

REVIVING HARPER

In 2013, the Australian Government announced that there would be the first comprehensive review of competition policy in Australia in a generation.

A policy field more actively used in Australia than in perhaps any other developed nation to improve the structure of the national economy was about to be reinvigorated.

So said the press release, issued by the then Minister Bruce Billson in conjunction with the then Prime Minister, Tony Abbott.

It said:

The Government will undertake a comprehensive review of competition laws and policy, the first in more than 20 years.

The 'root and branch' review delivers on a key election commitment and will help identify ways to build the economy and promote investment, growth and job creation.

Competition policy has contributed significantly to productivity and price changes in key sectors and in 2005 the Productivity Commission found that the changes resulting from the Hilmer Review increased Australia's GDP by 2.5 per cent.

And crucially:

This review is long overdue and will help identify microeconomic reforms and long-term improvements to build strong foundations for a more productive and competitive 21st century Australian economy.

That was in late 2013.

Two years later, the Harper Review has reported.

The media has since that time occasionally reported sightings of policy consideration, but with attention almost exclusively focused on one sub-section of the Inquiry report, amendments to Section 46 of the *Competition and Consumer Act*.

Because change to this section generates debate between the representatives of small business and the representatives of large business, it is good copy.

And most recently, it has apparently featured in the new Coalition agreement in Canberra.

Meantime, the rest of the Report is muddling along, we guess.

Unfortunately for productivity-enhancing reform in the micro economy, the rest of the report is where the scope for the serious gains lie.

The degree of interest in section 46 as a totem for competition policy reform is actually pretty absurd, when considered in the context of the gains that may come from it.

Indeed, it probably more a totem for how far we have fallen off the pace in national economic reform.

For too long now, under governments of both political persuasions, major reports seem to be left to languish if they no longer suit the immediate political agenda. An issue here or there may selectively be picked off, but the outcome is minimal change despite the initial promise.

Reports like Harper, or closer to home my organisation's report on Justice in Australia, now twelve months old, deserve a serious response, even if it is to reject – but explained with logic and thoughtfulness – what has been proposed.

This seeming lack of willingness to take on reform is of course not new – think of the previous government and the Henry Review.

The issues involved in these reports are not second order. They are social or economic first order matters.

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For Harper, as a successor to Hilmer, there is at this time no public sign of any structured effort to promote the remainder of the Report to the States and Territories.

States and Territories matter because, if the broad sweep of Harper reforms were ever to be implemented, they have to take responsibility for the larger part of it.

Whereas the Hilmer Report was from the outset recognised as the way that competition policy would refashion a Federation's handling of nation-wide economic management in the micro economy. And a Commonwealth-State process was central to it.

COAG has met since the report was finalised.

Harper was noted.

It is rare to recover bureaucratically from the fate of being noted by COAG.

Moreover, if you look up the COAG reform agenda on the official website, you will see commitments from 2009 and 2011.

But nothing of substance since.

Clearly, there is a need for a political revival.

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Of course, it is always possible that these matters are thought to be better conducted – and perhaps are being conducted - away from the gaze of public and media scrutiny.

This is clearly the thinking in international trade policy.

But as that agenda has shown, conducting discussions in such a manner leaves public policy open to serious misrepresentation.

And makes it all the harder when actions suddenly appear in front of an uncomprehending public.

It will now be a challenge to revive a report like Harper, since it was light on the sort of deep specifics that at least allow the Henry Report to still be drawn upon for guidance in tax reform contexts.

The value of Harper in substantial part lay instead in the directions proposed for new change.

These directions for change – applying competition principles-based thinking to health and other social welfare service provision, to road reform and to urban planning – are in need of serious detailed Commonwealth-State working groups with report-back dates and guidance from Ministers and leaders if they are to ever amount to anything.

That level of policy effort is worth it.

There is scope here for material gains to national income, to State and Commonwealth budgets, to quality of life and to economic growth.

Take health, on which Australia presently spends about \$150 billion per annum, the Productivity Commission has estimated gains of up to 20% in health budgets from applying *known* clinical best practice across the board.

More recently, Victoria University research suggests the gains from applying in Australia a *known* program to comprehensively address diabetes (conducted in Finland) would equate to 0.3% of GDP, through increased labour force participation. This is a gain well in excess of any traditional measures to lift labour force participation, and at a time when the imminent burden of an ageing population is becoming much more obvious.

