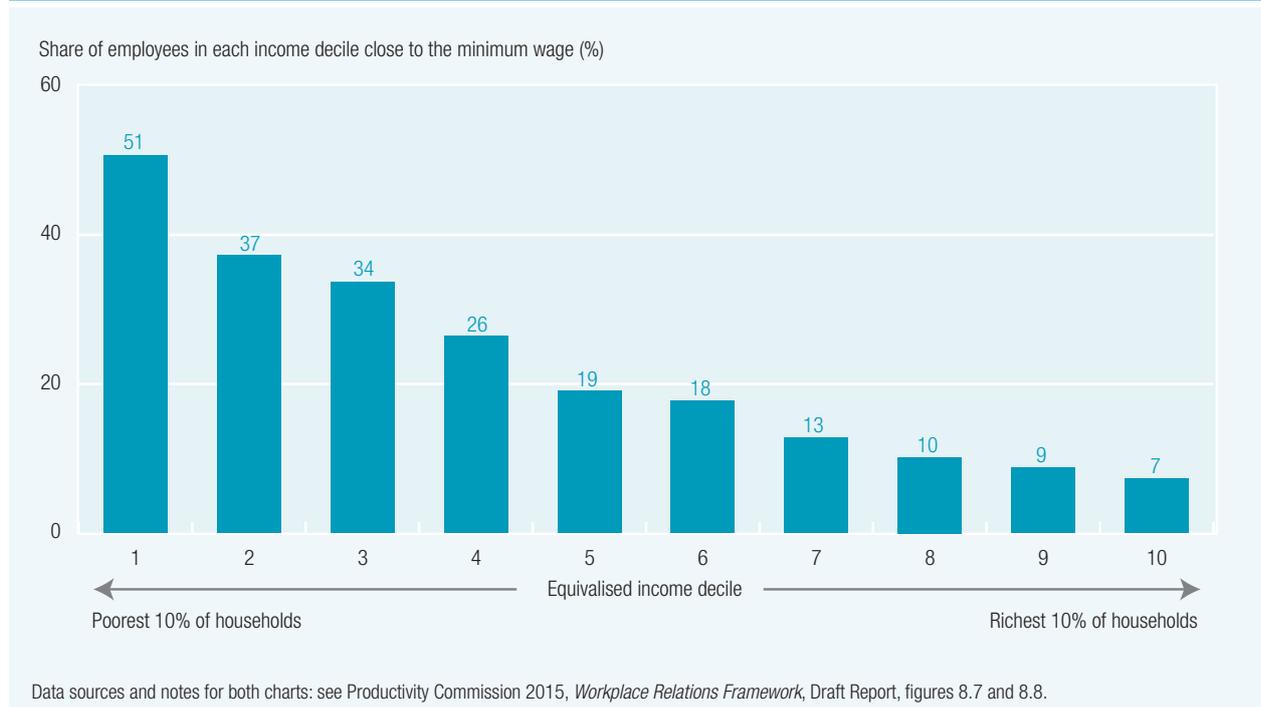
wage will be significantly affected, while working families in the lowest income groups receive considerable family benefits and other social security transfers, which partly shields them from the income effects of minimum wage movements.

The Productivity Commission considers that the FWC should give significant weight to employment impacts

Many people receiving wages around the minimum wage are from middle income households



But an employee in a low income group is much more likely to be paid around the minimum wage rate



Data sources and notes for both charts: see Productivity Commission 2015, *Workplace Relations Framework*, Draft Report, figures 8.7 and 8.8.

when determining the level of the minimum wage. The likelihood that minimum wages cause some dis-employment means that, in considering adjustments to minimum wages, there is a need to weigh up the potential benefits to low paid workers who retain their jobs (and/or hours) against the potential losses to those ‘would be’ employees who fail to gain employment, or experience greater underemployment or job loss, as a result. The greater the assessed risk and extent of such disemployment effects, the greater would be the case for constraining the growth of minimum wages or even reducing them. The FWC should also take into account uncertainties in forecasts of unemployment related to unexpected variations in economic circumstances, and the consequences for employment and household income of forecasting errors.

The Commission also sees scope for the FWC to enhance its approach to annual wage reviews including through more extensive use of evidence and research, more explicit recognition and measurement of the tradeoffs between the different elements of the minimum wage and modern awards objectives, and taking better account of the effects of determinations on all affected parties.

The draft report notes that a range of measures could be used to complement minimum wages. For example, many countries use earned income tax credits (EITCs) for this purpose. However, there are uncertainties about the feasibility, benefits and costs of some of these options.

Changes to the National Employment Standards

The National Employment Standards (NES) specify minimum requirements for 10 conditions of employment – including hours of work, various forms of leave and redundancy pay. Awards, enterprise agreements and employment contracts cannot exclude any elements of the NES, or provide less favourable employment conditions. The draft report notes that the NES as a whole have attracted little controversy, although there are concerns about the details of some elements.

The Commission’s draft recommendations include allowing employees to swap public holidays for another date if agreed with the employer, and ensuring that employers are not required to pay for leave for newly designated public holidays.

Repairing awards

Awards are the regulations that describe various floors on wages and conditions for a wide variety of skill levels across multiple industries. Awards are a longstanding part of Australia’s workplace relations framework, with

the FWC determining awards for more than 100 years. They are unique to Australia (and New Zealand until 1991)

The Commission found that awards have some undesirable inconsistencies and rigidities, but they are an important safety net and a useful benchmark for many employers. Nevertheless, there are strong grounds for improving the award system. Awards should be easier to understand and no more complex than they need to be. Awards should be in plain English and be written to avoid the mistakes and misunderstandings that arise from the present ambiguities of awards. The FWC should address specified troublesome hotspots on a thematic basis, rather than completely replace them. The four yearly award review process should cease.

Better aligning weekend penalty rates in some industries

The Commission does not recommend any changes to regulated penalty rates for shift, overtime and weekend work. However, in recent years, there has been intense debate about penalty rates for weekend work in the hospitality, entertainment, retailing, restaurants and cafes industries. Social trends and community norms have shifted so that in particular segments of the services sector – cafes, hospitality, entertainment, restaurant and retail industries – Sunday working is now inherent in the job. Australian society expects to be able to shop, go to a pharmacy, and eat at cafes and restaurants on weekends. Consequently, the workplace relations system should embrace the concept of 7-day weeks in the relevant services industries. Not doing so, imposes costs on the community that were not present when those norms and preferences were not widespread among Australians.

The draft report notes that rates for Sundays (usually around 200 per cent of base pay) are at odds with rates for times that are also important for social activities (evenings), and to an even greater degree for times that pose clearly demonstrated health risks (night shifts and rotating shifts). Evening/afternoon shift penalty rates can be as low as 10 per cent and night shift loadings as low as 15 per cent. Survey evidence shows that the overall social costs of daytime work on Sundays are similar to Saturdays, and consistently lower than evening work.

The Productivity Commission’s draft recommendation is that Sunday rates in the hospitality, entertainment, retailing, restaurants and cafes industries should be brought into line with Saturday rates, with a lag before any change occurs, allowing people to adjust their lives and working patterns.

