Submission to the Economic Regulation Authority Inquiry into Microeconomic Reform in Western Australia

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Mannkal Economic Education Foundation

Mannkal encourages the exchange of ideas and promotes free market thinking through events, conferences, publications and facilitating opportunities – locally, interstate and internationally, for young scholars to understand how free-market principles can improve the lives of all Australians. In 15 years, over 640 young Western Australians have been awarded Mannkal scholarships, with some of our alumnus now moving into senior roles within government and the private sector.

Background

This submission is based on the understanding that sound, free market approaches to public policy offer the best outcomes for all Western Australians. We support this inquiry, particularly with its focus on improving productivity, reducing regulation and policy frameworks which favour markets over government solutions.

In the context of this inquiry, limiting reform recommendations to those that are "easy to implement" unnecessarily restricts some important options. However, we note the parameters of the terms of reference.

While bipartisan political support reduces the barriers to reform, it is acknowledged that reform is difficult to achieve in the contemporary political system. This challenge (and success) of championing economic reform has been recently documented by the Committee for Economic Development of Australia report *Setting Public Policy*. The publication includes a range of essays about the reform process as well as interviews with key State and Federal Leaders who have championed major reform initiatives. While this inquiry is focused on the policy options and not the political process, it is a positive development that economic reform is now discussed in business forums and is of greater interest to the public. We hope that policy options, not the politics remains the focus until the inquiry has been completed.

Mannkal has outlined a general reform agenda in *Project Western Australia: A growth and productivity agenda for the next State Government* (http://goo.gl/93nTsl) which was released on August 12, 2012. In this report, we strongly encouraged cutting red-tape, deregulation and limited government involvement in the economy. There were a number of specific recommendations across a range of portfolios which we will not be repeating. However, we have included a number of copies with this submission so it can be considered in the inquiry.

In our experience, there are many barriers to implementing reform, especially where vested interests have their privileges or rents reduced (or ideally abolished). Mannkal suggests that Public Choice theory could help in identifying roadblocks and obstructions to proposed plans. This is particularly relevant in the context of the public sector payroll which has grown at an unsustainable rate and in many areas is far less efficient than the private sector. Some reforms may involve a reduction of government size and activity. Unfortunately this can result in job losses. The alternative is higher taxes, displacement of private sector activity and a less innovative and dynamic society.

We are extremely supportive of the work of the Economic Regulation Authority (ERA) including this inquiry. Debates over economic policy can only occur when there is high quality, unbiased and credible work such as that produced by the ERA. Ideally this inquiry should mark the beginning of a wider role for the ERA in micro-economic policy discussions within Western Australia.

Recommendation Summary

Mannkal strongly recommends consideration of three key points as part of this inquiry:

1. Emphasize accountability on major projects
2. Normalise peak period and cost reflective pricing
3. Entrench property rights
4. Roadmap for privatisation

1. **Emphasize accountability on major projects**

The Romans tested the integrity of their engineers by requiring them to stand under the bridges they built while the scaffolding was being removed. Today's financial engineers not only will do their utmost not to be identified as having built the bridge but will be as far as possible from it when it is opened to traffic.[1]

The proliferation of major infrastructure projects undertaken by government has meant that any cost blowout in a single project could have major implications for the bottom line of the budget. The State Government has not had the best record in managing major projects and there are now a number of these simultaneously underway.

Ideally, we would encourage greater private investment of infrastructure and a reduction of direct government involvement in major State projects. In some cases, such as the Perth stadium, we would leave this entirely to the private sector, should it see fit to finance, build and run such a facility.

As commitments have already been made, we noted that there will be a period of time when the State has a number of projects on its books. The delivery of these projects would improve if there was a move to institute greater accountability for those managing the projects which could be enhanced by more public disclosure of the ongoing performance of contractors and how this tracks to budget.

The era of mega-projects has resulted in the diffusion of accountability and decision making which has reduced the "skin in the game" for numerous actors in the system. Comments by Sir Arvi Parbo about practices linking the performance and the quality of project management of

[1] Sir Arvi Parbo as quoted by Ron Manners in "The Language of Leadership" (The 2009 Sir Arvi Parbo Oration) Association of Mining & Exploration Companies Mining Congress, Perth, Western Australia May 21, 2009.

Roman engineers shows one way this could be done. While we do not advocate WA project managers standing under bridges, greater incentive-based mechanisms could be considered, as could other public reporting processes.

2. **Normalise peak period and cost reflective pricing**

Roads, electricity and public transport are used every single minute of the day. However, the costs (be it absorbed by government or passed onto consumers) is often set for the peak level of usage. For example, we build our electricity system for the heaviest demand times, generally in summer, even though this infrastructure is only used a couple of days a year. Our roads are built to cope with rush hour and we need as many trains and buses to handle a similar morning and evening rush period. While we do not use a price mechanism to ration these goods, it occurs via other means. Waiting in traffic is one way this occurs.