At a more prosaic level, the Queensland Government eliminated a waiting list of 62,000 for public dentistry by offering payment vouchers and allowing recipients to choose private services.

And the NSW Government is considering private provision of ambulance services.

I emphasise these are known reforms, not hypotheticals.

And they are not alone. In a piece of work we published earlier this year, we examined – along with medical practitioners, funders and regulators – 22 efficiency improvements that could be applied by governments or private health funds to known system failures today.

We didn't give an estimate of gains to welfare and fiscal positions of States and Territories, but we could if a government sought such a number, as part of a wider inquiry.

The absence of incentives to apply these known reform options, and the conflicting objectives of potential implementing agents - governments, hospital management, private health funds - is the general feature that defines the list we examined.

If the Harper review resulted in working groups examining how to apply competition principles to implement better consumer choice and information provision in human services, it must surely act as a catalyst for these sort of changes.

The linkage between efficiencies like these and applying competition principles in social policy is not immediately intuitive. The imagery of competition is, after all, like buying fruit at a market, walking up and down the stalls `til you find the best quality at the right price.

But competition reform in social services is not going to be like this.

As the Harper Review itself noted, the models will be multiple, they will differ by service and by ability of participants to understand what is being offered and why.

The fact that some parties – general practitioners, for example – fulfil part of the role of consumer and part of the role of service supplier adds to the general conceptual uncertainty of what exactly is meant by competition.

In practice, the focus will most likely be on improvement to incentives, on reductions in barriers to sharing work or information, and creating much higher awareness of choice and preventative actions; adding up overall to improved consumer choice.

It is not simply about regulating to create fully functioning private markets - if such an anomalous proposition were possible – since these will be sustainable only in limited circumstances.

Thus the fruit market imagery of consumers rating surgeons or haggling with hospitals should be replaced by the imagery of determining which incentives are likely to improve availability of the most effective medicines and procedures; and on those that prevent consumers' own descent into chronic disease; or lift their personal awareness – and that of their medical adviser - of unnecessary procedures and providers with notable records of adverse outcomes.

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The same is true of the other major reform choice in Harper – road reform.

Here too the application of competition principles is all about reflecting consumer choice in investment decisions.

This does – to a degree - now occur in other infrastructure investment areas.

The electricity sector has learned to ignore consumers at its peril, as large price increases for infrastructure investment related to expected demand growth and system reliability proved excessive and demand fell.

Gas markets have exhibited quicker responsiveness to consumer interests.

Even commercial water markets are now developing to some extent, as it proves cheaper to buy-back water than to invest in additional infrastructure.

None of these markets are perfect, or even complete, but it hasn't stopped us using them to lift efficient infrastructure provision and lower the scope for misallocation.

But in roads, we don't bother.

There is effectively no method for the expression of consumer choice in roads.

Instead, we are offered road investment on a basis that does its very best to keep the putative payment system as far divorced from the allocation system as possible.

This will not prove sustainable over time.

Our demand for road infrastructure has exceeded the revenue streams to pay for it for some time, and our Infrastructure Report last year put the numbers to these words. The gap is widening, even as the vehicle kilometres driven per head of population flattens out.

In part, this is because building infrastructure in urban areas is expensive; and that isn't going to change. Blame land prices, as much as any other factor.

And on top of that, the services we expect today in an environment where delivery of on-line purchases has lifted demand for transport services will see urban use of light commercial vehicles continue to grow. And interstate freight too.

The Harper review gave more support to the Productivity Commission's 2014 Report on this subject, which had already received strong support from groups representing road consumers.

The Australian Automobile Association and its affiliated members are keen to fulfil the role of representing consumers in a new allocation system that would link funds for roads to investments favoured by consumers.

In doing so, it would improve planning – possibly the largest single gain from introducing competition principles to road infrastructure – and lift consumer awareness of the need in the longer term to apply direct pricing for some road use.

The technology necessary to apply dynamic pricing in road use is now well-established.

But consumers are not likely to support such shifts in policy until it is first very clear from revised allocation structures that the price paid will influence the infrastructure provided. And that all revenue raised will be returned to the task of improving freight and personal travel.