Removing some flaws in enterprise bargaining

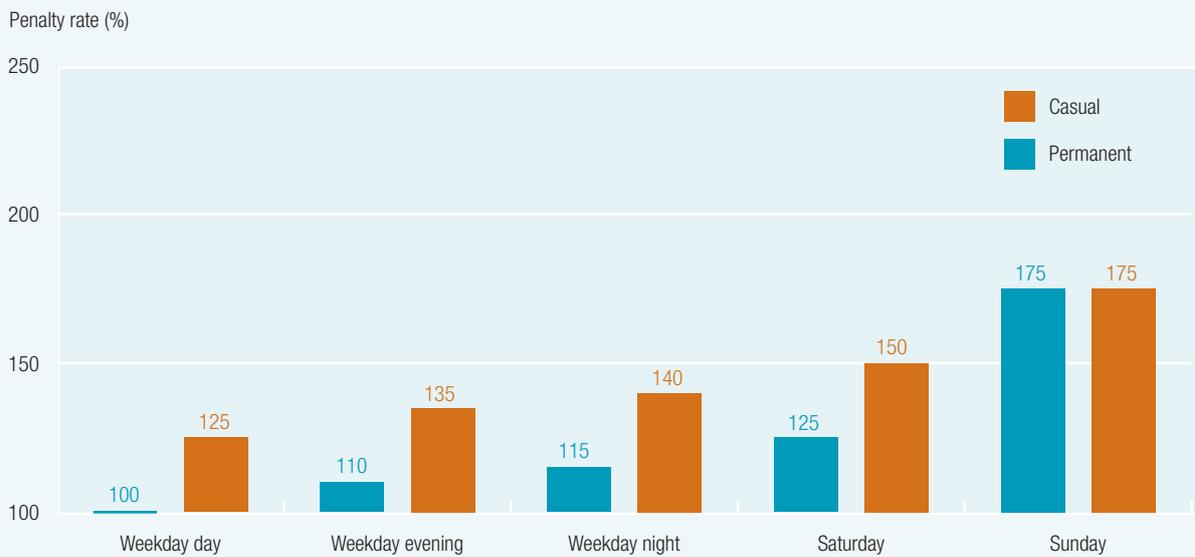
Following almost one century of centralised conciliation and arbitration, enterprise-level bargaining was introduced in Australia in 1993. Enterprise bargaining involves employees working together to reach an agreement with their employer over the terms and conditions of their employment. The Commission found that while enterprise bargaining is generally working

well, there are several flaws in the current arrangements, and it is often ill-suited to smaller enterprises.

- The application of the better off overall test (BOOT) is creating uncertainty during the bargaining process and at the agreement approval stage. The BOOT should be replaced by a no-disadvantage test, and the same test should be used for individual agreements.

Wage relativities by day and time of the week

Permanent and casual employees in the hospitality industry



The social 'disabilities' of working on Sundays are always less than evening work and sometimes less than Saturdays



Data sources and notes: see Productivity Commission 2015, *Workplace Relations Framework*, Draft Report, figures 14.8 and 14.10.

- Allowing parties to negotiate agreements with longer durations, up to five years, would reduce the costs associated with bargaining.
- Bargaining arrangements for greenfields agreements pose risks for large capital-intensive projects with urgent timelines. The rules around negotiation of greenfields agreements require modification to reduce inefficiencies and end stalemates in negotiations

Increasing the use of individual flexibility arrangements

Once an enterprise agreement is in place, individual flexibility arrangements (IFAs) can be made. IFAs allow individual employees and employers to vary an enterprise agreement to suit their circumstances. For example, IFAs can be made in relation to working hours and family-friendly work practices.

The Commission found that IFAs within enterprise agreements are underutilised. This is surprising because in principle they offer flexibility, provide protections for employees, and are not hard to make. In part, this reflects ignorance about the existence of IFAs. But there are perceptions (sometimes not well based) of defects that also constrain their use. These could be resolved, including by providing information on their use, extending the termination period of the arrangements and by moving to the no disadvantage test.

A new type of agreement – the enterprise contract

The Productivity Commission has floated the option of a new type of statutory agreement – the ‘enterprise contract’ – to fill the gap between enterprise agreements and individual arrangements. This would offer many of the advantages of enterprise agreements, without the complexities, making them particularly suitable for smaller businesses. Any risks to employees would be assuaged through a comprehensive set of protections, including the right to revert to the award (and maintain generic protections, such as those relating to unfair dismissals).

The enterprise contract would effectively amount to a collective individual flexibility arrangement, but with some further flexibility. Employers could offer it to all prospective employees as a condition of employment (resembling enterprise agreements, where new employees are covered by an existing agreement when they are hired). No employee ballot would be required for the adoption of an enterprise contract, nor would any employee group be involved in its preparation and

Where a staple can undo an agreement

A number of participants in the Commission’s inquiry argued that undue emphasis can be placed on the procedural requirements of enterprise bargaining.

Peabody Moorvale Pty Ltd provided three pages – stapled together – to all of its employees to be covered by a proposed enterprise agreement. Some bargaining ensued, an agreement was struck, and the agreement was lodged with the FWC. However, by attaching the three documents together, the employer contravened requirements about the form of notice to be given to employees. The FWC had no real discretion in the matter, and was obliged by the Fair Work Act to reject the agreement. So the employer had to recommence the agreement process. The Commission found a convincing variety of similar examples.

While there are often good reasons for imposing procedural requirements, substance rather than form should prevail. The FWC should have the discretion to overlook a procedural defect (that poses no risks to employees) without requiring an undertaking by the employer.

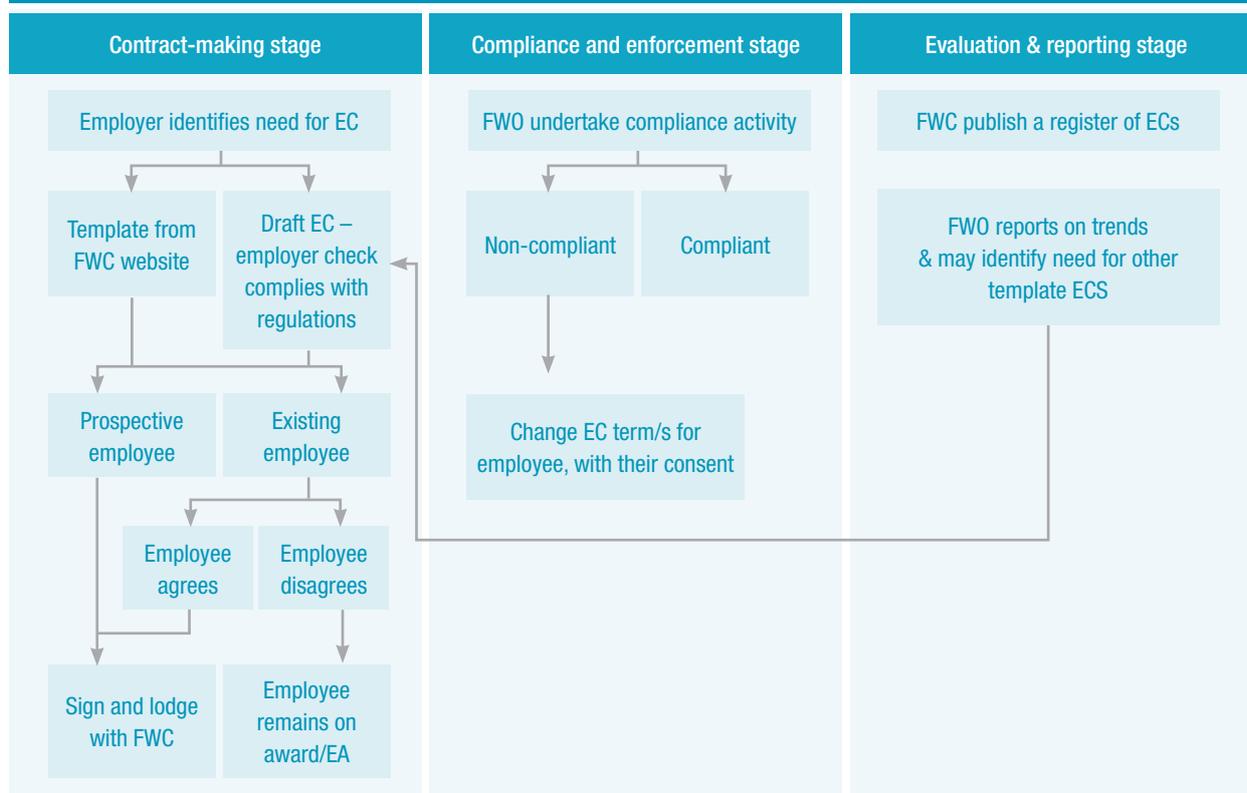
agreement unless the employer wished this to be the case. As in enterprise agreements, employers and individual employees could still negotiate individual flexibility arrangements as carve outs from the enterprise contract if they mutually agreed.

The Productivity Commission has sought information on the costs (including compliance costs) and benefits of the proposed enterprise contract to employers, employees and to regulatory agencies. It also welcomes any variations that would achieve the goals of this new contract type.

Other issues

The draft report contains analysis and draft recommendations on a range of other issues related to the WR framework. These include: unfair dismissal, anti-bullying, public sector bargaining, industrial disputes and right of entry, alternative forms of employment (independent contracting, labour hire, casual workers and out workers) and protections for migrant workers.