Cost reflective, time of use pricing would solve some of these problems. We already use this pricing mechanism in public transport for some market segments. Western Australian seniors enjoy free travel between 9.00am-3.30pm on buses and trains. While this has an impact on revenue, it does shift some passenger numbers to off-peak periods which can have a positive impact on reducing capacity requirements (and cost) for peak period. Similar techniques are used by cinemas by pricing weekend evening sessions at a premium and discounting mid-week matinee sessions.

We encourage consideration of the implementation of cost reflective pricing for products and services provided by the State (be it roads, public transport, electricity and water). Accordingly, with current technology allowing almost second by second price differentiation, we call for a shift to peak period pricing for all goods and services in circumstances where curbing peak demand would reduce overall costs. This need not be limited to electricity, road use and public transport, but, as in the case of Perth traffic it would change the rationing mechanism to price rather than congestion. It would also give price sensitive consumers a time when goods and services become cheaper, allowing those on lower incomes to benefit from a discounted price. A similar phenomenon occurred before “Fuel Watch” which flattened the price curve for fuel and reduced the mid-week “cheap petrol” queues.

3. Entrench property rights

There has been a slow erosion of property rights in Western Australia. This has reduced the incentive to invest, created more uncertainty and introduced a culture where government permissions and approvals have the ability to undermine property values.

Of considerable concern is a tendency for the Department of State Development to become involved and further complicate the well-established layers of red tape already extending the timeframe of the land approvals process and adding significantly to the cost to bring much needed land to market. There is a major development of 3,000 home building blocks, south of

Perth, which has met all the specified requirements and hurdles but appears to be still caught in a form of 'limbo'. This is a very strange situation where there is a serious shortage of home building lots and these bureaucratic delays are driving up the lot price, contributing further to the housing affordability crisis in Western Australia.

A Private Property Rights Bill would mean that when existing rights are taken, the intended public benefits are met at public cost rather than that of unlucky individuals. That justice requires adequate prompt compensation is obvious. Furthermore, people will not invest, or will demand higher rates of return, when the benefits of investment may be taken by government fiat. Sovereign risk is restricting investment and thereby State Domestic Product and living standards. We recommend that the government legislates for the protection of property rights.

4. Roadmap to Privatisation

The State Government is far too active in a range of activities which would be best left to the private sector. We encourage a review initially of Government Trading Entities and then parts of service delivery which could be privatised. Rather than rushing to privatisation, we would call for appropriate pricing mechanisms (as outlined in point 3) and then regulatory frameworks (in the case of monopoly assets) to be implemented. After this has occurred, there should be a roadmap for the divestment of State assets.

Appendix 1: Terms of Reference

The Treasurer of Western Australia has given written notice to the ERA to undertake an Inquiry into Microeconomic Reform in Western Australia.

The Terms of Reference for the Inquiry require the ERA to develop the most advantageous package of microeconomic reform measures that the Western Australian Government could implement to improve the efficiency and performance of the Western Australian economy, with a focus on areas of reform that have the potential to achieve the following outcomes:

- improved productivity and flexibility of the Western Australian economy;
- increased choice for consumers and business, leading to net economic benefits to Western Australia;
- increased opportunities for Western Australian businesses to effectively compete for national/international market share; and
- removal or streamlining of unnecessary regulation.

In developing its recommendations, the ERA is required to:

- assess the current level of efficiency of Western Australia's economy, including a comparison with other relevant national and international economies;
- identify those areas in the economy where reform could enhance their contribution to the overall Western Australian economy;
- identify options for improving the economic efficiency of the key areas identified above;
- prioritise key areas of reform based upon their potential impact on overall economic efficiency and future growth; and
- recommend a small number of specific key reforms or sectors that require further investigation by the ERA and/or policy development by the Government.

Appendix 2: ERA Framing Questions for Submissions

1. What sectors of the Western Australian economy are likely to benefit from the implementation of microeconomic reforms?

2. What specific reforms might improve the efficiency, productivity or flexibility of those sectors, and why?

3. What economic and social benefits might those specific reforms have for individuals, businesses and/or the State?

4. What economic and social costs might those specific reforms have for individuals, businesses and/or the State?

5. Are you aware of any additional information that may assist the ERA in assessing the efficiency of the sector in question, or the costs and benefits of the proposed reforms?

6. Are you aware of any examples of other jurisdictions (either in Australia or overseas) where similar reforms have been implemented? How effective were the reforms in those jurisdictions?

7. Is the ERA's proposed use of the Compensation Principle appropriate or is there a more appropriate way to evaluate the net benefit of reforms?

8. Is the ERA's framework for prioritising reform opportunities (that is, likely benefit versus ease of implementation) appropriate?

9. Are there alternative frameworks that would provide a superior assessment?

10. What do you consider to be the most appropriate method for assessing the economic value of a given reform? What are the significant advantages and disadvantages of this approach?

11. Can you provide any additional information that may assist the ERA in understanding microeconomic reform opportunities in Western Australia?

Appendix 3: Contributors

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