



# Senate Inquiry into the Privatisation of State and Territory Assets and New Infrastructure

## Northern Territory Submission

### Executive summary

The Northern Territory is committed to delivering new public infrastructure which increases productivity, promotes economic diversity and supports growth. The Northern Territory acknowledges that not all public assets are suitable for privatisation, particularly where assets are required to provide social as well as economic benefits or where there is potential for market failure without government participation.

However, as economies develop and public policy priorities shift, there are instances where there is no longer a strong justification for direct government ownership or participation in a market. For some assets, the net benefits of continued public ownership may be outweighed by the net benefits of transferring ownership to the private sector and reallocating capital, either into new projects that generate a higher public benefit or into areas that are more closely aligned with core government services or desired policy outcomes.

The Commonwealth has a significant role to play in facilitating the development of new infrastructure, including projects funded through the sale of existing state and territory assets. The Commonwealth is often the primary financial beneficiary of asset privatisations, as tax equivalent payments to state and territory governments are replaced by corporate tax paid by the new private owners to the Commonwealth. Further, the productivity benefits generated from new or improved infrastructure flow through to increased Commonwealth income and corporate tax receipts.

The Northern Territory acknowledges that, regardless of funding sources, evaluating potential projects in a robust and objective manner will help ensure that net public benefits are maximised. In many regions of Australia, public infrastructure projects often have a diverse range of drivers, including factors such as equity of access to essential services and social connectivity, for which there are less well developed evaluation methodologies.

Consideration of the full scope of potential economic and social benefits that flow from new infrastructure projects should form part of the project selection and prioritisation process. In some instances, this may require the use of a range of different assessment methodologies as there may not be a single tool that adequately measures all the potential and less tangible social benefits of a project.

Where it can be clearly demonstrated that privatisation would lead to a better allocation of government resources, and the long term interests of the public can be maintained, the sale of existing assets should be considered as an option for providing the financial resources to fund new public infrastructure. Commonwealth incentive payments can be an appropriate mechanism for aligning the contributions made by each level of government with the benefits that each level of government receives from the provision of new public infrastructure.

## The role of the Commonwealth in working with states and territories to fund nation-building infrastructure

The Commonwealth has a significant role to play in facilitating the development of new infrastructure, including that funded through the privatisation of existing state and territory assets.

Under current federal-state arrangements, the Commonwealth has substantially greater revenue-raising capacity than the states by which to fund infrastructure. Further, the Commonwealth benefits the most from the provision of new public infrastructure, as the productivity benefits generated from improved infrastructure flow primarily to the Commonwealth through higher corporate and income tax receipts.

In addition, the privatisation of state and territory assets results in additional corporate tax revenue for the Commonwealth and lower receipts of tax equivalent payments for the state or territory, representing a further shift in revenue-raising capacity away from states and territories towards the Commonwealth.

The Northern Territory believes that the Commonwealth has the capacity to make contributions towards new infrastructure projects that are funded through the sale of existing state and territory assets. As noted, the Commonwealth will capture most of the benefit of state and territory funded infrastructure through increases in taxation revenues, which will offset initial Commonwealth contributions.

With respect to the size of Commonwealth contributions under the asset recycling initiative, the Territory's position is that a flat rate of 15 per cent is inequitable for small jurisdictions. The costs associated with the privatisation of state and territory assets are not proportionate to the asset value. For relatively small projects, such as those that are likely to occur in less developed or regional and remote areas of Australia, a substantial amount of the Commonwealth contribution will be offset by the transaction costs associated with the privatisation process.

## The economics of incentives to privatise assets

There are benefits associated with public ownership of assets, including revenue streams and the ability to align asset operation with policy objectives. However, these can be offset by factors such as the opportunity cost of the capital employed, the potential for less efficient commercial outcomes arising from operational constraints, and an expectation that a broader set of objectives will be met.

Privatisation of an existing asset can provide governments with the financial flexibility to reallocate capital into areas that generate a higher public return on capital or are better aligned with core government service provision. In some cases, private owners may be able to operate assets more efficiently and better manage operational and financial risks. This can mitigate risks to the public and reduce the conflicts that can arise where government acts as a regulator and is also a market participant.

Potential benefits from privatisation need to be carefully considered against factors including the costs associated with the disposal of the assets and, in some cases, the increased regulatory burden associated with a transfer of ownership from the public to the private sector.

Privatisation of assets should be considered where it can be clearly demonstrated that the net benefits of continued public ownership are outweighed by the net benefits of transferring ownership of an asset to the private sector.

Providing incentives to states and territories to reinvest the proceeds of any appropriate asset sales into the creation of new economic infrastructure is an effective way of expediting national

reform, and promoting cooperation between the Commonwealth and other jurisdictions. Commonwealth incentives can appropriately encourage states and territories to invest in projects that have national significance and benefits in addition to those at the state level.

There is strong economic justification for incentive payments, given that privatisation of existing state and territory assets often results in some, or all, of the benefits being captured by the Commonwealth rather than by the jurisdictions implementing the reforms. Where proceeds from privatisations are reinvested into new infrastructure, the Commonwealth will benefit further as the productivity gains generated by improved infrastructure flow through to increased income and corporate tax receipts.

### Safeguards to ensure privatisations are in the interests of the state or territory, the Commonwealth and the public

The Northern Territory acknowledges that not all public assets are suitable for privatisation. As a jurisdiction with a small but developing economy and a widely dispersed population, some infrastructure is currently provided in the Northern Territory on the basis that it meets social objectives, such as equitable access to essential services, rather than for commercial or economic reasons. However, as economies develop and new markets emerge, there are instances where governments continue to own assets in markets that could operate efficiently without direct government participation, or where there is little alignment with core service delivery objectives.