Making an enterprise contract



Workplace Relations Framework: Summary of key draft recommendations*

Institutions

The Fair Work Act should be amended to establish a Minimum Standards Division as part of the Fair Work Commission. This Division would have responsibility for minimum wages and modern awards. All other functions of the Fair Work Commission should remain in a Tribunal Division.

The Fair Work Act should be amended to stipulate that new appointments of the President, Vice Presidents, Deputy Presidents and Commissioners of the Fair Work Commission be for periods of five years, with the possibility of reappointment at the end of this period, subject to a merit-based performance review.

The Fair Work Act should be amended to change the appointment processes for Members of the Fair Work Commission. The amendments would stipulate that:

- an independent expert appointment panel should be established by the Australian Government and state and territory governments
- members of the appointment panel should not have had previous direct roles in industrial representation or advocacy
- the panel should make a shortlist of suitable candidates for Members of the Fair Work Commission against new eligibility criteria
- the Commonwealth Minister for Employment should select Members of the Fair Work Commission from the panel's shortlist, with appointments then made by the Governor General.

Minimum wages

In making its annual national wage decision, the Fair Work Commission should broaden its analytical framework to systematically consider the risks of unexpected variations in economic circumstances on employment and the living standards of the low paid.

Workplace Relations Framework: Summary of key draft recommendations...cont*

National Employment Standards

The Fair Work Commission should, as a part of the current four yearly review of modern awards, incorporate terms that permit an employer and an employee to agree to substitute a public holiday for an alternative day into all modern awards.

The National Employment Standards should be amended so that employers are not required to pay for leave or any additional penalty rates for any newly designated state and territory public holidays.

Penalty rates

Sunday penalty rates that are not part of overtime or shift work should be set at Saturday rates for the hospitality, entertainment, retail, restaurants and café industries.

The Fair Work Commission should, as part of the current award review process, introduce these new penalty rates in one step, but with one year's advance notice.

Enterprise bargaining

The Fair Work Act should be amended to allow the Fair Work Commission wider discretion to approve an agreement without amendment or undertakings as long as it is satisfied that the employees were not likely to have been placed at a disadvantage because of the unmet requirement.

The Fair Work Act should be amended to allow an enterprise agreement to specify a nominal expiry date that:

- can be up to 5 years after the day on which the Fair Work Commission approves the agreement, or
- matches the life of a greenfields project.

The Fair Work Act should be amended to replace the better off overall test for approval of enterprise agreements with a new no-disadvantage test. The test should be applied across a like class of employees for an enterprise agreement. The Fair Work Commission should provide its members with guidelines on how the new test should be applied.

The rules around greenfields agreements in the Fair Work Act should be amended so that bargaining representatives for greenfields agreements are subject to the good faith bargaining requirements.

The Fair Work Act should be amended so that if an employer and union have not reached a negotiated outcome for a greenfields agreement after three months, the employer may request that the Fair Work Commission undertake 'last offer' arbitration of an outcome by choosing between the last offers made by the employer and the union.

Individual arrangements

The Australian Government should amend the Fair Work Act to introduce a new 'no-disadvantage test' to replace the better off overall test for assessment of individual flexibility arrangements.

The Fair Work Ombudsman should develop an information package on individual flexibility arrangements and distribute it to employers, particularly small businesses, with the objective of increasing employer and employee awareness of individual flexibility arrangements.

** A complete list of draft recommendations, and requests for further information, are available in the report overview.*

Workplace Relations Framework

> Draft Report

> Released August 2015

Superannuation policy for post-retirement

As part of a research series on policy issues that arise from population ageing, the Commission has completed a research report on two important elements of the retirement income landscape – when and how people access their superannuation.



The Commission examined what might happen if the age that people can access their superannuation – the preservation age – were gradually increased from 60 to 65 years. Modelling undertaken to better understand the impacts of such a change suggested that, in 2055:

- there would be a modest increase in the workforce participation of older workers of around 2 percentage points – mainly among those with higher wealth at or near retirement
- households that delay their retirement would likely do so by around two years and would have superannuation balances around 10 per cent larger in real terms when they retire
- there would be an indicative annual fiscal improvement of around \$7 billion – mainly due to more tax revenue from wealthier households.

Changing the preservation age would have little, if any, impact on the many older Australians who retire involuntarily. Currently, almost one half of men and around one third of women who retire between the ages of 60 and 64 do so involuntarily.

While the report has assessed the likely impacts of raising the preservation age, important implementation

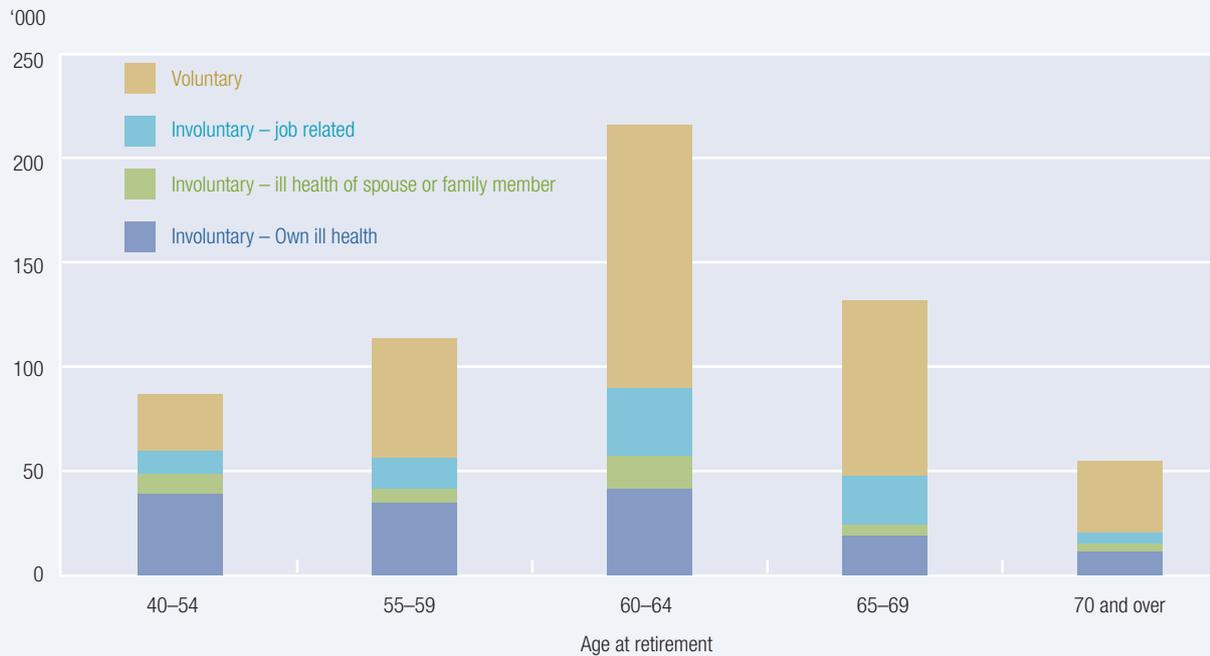
issues would need to be considered and resolved before any changes are made. For example, an appropriate safety net for those who become involuntarily retired would be a priority.

In examining how people draw down their superannuation, the Commission also found that most retirees are prudent. While the use of lump sums attracts much attention, the suggestion that their use is problematic is not supported by the available evidence. Less than 30 per cent of superannuation benefits are taken as lump sums, with most superannuation benefits taken as income streams. Where lump sums are taken, they are most frequently used to pay down debt, invest in income stream products, and purchase durable goods that are used throughout retirement.

In undertaking its analysis, the Commission identified a number of features of the retirement income system that warrant more detailed analysis, and highlighted that there would be merit in a holistic review of retirement income policy. Such a review would need to be informed by community consultation, so that any changes to the system could cater for the diverse circumstances of retirees.