So our model starts with a proposed revised allocation system, which gives consumers a clear role in determining infrastructure priorities.

And only over time would this group of road transport authorities, State and Federal Ministers and roads and motorists organisations move to address the question of price, and so create the incentives necessary for market-like behaviour.

As in health, the concept of fully private markets for road use is only likely to be observed in future in limited circumstances, of which today a handful of toll roads are the only example.

But the shift in awareness and incentives that comes from involving these organisations and political leaders in *collectively* establishing the planning and priorities will, even in the short term, improve resource allocation and create better incentives for wise investments.

We *know* now, to continue the theme from health, of road-based efficiency reforms with very high net benefit levels - such as electronic access to freeways - that are not being funded.

And we *know* of very large failed projects that refused to accept – indeed in some cases refused to release - the results of their own analysis showing very low levels of net community benefit.

While some say that the road or tunnel is still there despite going broke, this is perverse thinking. Not only does it discourage future private investment – our 2014 Report received many submissions from investors on just this point – but there is an obvious opportunity cost. What else might we have built instead of this failed tunnel?

And it doesn't help the Victorian example of some hundreds of millions of dollars in payment for which there was no asset created.

We are not so wealthy in this country as to see *any* infrastructure project regardless of its poor net benefit as being worthwhile.

Models which apply the kind of thinking set out in Harper do apply internationally, in New Zealand and in Europe.

Unlike in health, road systems are not unique and we would not have to go too far to draw from their experience.

But without a commitment to put this kind of policy shift to active study via a process such as recommended in Harper, there is no other obvious catalyst for change.

In health and other human services, the ageing of the population and the expectations of ever higher quality of care will put such immense budget pressure on governments that some reform effort may be triggered.

Not a comprehensively considered Harper-style application of competition principles. But at least some change.

In roads policy, by comparison, that level of pressure may be some time off. Only once we have reached the limits of public investment, and the tolerance of risk by private investors, and when fuel excise rises in excess of last year's indexation consequently become again a topic of conversation might the idea of empowering road consumers gain traction.

Or we could move earlier, and apply Harper.

Again, the States must be involved. The road networks are their assets. The private investment projects are their projects. They fund large parts of the roads budget. And the consumer organisations – the roads and motoring clubs – are structured on State lines.

The current tax debate shows how difficult it is to focus in public discussion on the question of *why* reform is necessary, when it is so much easier to write about *what* options one party or the other seeks to advocate; and emphasise the losers from that.

This is certainly the case with road reform. The public debate, such as it has been to date, paid no attention to the widening revenue gap and the astonishing paucity of public analysis over large projects.

In the time since our 2014 Report, the policy debate has lost focus now on why price and competition in infrastructure provision matters.

It matters because pricing and allocation reforms are tools for making best use of resources; and carry with them the remarkable inherent positive of giving consumers a chance to do what should happen in all effectively operating markets: determine what service is provided and at what cost.

The models that have to be used are always more complicated and less effective than a fully private market, due to the public interest aspect in the provision of services like health and roads. It cannot and should not be avoided.

As with health, so also with roads: the aim should be reforms that create effective incentives, allow choice – choice in whether a project proceeds, choice in who pays and how they pay - and improve information.

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The Governor of the Reserve Bank last month offered some useful advice on reform and the need for active public communication:

I would like to suggest that ‘reform’ is a term which excites the intellectual elites and the various interest groups (including those who feel they have something to lose from reform) but doesn’t do much to excite the general public. And getting buy-in from them is ultimately critical. To be sure, they have to be led. But they have to be convinced too.

The value of a COAG reform process for competition policy is that it would take the notion of ‘reform’ and necessarily make it part of the national conversation.

Premiers and Prime Ministers would need to lead such a discussion, as per the Governor’s advice.

They can make the case for why we need to address health and aged care and road infrastructure investment in advance of crises or the other traditional drivers of change.

They can explain – and agencies such as mine can provide content to support the view – that it is all about the scope for improved quality of life: better resource allocation that actually meets consumer needs: and greater efficiency in service provision putting less pressure on taxes as the default means of funding big budget items exemplified by health and roads.

Without such a process, the important concepts in Harper otherwise are sure to languish.

And all we will have to show for the successor to Hilmer will be an amendment to section 46.