The Northern Territory is of the view that privatisations should be in the long term interest of the state/territory government, the public and, where possible, the nation as a whole. To this end, the Northern Territory believes a range of appropriate safeguards already exist including legislation and other regulatory arrangements covering measures to support transparent, fair and equitable pricing for consumers, and fair access for market participants. Community service obligations may also be used where there are community or social objectives that would not be achieved from privatised assets if left solely to market forces.

It is noted that privatisations often relate to assets that are monopolistic or oligopolistic in nature, such as power networks, ports and roads, or other services where there is potential for market failure without government involvement. An appropriate regulatory regime for these assets prior to privatisation provides suitable safeguards for infrastructure users and enables the market to be fully informed when valuing the assets.

### The process for evaluating potential projects and for making recommendations about grant payments, including the application of cost-benefit analyses and measurement of productivity and other benefits

The Northern Territory acknowledges that regardless of funding sources, evaluating potential new infrastructure projects in a robust and objective manner will help ensure that public benefits are maximised. This view has been endorsed by the Council of Australian Governments, which has supported work on ways to prioritise projects that improve productivity or unlock economic growth potential, including in regional economies.

As a region that is relatively underdeveloped compared to other jurisdictions, the Northern Territory has a substantial requirement for enabling infrastructure to drive economic growth as well as generate better social outcomes. Public infrastructure projects often have a diverse range of considerations, including factors such as equity of access to essential services and social connectivity, for which there are less well developed evaluation methodologies.

There are a range of alternative project evaluation methodologies available, each with their own advantages and limitations. Cost benefit analysis (CBA) is arguably one useful tool for project evaluation. However, a narrow interpretation of the CBA model has the potential to understate the net public benefits of projects in underdeveloped regions, particularly given the difficulties that exist in measuring the less tangible social benefits of projects in less developed or regional and remote areas.

Consideration of the full scope of potential economic and social benefits that flow from new infrastructure projects should form part of the project selection and prioritisation process. In some instances, this may require the use of a range of assessment methodologies as there may not be a single tool that adequately measures all the potential and less tangible social benefits of a project.

This approach is already evident in the assessment process for road transport projects. The National Guidelines for Transport System Management in Australia (NGTSM) includes a project assessment framework that encourages the use of various techniques to support a CBA, including considering a potential project's non-monetised impacts and applying weights to objectives other than economic efficiency to reflect the relative importance governments place on different objectives.

The NGTSM is currently being updated to provide guidance on tools and techniques that have implications for future approaches to transport project appraisal including wider economic benefits, productivity metrics, and real options analysis. The Northern Territory believes that adopting a similar approach, where a CBA may form one part of a broader range of project assessment techniques, would be beneficial for all infrastructure projects, particularly in regional and remote areas.

### Parliamentary scrutiny

The privatisation of public assets in the Northern Territory typically requires a high level of scrutiny in the Territory parliament. Given the complexity of major transactions, enabling legislation is usually required to be debated and passed by the parliament in order to enable the transfer of ownership of public assets to the private sector.

The Northern Territory contends that current levels of parliamentary scrutiny and other regulatory and legislative safeguards are sufficient to ensure an appropriate balance between ensuring that the long term interests of the public are maintained and allowing sufficient flexibility in achieving the best outcomes for investment in new economic infrastructure.

### Alternative mechanisms for funding infrastructure development in states and territories

The Northern Territory does not intend the privatisation of existing assets to be the only means of funding for new economic infrastructure. While there are a range of alternative funding options for governments, some of the alternative funding models that are being applied elsewhere, such as user charging, may have limited application in smaller jurisdictions.

User charging is attractive for certain projects, particularly in larger jurisdictions, given that states and territories have limited capacity to raise revenue directly to fund infrastructure. This results in greater scope for user charges to be implemented than to use taxation as a funding mechanism for economic infrastructure.

However, in its current stage of economic development, the Northern Territory has limited ability to recover costs by applying user charges to its infrastructure. Instead, the Northern Territory

has a substantial requirement for enabling infrastructure to drive not only economic growth but improved social outcomes.

Additionally, the Commonwealth conducted private sector consultations with banks, credit ratings agencies and private sector infrastructure investors which found there is a shortage of infrastructure projects with sufficient revenue streams, such as user charges, that enable private sector infrastructure investment across Australia. This is particularly the case for projects in the Territory that generally do not have the throughput to make them commercially viable.

### Equity impacts between states and territories arising from Commonwealth incentives for future asset sales

As a developing jurisdiction, the Northern Territory has a much smaller existing asset base than other states and these assets are generally of a much lower value. Further, a large proportion of public assets in the Territory address broader policy issues than similar assets in other jurisdictions, which may add complexity to any privatisation process.

In contrast, some jurisdictions appear to be at a much more advanced stage of preparation for asset sales and have a large pipeline of potential privatisations. It is foreseeable that the existing pipeline of privatisations in the larger jurisdictions may significantly eat into the pool of funds allocated for incentive payments under the asset recycling initiative.

Jurisdictions with a lower level of assets suitable for privatisation are likely to find it difficult to receive a reasonable share of infrastructure funding under the asset recycling initiative. This inequity may be compounded if the pool of funding available for infrastructure outside the asset recycling initiative is reduced. There is also potential for differential treatment in the GST distribution process, with Commonwealth funding under the asset recycling initiative quarantined from assessment, whereas infrastructure funding received outside the initiative may impact on a jurisdiction's GST relativity.

There is also inequity in the size of potential Commonwealth contributions due to the fixed 15 per cent contribution rate. As previously noted, a flat rate of 15 per cent represents a significant contribution for larger projects. However, for relatively small projects (under \$200 million) such as those that are likely to occur in less developed or regional and remote areas of Australia, a substantial amount of the Commonwealth contribution may be offset by transaction costs.