A significant number of older Australians retire involuntarily

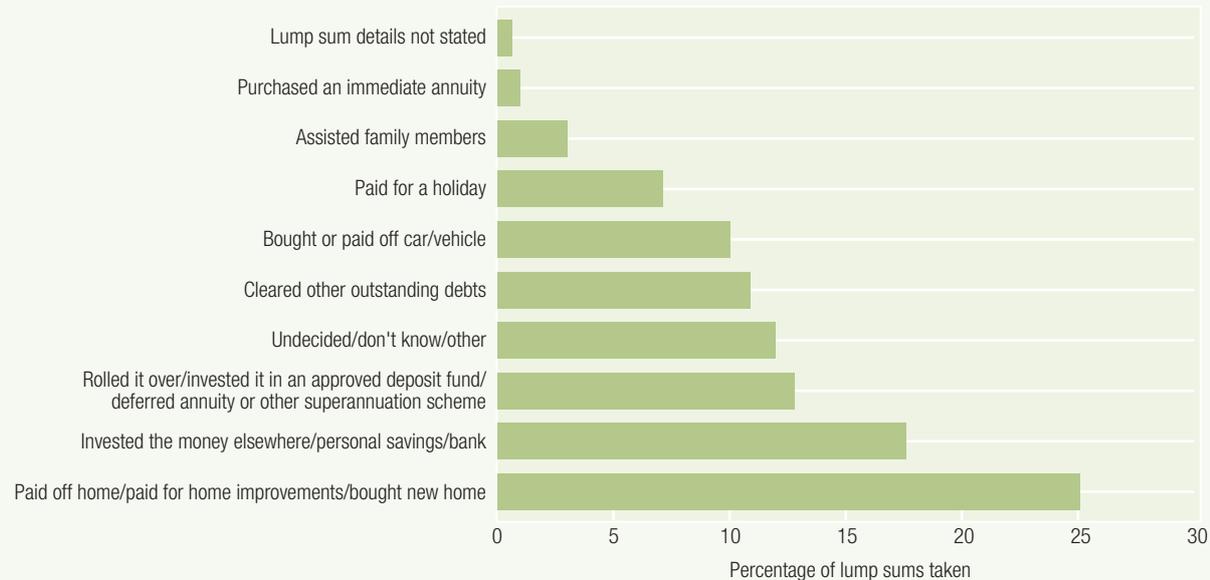
Number of people retiring, by age group and reason for retirement, 2011



Data sources and notes: Productivity Commission 2015, *Superannuation Policy for Post-Retirement*, Commission Research Paper, figure 3.2.

There is little evidence that lump sum benefits are being squandered

Main uses of superannuation lump sums, 2012-13



Data sources and notes: Productivity Commission 2015, *Superannuation Policy for Post-Retirement*, Commission Research Paper, figure 4.9.

Superannuation Policy for Post-Retirement

> Productivity Commission Research Paper

> Released July 2015

International education services

International students make a significant economic and social contribution to Australia. However, a recent Commission Research Paper identifies a number of risks to the sustainability of Australia's international education sector.



The global market for education services is expanding as incomes and participation in education in emerging economies continue to rise. Australia is an attractive destination for international students at all levels of education. There is also a high demand for Australian education providers delivering courses abroad.

Following a period of rapid growth in the international education sector from 2007 to 2009 – partly

driven by the direct pathway from the student visa program to permanent skilled migration – the sector experienced a major downturn from 2009 to 2011. The high Australian dollar, the global recession, the introduction of a series of visa integrity measures, negative publicity about student safety in Australia, and uncertainty about college closures were key contributing factors.

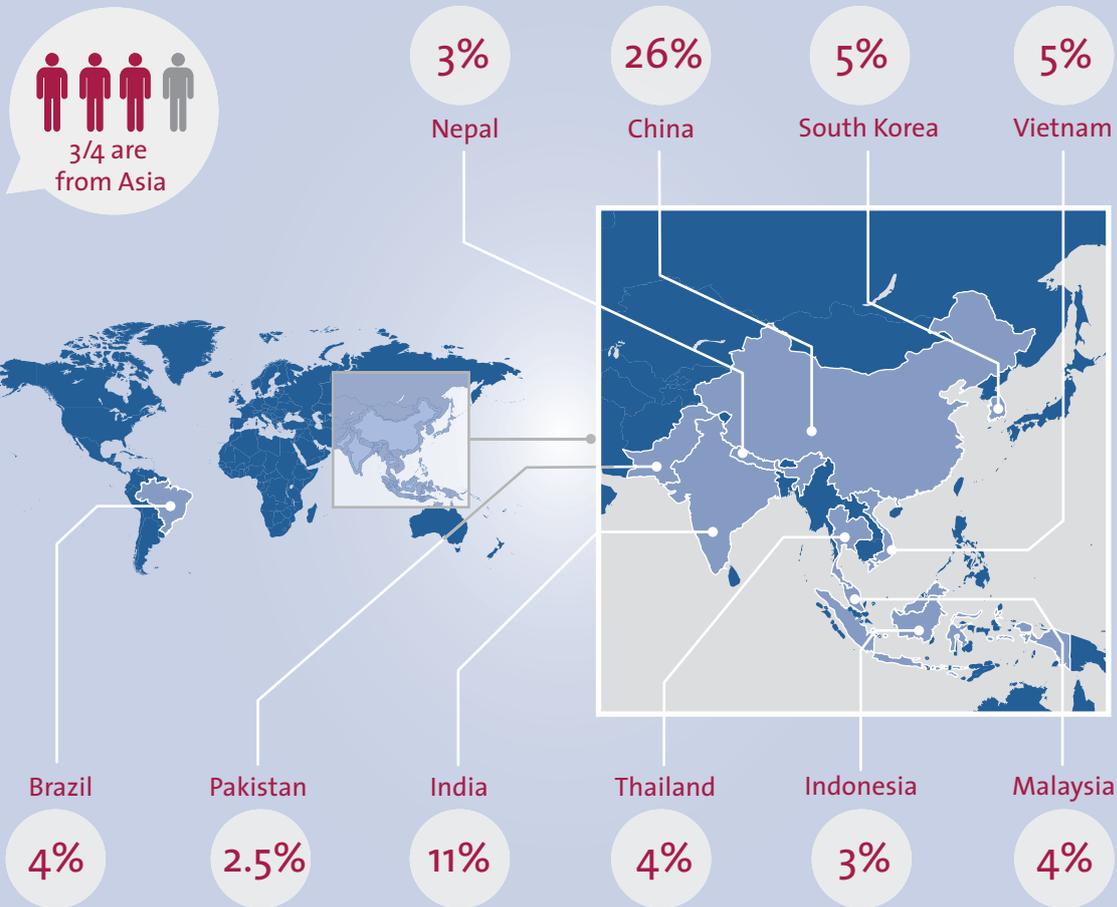
The sector has since recovered from this decline and

International students in Australia

- International education services contributed \$17 billion to the Australian economy in 2014.
- Around half of this was from fees paid to educational institutions, with the remainder from expenditure on goods and services by international students living in Australia.
- The sector represented about 27 per cent of services exports and close to 5 per cent of total Australian exports.
- In 2014, there were over 450 000 international students onshore, representing around 20 per cent of higher education students and 5 per cent of students enrolled in vocational education and training.
- Around three quarters of all international students enrolled in Australia in 2014 were from Asia, with China and India accounting for 37 per cent of all international students (26 and 11 per cent respectively).
- Of the 160 000 enrolments in courses delivered offshore, more than two thirds were in the higher education sector.

Where are Australia's international students from?

Australia's top 10 source countries, 2014



is back on a high growth trajectory. In 2014, the number of international students in Australia increased by more than 10 per cent on 2013 levels and education related exports also grew by a similar rate.

A number of factors contributed to this rebound. These include the introduction of an expansionary student visa policy through streamlined visa processing (SVP), post study work rights, and improved economic conditions following the global financial crisis.

Competitive pressures are intensifying

The four leading English speaking destination countries – the US, the UK, Australia and Canada – dominate the global market for the provision of international education services (IES), with market shares of 16, 13, 6 and 5 per cent respectively. While the US remains the top destination for international students, Australia

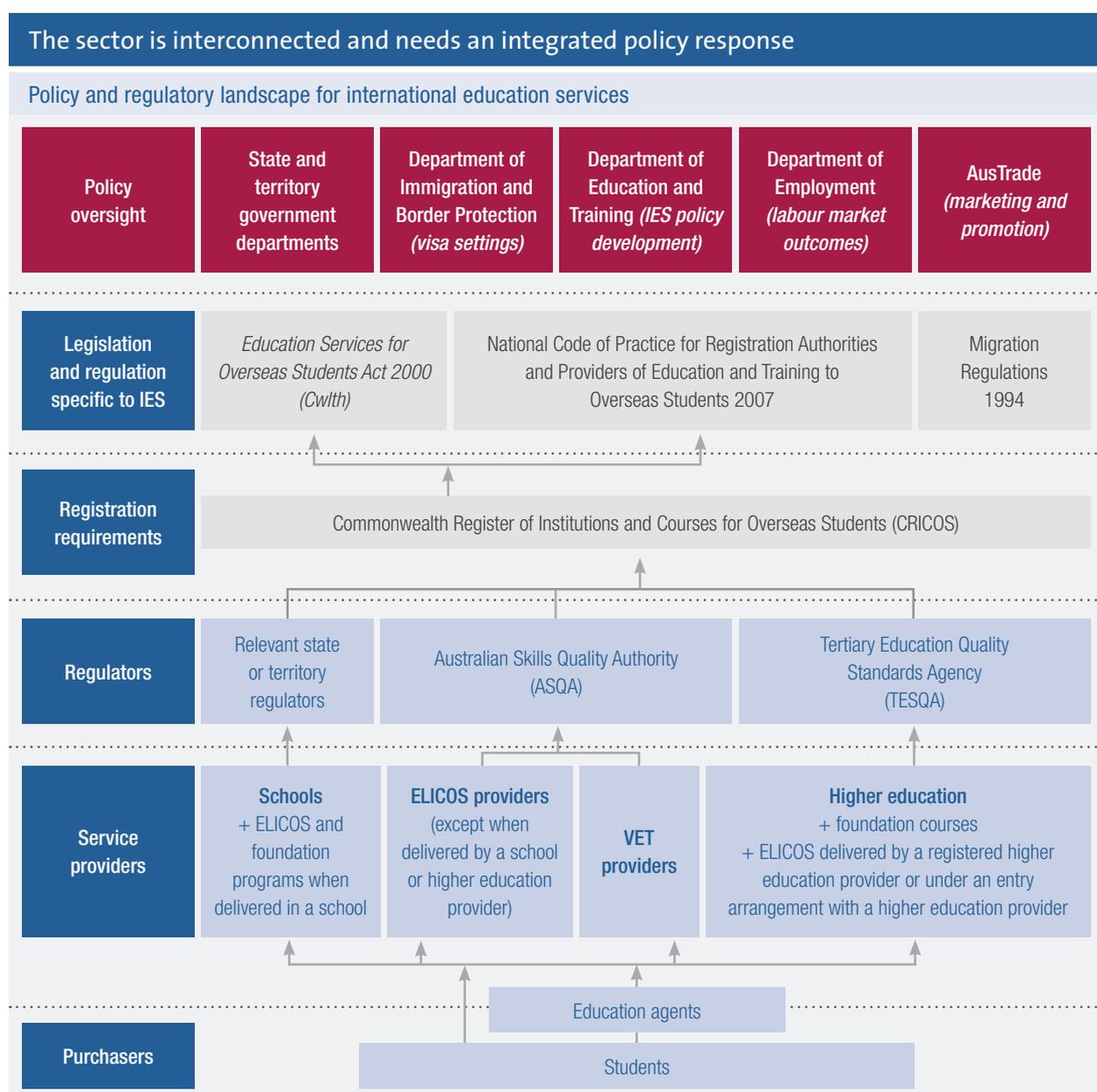
and the UK have the highest concentration of international students in total national tertiary enrolments. International students as a proportion of total tertiary enrolments within Australia grew from 14 per cent in 1999 to 18 per cent by 2013. In the UK, the comparable share grew from 11 to about 18 per cent. International tertiary students as a proportion of total enrolments in the US has remained around 3 per cent over the period 1999 to 2012.

In parallel with the growth in demand for international education, competition in the provision of international education is increasing globally. Many of the 'traditional' providers of IES are extending their international reach through the delivery of courses offshore. Further, many countries in Asia and in the Middle East are seeking to develop world-class capacity in higher education and research, and are investing heavily in higher education systems.

Whether Australia remains an attractive destination for overseas students will depend on how well education providers respond to students' expectations for their learning experience and provide a value proposition as technology and business models evolve. The Commission report finds that the sustainability of international education is closely linked to regulatory settings around the quality of education and student visas.

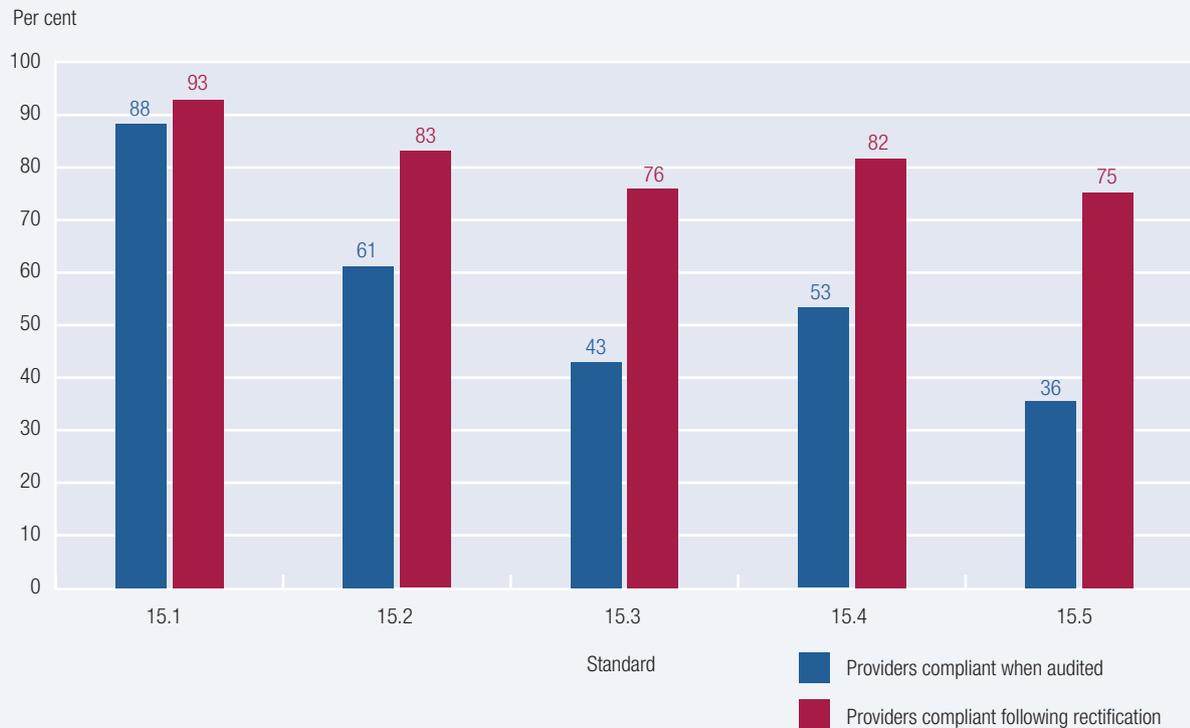
Education quality regulation is a 'work in progress'

The quality and reputation of Australia's education services rank highly as a determinant of student demand. Australia has a specific regulatory framework aimed at providing quality assurance and consumer protection for education services supplied to international students. This complements the regulatory framework that applies to the provision of domestic education services. Two national regulators were established in 2011 – the Tertiary Education Quality Standards Agency (TEQSA) and the Australian Skills Quality Authority (ASQA).



There are ongoing risks to the quality of some services provided by VET

Compliance with standard 15^a found at audits of providers registered under CRICOS^b to deliver VET



^a S. 15.1 – Continuous improvement of training and assessment, S. 15.2 – Training meets the requirements of the training package, S. 15.3 – Required staff, facilities, equipment and material, S. 15.4 – Qualified and competent trainers and assessors, S. 15.5 – Assessment is undertaken properly.

^b Commonwealth Register of Institutions and Courses for Overseas Students.

Source: See Productivity Commission 2015, *International Education Services*, figure 4.3

Stakeholder concerns about the quality of IES appear to be mainly confined to some segments of the VET sector. These concerns stem partly from experience (namely, the emergence of poor-quality providers in the 2007-09 boom years) and partly from the nature of the sector (relative to the higher education sector), specifically:

- the larger number of providers (around 500 registered to offer courses to international students, compared with 133 in higher education)
- the prevalence of small scale operations and relatively short duration courses
- lower barriers to entry and exit for providers.

Education providers' compliance with regulations aimed at managing risks to the quality of education services has improved in recent years. Providers also seem responsive to regulatory intervention. However, ongoing risks to the quality of education services offered by some VET providers remain. In June 2014, ASQA reported that 33 per cent of all registered training organisations were rated as having a medium or high risk of their not complying with the relevant legislative obligations.

A rebalancing from teaching to learning standards is required

To be registered as a higher education provider or a training provider, organisations must satisfy standards related to provider characteristics and governance, qualification, information, and the quality of teaching and learning. Within the teaching and learning standards category, the current quality assurance frameworks used by TEQSA and ASQA focus on input-based or teaching standards, such as the quality of teaching and the availability of supporting infrastructure.

Such standards are valuable as leading indicators of quality. However, given that student achievement is the ultimate goal of education, outcome-based or learning standards such as the demonstration of generic and discipline-specific learning objectives (including competency in the English language), are equally important from a quality assurance perspective. The Commission report argues that the current emphasis on teaching standards should be rebalanced to provide for learning standards to have a greater role in quality assurance arrangements.

Better information to inform student choice

Information on courses for international students is available through various web portals hosted by government agencies, individual institutions, industry bodies and education agents. While providers are required to supply students with information that will enable them to make informed decisions about their studies in Australia, national regulators are not required to make public other information that would assist students to make comparisons *between* providers.

The current regulatory regime also provides no publicly available information on the relative quality of education services offered by providers, or measures of comparative education outcomes such as completion rates or the distribution of levels of attainment for students completing their studies.

The availability of such information would offer greater transparency about the comparative 'quality' ranking of providers and would benefit prospective students – both domestic and international. It would help counteract misleading information provided to international students by education agents, and may strengthen the incentive for individual providers to improve the quality of their education services.

The use of education agents is extensive and risky

Education agents are usually located offshore and work on behalf of a wide range of institutions across different countries, although agents also operate domestically. They identify prospective students for Australian institutions (and institutions in other countries), provide students with information about courses, education providers and the features of living and studying in Australia (and other countries), assist students with enrolment applications (and visa applications where qualified), and sometimes collect course fees on a provider's behalf.

Educational institutions in Australia use agents extensively for recruiting international students, more so than in other comparable countries. And, on average, Australian institutions tend to pay higher commissions to agents relative to other countries. Commissions paid on a per student basis on admission create incentives for agents to maximise the volume of international students, with little regard to the quality of the advice provided to students (affecting student expectations) or the quality and aptitude of the students.



Education agents can play a useful advisory and intermediary role for international students and can be a cost-effective option for institutions looking to recruit students across a range of countries (at least in the short-term). However the Commission received considerable anecdotal evidence that suggested unscrupulous behaviour of agents is an issue.

Like several other countries, Australia does not regulate education agents directly. The lack of a system for tracking agents and their clients' outcomes, the lack of transparency about provider-agent relationships, and the offshore location of many agents make the oversight of the conduct of agents challenging. The Commission report suggests ways to mitigate these risks, including through internalising the risk and reducing the reliance on agents for recruitment through:

- a more direct recruitment approach by flagship Australian education institutions targeted to the higher end of the value chain
- greater transparency around the relationships between agents and providers
- data systems that allow agent conduct and performance to be tracked over time
- the provision of training and information exchange programs.

International Education Services

- > Productivity Commission Research Paper
- > Released April 2015

Realising the opportunities to export services

The Commission has proposed steps that Australian governments should take to reduce barriers to service exports.

The opportunities for Australian service providers to participate in international trade are greater than ever before. Global demand for services is increasing due to rising household incomes, particularly in some countries in Asia. Services are also becoming increasingly important to global value chains.

Reflecting the growing opportunities to export services, the Australian Government asked the Commission to conduct a study into barriers to growth in Australian service exports focusing on six services sectors (the tourism, education, financial, professional, information technology and health sectors). The draft report was released in August 2015.

The study focuses on identifying policy relevant barriers that affect Australian service exports. A barrier is anything that *unnecessarily* impedes the ability of businesses to export services. This definition recognises that there may be a legitimate rationale for government involvement in markets to address a market failure or to meet an equity objective.

The Commission identified a number of policy and regulatory barriers to service exports – both in Australia and overseas – that are preventing Australian service providers from realising the full opportunities from international trade.

On the domestic front, the priority for the Australian Government should be policy reform that promotes competition and provides incentives for domestic firms, including in services sectors, to innovate and lift their productivity. A flexible and productive economy can enable all sectors of the economy, including service providers, to respond to market opportunities in Australia and in international markets.

The Commission also identified domestic reforms to reduce barriers to service exports.

- The Australian Government is reforming short-term visitor and education visa processing arrangements. The reforms will address shortcomings of the current arrangements while maintaining immigration integrity and could help to facilitate the entry into Australia of short-term visitors and international students.
- Further liberalising air services arrangements would promote competition and encourage airlines to reduce their costs, innovate and expand services. Liberalising air services arrangements would be

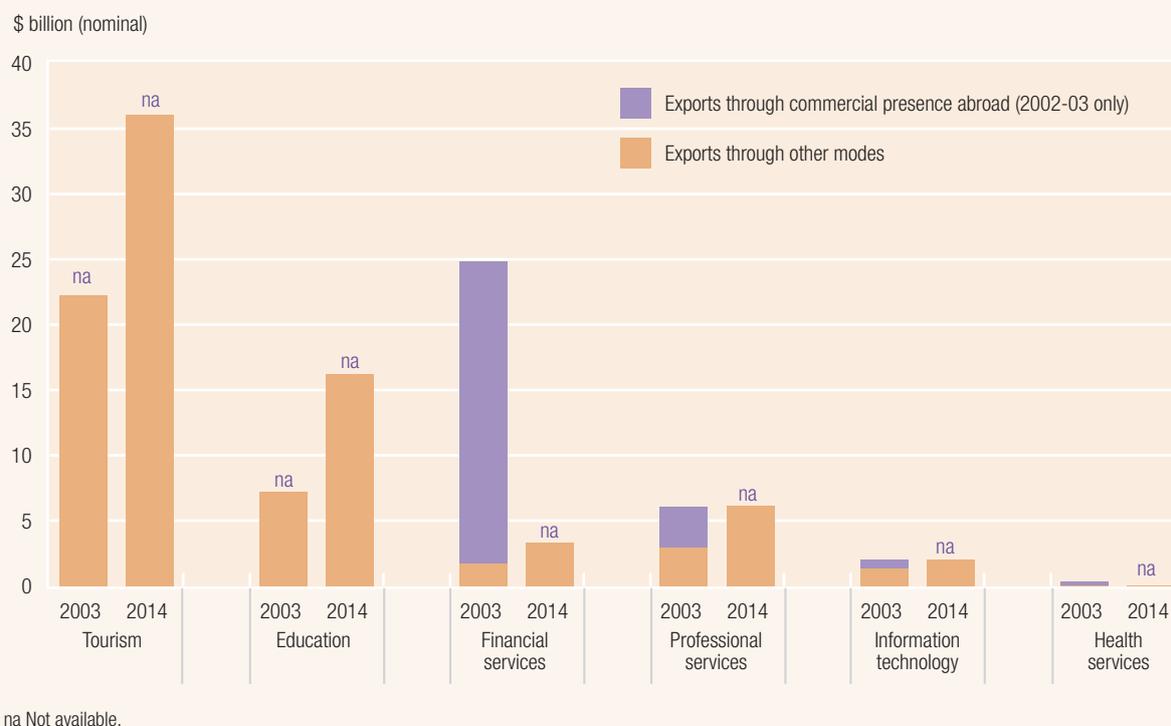


expected to promote greater service exports in service sectors where providers rely on face-to-face delivery of their service.

- Australia's system of withholding taxes is complex, with various exemptions and special rates applying to different types of investment. Simplifying the system would reduce investment distortions, which affect the demand for financial service exports.

Australian exports by services sector

2002-03 and 2013-14



Withholding taxes should not be lowered simply to match the rates in other jurisdictions – domestic policy settings should be based on broader community welfare considerations.

- Reforming policy arrangements underpinning infrastructure investment could help to address concerns about the adequacy of education and tourism infrastructure. Proposed reforms include implementing best practice project selection processes for public infrastructure projects and the ongoing review and reform of development approval processes that apply to private and public infrastructure.

On the international front, there are a range of mechanisms for addressing barriers to service exports, including mutual recognition agreements (MRAs) and international trade agreements. Some study participants considered that trade agreements are a necessary precursor to facilitating service exports, but highlighted that some barriers have persisted even where Australia has signed an agreement. A clear lesson that emerges is that no one mechanism will be sufficient to address international barriers to services trade.

The Commission identified key areas for international negotiations where barriers are imposing costs on Australian service providers. Service providers that

rely on setting up operations overseas to export their services – such as the financial service providers – are heavily influenced by international barriers.

- The increased use of digital technologies to trade services has seen governments impose restrictions on the flow of data across their borders. Data restrictions can force businesses to invest in data centres that cost tens of millions of dollars, or develop costly workarounds. Removing unnecessary data restrictions would benefit a range of service providers, with the greatest benefits likely to accrue to financial service providers. Some countries with data restrictions have large and growing demand for financial services, including China, Malaysia and Singapore.
- Some countries have overly burdensome licensing and standards regulations that go beyond what is required to address legitimate policy objectives. In India foreign lawyers may be admitted as a local lawyer only if they are an Indian citizen, and in some countries in Asia accountants need to be living in the country to provide services.
- Investment barriers can prevent Australian service providers from entering particular export markets or impose costs through constraining how service providers operate. For example, foreign equity limits

are considered the primary barrier to accessing Asian banking markets, and the provision of accounting services using a foreign affiliate is not permitted in India. Mandatory joint ventures in China can impose substantial costs where they impose a non-preferred business model.

While reducing barriers to service exports could deliver significant benefits to the Australian

community, increasing service exports is not a goal in itself. For example, while the financial sector faces burdensome barriers to service exports, Australian governments should not introduce reforms simply to increase the international competitiveness of financial service providers. Increasing service exports should only be pursued where it is expected to deliver net benefits to the community.

Service Exports: summary of the Commission's draft recommendations*

Some priorities for domestic reform

Governments should pursue sound policy settings that promote competition and a flexible and productive economy. Government actions should address concerns about infrastructure acting as a constraint to service exports.

The Australian Government should make screening thresholds for examination of investment proposals by the Foreign Investment Review Board consistent across investors from different countries.

The Australian Government should remove the priority afforded to specific industries under the Industry Skills Fund.

Opportunities to grow financial services exports

The Australian Government should continue to progress the Asia Region Funds Passport and encourage other jurisdictions to participate in the Passport.

The Australian Government should simplify Australia's regime of withholding taxes..

Enhancing export capacity in education and health

The Department of Education and Training should review the effectiveness of the Quality Indicators for Learning and Teaching online platform in meeting its proposed objective.

The Australian Government should examine the relationship between the use of online education by international students studying in Australia and student visa non-compliance to inform options for enabling more innovative and flexible approaches to delivering education services.

Removing impediments to tourism exports

The Australian Government should liberalise air services arrangements in Australia's major gateway cities.

Reducing international barriers to service exports

The Australian Government should put in place a framework for developing and implementing mutual recognition arrangements as part of, or following, the inclusion of mutual recognition provisions in trade (or other) agreements.

The Australian Government should seek to ensure that measures restricting cross-border data flows are the least restrictive necessary to address privacy or security objectives, and are only applied where other remedies could not achieve the same objective at a lower net cost.

** A complete list of draft recommendations are available in the report overview.*

Service Exports

> Draft Report

> Released August 2015

Reforming funding arrangements for natural disasters

The Commission recently recommended a major restructure of Australia's natural disaster funding arrangements. This would boost Australian Government funding for disaster mitigation while giving states and territories greater autonomy and responsibility for recovery.

Natural disasters have a major impact on Australia's economy, environment and communities. Since 2009, bushfires, floods and cyclones have claimed over 200 lives and destroyed more than 2600 houses. Although there is little evidence of changes in the pattern of these disasters in the past 40 years, their economic impact has risen, broadly in line with growth in population and the value of assets in risky areas (see figure). These disasters have had a financial impact on governments through the costs of repairing damaged public infrastructure and providing support to affected communities.

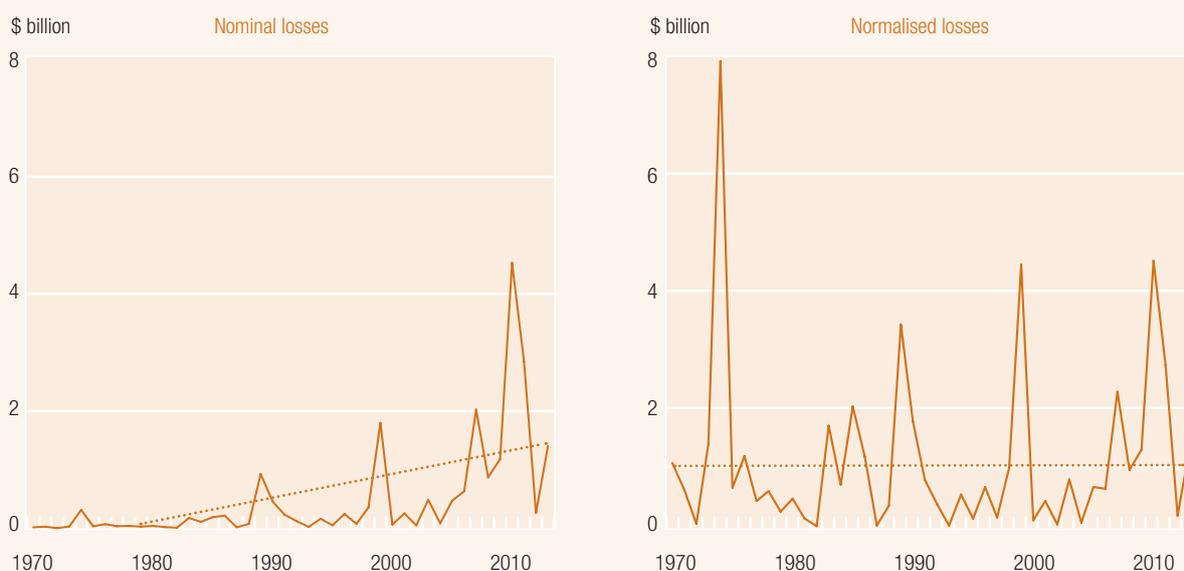
Most natural hazards are unavoidable, but their consequences can be managed. Yet there are widely held concerns that governments spend too much on recovery and do not do enough to mitigate disasters, raising the costs to the community when disasters strike.

Reflecting these concerns, the Australian Government asked the Productivity Commission to conduct an inquiry into the effectiveness and sustainability of Australia's natural disaster funding arrangements. The report was released in May 2015.

Commonwealth–state funding

State and local governments are responsible for most infrastructure and service delivery, and thus for managing the risks of natural disasters. The Australian Government provides financial support to the states and territories through the Natural Disaster Relief and Recovery Arrangements (NDRRA). It funds up to 75 per cent of the costs of disaster relief and recovery, above a given threshold.

Insurance losses from natural disasters^a



^a 'Normalised' losses are losses that would have occurred if past natural disasters were to happen in 2011. They are calculated by adjusting nominal losses for inflation and changes in population, wealth and building standards in cyclone prone areas.

The Commission's recovery funding model

Cost sharing	50 per cent of above-threshold costs
Annual expenditure threshold	0.45 per cent of total state government revenue
Small disaster criterion	\$2 million, indexed over time
Provision of funding	Essential public assets – assessed damages and benchmark prices Community recovery – reimbursement model, transitioning to untied grants based on assessed recovery costs
'Top-up' fiscal support	Actuarially fair premium for states to purchase a lower small disaster criterion or threshold, or higher cost-sharing rate

While the NDRRA provide an important fiscal 'safety net' to the states, the arrangements also influence the incentives states have to manage risks. A major problem is that the arrangements are highly prescriptive, with funding only provided to restore assets to their pre-disaster standard. This makes it difficult for state and local governments to rebuild assets in a way that improves resilience to future disasters ('betterment'). By subsidising recovery, the arrangements can also discourage states from undertaking mitigation or taking out insurance.

To address these problems, the Commission recommended a new funding model that would give state and local governments greater autonomy in how they spend recovery funding. Funding to restore public infrastructure would be provided based on upfront estimates of damages and 'benchmark prices', with states having more flexibility in their expenditure decisions. The Australian Government would also cover half the additional costs of betterment to make assets more resilient, provided adequate asset management plans are in place.

At the same time, the Australian Government's marginal cost sharing rate would be limited to 50 per cent and the expenditure thresholds that determine when it will contribute to a state's costs would be raised. This would better align with relative fiscal capacity in the federation.

Reimbursement for community recovery activities – including counter disaster operations and personal hardship relief – would also be rationalised. Australian Government funding would move towards a system of untied grants to give states greater flexibility to respond to local needs. In addition, eligibility criteria for the Australian Government Disaster Recovery Payment would be legislated to reduce ministerial discretion, with the amount reviewed to reflect immediate relief needs.

The Commission also found that governments underinvest in mitigation that would reduce the impact of natural disasters in the first place. It recommended that the Australian Government increase its mitigation funding to the states to \$200 million per year, allocated to jurisdictions on the basis of natural disaster risk. This would be conditional on states matching funding and adopting best-practice arrangements for selecting mitigation projects.

Other policy areas

The Commission also examined policy areas that influence the community's exposure and vulnerability to natural disasters. It found that governments, insurers and others have improved the accuracy and availability of natural hazard information, but more can be done. Governments should work together to develop guidelines for future natural hazard modelling and mapping. They also need to release more of the data they hold and give greater thought to how to disclose risk information to the community. Insurers have a role to play too, by providing better information to their customers on natural hazards and indicative rebuilding costs.

There is also room for state and local governments to better consider natural disasters in their land use planning. While planning usually only affects new properties, it can have a major long-term influence on the community's exposure to natural disasters. States can do more to help local governments to better incorporate natural disaster risk into their decisions by providing better guidance and limiting their legal liability for actions taken in 'good faith'. Local governments could make greater use of private funding sources to recover the costs of disaster mitigation from the beneficiaries, especially in high risk areas of existing settlement.

Natural Disaster Funding Arrangements: Summary of the Commission's key recommendations*

Funding arrangements for recovery

The Australian Government should fund natural disaster recovery by:

- cost sharing with state and territory governments at a rate of 50 per cent above an annual expenditure threshold
- providing funding based on assessed damages and benchmark prices
- providing an option for states to purchase 'top up' fiscal support at an actuarially fair price.

This funding would be triggered where an annual threshold of 0.45 per cent of state government revenue is met, with a small disaster criterion of \$2 million applied to events at the state level. There should also be a transparent mechanism for exceptional circumstances support.

Funding arrangements for mitigation

The Australian Government should increase the amount of annual mitigation funding it provides to the states to \$200 million, conditional on states matching funding and adopting best practice project selection.

Transparency and accountability

The Australian Government should publish estimates of future costs of natural disasters in its budget, and provision for a base level of natural disaster expenditure in the forward estimates.

States should be required to report on: published risk assessments; transparent natural disaster liabilities in state budgets; asset registers and asset management plans at the state and local level that incorporate natural disaster risk; implementation of the *Enhancing Disaster Resilience in the Built Environment Roadmap*; and effective mechanisms to identify and prioritise mitigation spending.

Managing shared risks

The Australian Government should legislate the current eligibility criteria for the Australian Government Disaster Recovery Payment, remove Ministerial discretion, and review the amount provided so it is more reflective of immediate emergency relief needs.

Information

Governments at all levels should make new and currently held natural hazard data publicly available in accordance with open public sector information principles.

State and local governments and insurers should explore opportunities for collaboration and partnerships.

Governments should support the development of guidelines for the collection and dissemination of natural hazard mapping, modelling and metadata.

Built environment

States should clearly articulate their statewide natural hazard risk appetite in land use planning policy.

States should provide their local governments with statutory protection from liability for releasing natural hazard information and making changes to local planning schemes where such actions have been taken in 'good faith'.

Insurance

State taxes and levies on general insurance should be phased out and replaced with less distortionary taxes.

Insurers should provide additional standardised information to households regarding their insurance policies, the natural hazards they face and indicative costs of rebuilding after a natural disaster.

* A complete list of draft recommendations are available in the report overview.

Natural Disaster Funding Arrangements

> Inquiry Report

> Released May 2015

Australia's productivity performance

In 2013-14, Australia's measured productivity increased overall. But growth among industries was uneven, with productivity declining in some sectors.

The latest issue of the Productivity Commission's *Productivity Update* was released in July 2015. The Update provides a snapshot of key nation-wide and industry-specific productivity trends from the most recent release of ABS productivity statistics.

In 2013-14, labour productivity growth in both the Australian economy and the 12-industry market sector (which accounts for 65 per cent of the economy) was slightly above the trend of the last two and half decades. However, growth of multifactor productivity (MFP) remains below the longer-term average. And there were mixed results for MFP growth across industries.

Commission analysis suggests that Mining may be coming out of the 'investment phase' and lifting production – providing an early sign of productivity growth, but with some way to go.

The Financial and insurance services industry has long been a strong source of productivity growth, particularly in terms of multi-factor productivity. But its performance has varied significantly in recent years. *PC Productivity Update* suggests that much of this variability may be attributed to big swings in the Insurance, superannuation and auxiliary services component of the industry.

Investment in new capital has played a key role in lifting Australia's labour productivity by supporting the introduction of new technologies and improving ways of working. The *Update* highlights the importance of efficient investment in public infrastructure – an area in which governments at all levels are not always following processes needed to ensure that the most socially beneficial projects are selected, and that funding or pricing mechanisms align those investments with the preferences of consumers. The *Update* outlines recent work by the Commission aimed at improving the efficiency of public infrastructure investment.

Productivity growth among industries is uneven MFP growth 2013-14

Positive growth	%
Accommodation and food services	+1.1
Retail trade	+1.5
Wholesale trade	+3.1
Information, media and telecommunications	+3.1
Financial and insurance services	+3.3
Arts and recreation	+5.4
Negative growth	
Agriculture, forestry and fishing	-0.1
Mining	-0.1
Manufacturing	-0.3
Construction	-0.7
Transport, postal and warehousing	-3.1
Electricity, gas, water and waste services	-5.4

Efficient capital investment can help boost growth

The key components in efficient public infrastructure investment are:

- Project selection: rigorous cost-benefit analysis
- Development and finance: drawing on the private sector, where opportune
- Funding of ongoing operations: efficient user pricing.

'Smart investment decisions and productive use of the asset will make a big difference in future economic growth. More can be done to improve decision making in the provision and use of public infrastructure.'

Productivity Commission Chairman Peter Harris.

PC Productivity Update 2015

> Released July 2015

Current commissioned projects

19 October 2015

Public Safety Mobile Broadband – *Commissioned Study*

Issues paper April 2015

Draft report September 2015

Final report to Government December 2015

Contact: Carl Toohey 03 9653 2114

Email: psmb@pc.gov.au

www.pc.gov.au/inquiries/current/public-safety-mobile-broadband

Migrant Intake Into Australia – *Public Inquiry*

Issues paper May 2015

Draft report November 2015

Final report to Government March 2016

Contact: Stewart Plain 02 6240 3219

Email: migrant.intake@pc.gov.au

www.pc.gov.au/inquiries/current/migrant-intake

Service Exports – *Commissioned Study*

Issues paper April 2015

Draft report August 2015

Final report to Government December 2015

Contact: Ana Markulev 03 9653 2137

Email: services.exports@pc.gov.au

www.pc.gov.au/inquiries/current/services-exports

Workplace Relations Framework – *Public Inquiry*

Issues papers January 2015

Draft report August 2015

Final report to Government November 2015

Draft report inquiries: ph 02 6240 3200 – ask for Workplace Relations inquiry team

Email: workplace.relations@pc.gov.au

www.pc.gov.au/inquiries/current/workplace-relations

Intellectual Property Arrangements – *Public Inquiry*

Issues paper October 2015

Draft report March 2016

Final report to Government August 2016

Contact: Leo Soames 02 6240 3214

Email: intellectual.property@pc.gov.au

www.pc.gov.au/inquiries/current/intellectual-property

Log on to the Commission's website www.pc.gov.au for full details of all current projects.